

# Low Pay & Productivity in Greater Manchester

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# Contents

<b>Executive Summary</b>	<b>4</b>
<b>1 Introduction</b>	<b>9</b>
<b>2 Life on Low Pay</b>	<b>15</b>
<b>3 Low Wage Work in Greater Manchester</b>	<b>19</b>
<b>4 Productivity: Will Higher Productivity Reduce Low Pay?</b>	<b>39</b>
<b>5 Skills and Low Pay</b>	<b>51</b>
<b>6 Progression and the Low Wage Labour Market</b>	<b>63</b>
<b>7 Business Models and Employer Perspectives on Pay, Productivity and Skills</b>	<b>69</b>
<b>8 Tax Credits: Supporting the Working Poor</b>	<b>79</b>
<b>9 The National Living Wage, 'Real' Living Wage and Personal Tax Allowance</b>	<b>86</b>
<b>10 Conclusions</b>	<b>92</b>

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# Executive Summary

## Findings

- The extent of low pay is sensitive to the measure used. The number of people in Greater Manchester who earned less than the low pay threshold (defined as two thirds of national median income, or £7.74 an hour in 2014) has increased during the decade leading up to 2014 (from 210,780 in 2004 to 233,500 in 2014). Yet when viewed as a percentage of the Greater Manchester population this figure is stable, with approximately 22.4% earning less than the low paid threshold in 2004 and 22.5% in 2014. More people in Greater Manchester earned less than the low pay threshold than the UK average (21.2%) in 2014.
- However, the low pay threshold is beneath the level of the living wage (£7.85 an hour outside London in 2014; £8.25 an hour since November 2015) – enough to maintain a ‘basic acceptable’ standard of living for an ‘average worker’. The number earning less than a living wage has grown sharply in recent years. For example, in 2013 the proportion of employees earning less than a living wage in Greater Manchester was 21.7%, but by 2014 this had increased to 23.3%<sup>1</sup>. Provisional data released in December 2015 suggests the proportion has risen once more to just over 24%. In some parts of the conurbation more than a third of jobs paid less than the living wage of £7.85 (but this is not the same as the proportion of residents who earn less than a living wage).
- Yet while alternative measures tell subtly different stories on low pay, there has been a decline of living standards overall with Greater Manchester falling faster than the UK. Average hourly pay (for all workers) in 2014 was below that of 2002. In 2004, workers earned £11.62 on average for every hour they worked. By 2014, it was £11. Since 2009 wages have fallen by 10% in Greater Manchester (compared with 9% in the UK). Until 2007 the pay gap between Greater Manchester average wages and the UK was declining, but by 2014 was expanding again.
- The very lowest hourly paid workers in Greater Manchester (at the 10th percentile of the wage distribution) experienced a 7.1% drop in their real pay between 2007 and 2014 (from £7.13 an hour to £6.57 – close to the National Minimum Wage, which at that time was £6.50). But low-paid workers earning rates slightly above the legal pay floor (at the 20th percentile or bottom fifth of the wage distribution) saw a larger 10% fall in their incomes (from £8.26 an hour to £7.44 an hour). This was the same percentage fall as workers earning far higher incomes (at the median and at the 80th percentile). The legal pay floor thus appears to have reduced the post-recessionary pay drop for the very lowest paid, but exposed those just above the pay floor to disproportionately severe pay cuts.
- ‘Low paying sectors’ (defined as sectors in which at least 30% of jobs pay below the low pay threshold) account for 35.7% of all jobs out of Greater Manchester’s total employment of 1.2 million. Some 400,000 people work in these sectors in Greater Manchester. The sectors with the highest incidence of low-paid work are hospitality (76% of jobs are low paying), accommodation (60%), retail (53%), cleaning (53%) and residential care (53%). The largest single low paying sector is retail with 121,700 employees (accounting for 10% of all employees).
- Approximately 130,000 women (27%) and 90,000 men (18%) were low paid in 2014. Some 44% of part-time jobs and 17% of full-time jobs paid less than the low pay threshold. The wages of men have declined most during the recession and after it, leading to a shrinking of the gender pay gap due to male ‘levelling down’. In 2002, average pay for men was £13.48 and for women it was £9.78 an hour (a gap of 38%). By 2014, after adjusting for inflation, men earned an average of £12.92 an hour and women earned £10.37 (a gap of 25%).
- Among young people under 25, well over half (55%) are low paid. In sectors such as accommodation and hospitality between 80% and 90% are low paid. Low pay reduces among people over 30, but is also an issue for workers aged over 50.
- Small firms – especially those with fewer than 20 employees – are far more likely to pay low wages. Small firms are, however, the organisations which generate 90% of jobs.
- There is a lack of high-quality data regarding the wages of self-employed workers on a Greater Manchester level. However, self-employment has grown faster in Greater Manchester than in the UK, but from a lower starting point. In the year to March 2014, the self-employed in Greater Manchester were 13.2% of those in employment (compared to 14.7% in the UK). Between March 2012 and March 2014 this number grew by 19.2% in Greater Manchester compared with 9.1% in the UK. Some estimates suggest 51% of the self-employed are in low wage work<sup>2</sup>.
- Greater Manchester’s post recessionary work culture has become more ‘casual’, as evidenced by the rapid expansion of employment agencies. Employment agencies generated more additional jobs than any other sector between 2009 and 2014 (15,000).

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<sup>1</sup>This figure uses an average of the 10 Greater Manchester districts

<sup>2</sup>See Corlett, A. and Gardiner, L., Low Pay Britain 2015, Resolution Foundation, October 2015

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## Productivity: does it cause low pay?

- Most economists would begin their explanation of low pay from the concept of productivity. Greater Manchester's Gross Value Added (GVA – the standard measure of sub-national output) per job is £39,328 compared with the UK's of £45,093. There are five sectors with productivity of less than £30,000 per job in Greater Manchester and they correspond with the lowest paying sectors with minor exceptions ('other personal services'<sup>3</sup> and textile manufacturing which has relatively high productivity but pays low wages). The five low-productivity sectors are: administrative and support services; human health and social work; arts, entertainment and recreation; accommodation and food services; and retail. The low productivity sectors account for a growing share of jobs. In 2000 they represented 35% of employment. By 2014 the proportion was 40%. Two sectors are responsible for most of this growth. They are administrative and support service work (10.3% of all jobs) and human health and social work activities (12.7% of all jobs).
- The low productivity sectors have grown at a faster rate in Greater Manchester than the UK (by 5.1 percentage points (ppt) compared with 3.6ppt in the UK). However, this growth appears to be at least in part due to additional jobs being created, rather than a downgrading of the existing sectoral base.
- But the conurbation's sectors with the lowest absolute productivity have nevertheless been relatively productive over recent years. Their performance has outpaced average productivity growth between 2000 and 2014 (average annual growth between 2000 and 2014 was just 1.3%). The low productivity sectors exceeded this rate (with the exception of administrative and support services). The worst productivity lags are among the more knowledge intensive (and better paying) sectors such as business and professional services, property, manufacturing and digital work.
- Jobs in the low productivity sectors are typically people-facing, interactive service tasks that are difficult to automate (and to a lesser extent to standardise) in order to drive productivity improvements. They have been productivity laggards throughout recent economic history. The exception may be retail, which has seen greater increases in productivity (spurred by automation, self-service and online innovation) than the others. For these reasons, the chances that productivity growth in most low productivity sectors will reduce the incidence of low pay in the near to medium future are slim.

## How the low paid perceive life at work

- From the perspective of low paid workers, wages are not the main problem they face, but are part of a package of job quality issues. According to interviews for this research, the principal complaints of low paid workers related to insecurity (for example, not knowing when or where the next shift would occur until they received a text message), the chaotic, ad-hoc nature of organizational management, the use of agency staff and inaccurate payments for hours or shifts worked.
- The burdens for low wage workers caused by extended outsourcing and contracting out (for example, the two-tier workforce, organisational turmoil and opaque accountability chains) emerged extremely strongly from interviews. Complex contractual arrangements were associated with 'being unproductive' and 'inefficient' by some interviewees.
- The low paid tend to feel their work situations were 'the way of the world' over which they had limited control. Asked about the possibilities of promotion, the prevailing view was 'I've never asked and I've never been told'. Most claimed to feel a strong attachment to 'doing a good job', but they felt their employers did not share their values and were uninterested in using their skills.
- Cost pressures have driven employers to implement extreme working patterns (for example, in the care sector scheduling rotas for three half hour appointments in each hour) that interviewees felt resulted in low quality services. Some care companies also recruit from economically troubled European Union countries in order to secure graduates to work in the Greater Manchester low wage economy. Carers can receive as little as one week's training before starting client-facing work.

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<sup>3</sup> 'Other personal services' is a very small group (just 7,500 total jobs) which includes hairdressers, beauticians, undertakers, wellbeing therapists, tattooists and pet care workers.

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## The role of skills in Greater Manchester's low paying labour markets

- The low paid tend to have lower qualification levels than others. Those without any qualifications have the lowest average pay rates (£8.07 an hour). Yet pay progression does not always follow skill progression, especially in lower wage work. For example, at level 2, our research confirms other research in finding 'negative returns' at level 2, meaning that those whose highest qualification is level 2 earn less on average than those with lower qualification levels. Meanwhile, some vocational education qualifications are of lower labour market value (in terms of wages paid) than academic qualifications despite theoretical equivalence (for example, those whose highest qualification is a vocational level 3 tend to earn less than those with A levels). There are clear wage returns to an apprenticeship, but again workers with an apprenticeship under their belt tend to earn slightly less than those whose highest qualification is at A level. There are, however, very wide discrepancies lying behind these averages (the results for both intermediate and advanced apprenticeships have been averaged).
- In general, low paid occupations are low skilled occupations. The low-qualified form 61% of the low paid, compared to being 36% of the workforce, although there are many who are low paid and are qualified at level 3 and above. In two low paying occupational groups – elementary occupations and sales and customer service occupations – most workers have a qualification level no higher than GCSEs. Yet there are groups for whom the relationship between skill and pay does not hold. Workers in the caring, leisure and other service occupations are typically medium skilled (nearly two thirds are either educated to degree level, hold other higher education qualifications or have a level 3 qualification) but are low paid.
- In addition, there are different patterns regarding the evolution of pay and skill. High paying, high skilled work grew by 3.3% in the last decade. Medium skilled work has shrunk by 4.7%, but medium paid work has declined by a smaller proportion (2.1%). Meanwhile, low paying work has grown slightly (0.6%), but low skilled work has shrunk by 2.1%. These patterns render popular labour market metaphors such as 'the hourglass model' potentially misleading.
- But the inference should not be drawn that increasing qualification levels will 'solve' low pay. Qualification is a poor proxy for skill – international evidence suggests this is a particular problem in the UK. Employers do not necessarily value the skills the system produces (in wages terms). And there are profound issues on the demand side: poor use of skills, inadequate job design and ongoing problems with over-qualification (about a third of workers in the UK claim they are over-qualified).

- Demand for skills is also constrained by the business models of Greater Manchester employers. Employers in the city region appear to pursue 'low cost, low value, low skill' business models to a greater extent than is the norm in the UK. Some 21% of Greater Manchester businesses have 'low or very low specification product market strategies'. This compares with 18% for the UK as a whole. This low road approach implies lower demand for skills than would be the case if customised, differentiated, innovative (and in turn higher cost) products and services were being marketed by more employers. Some 45% of businesses in the UK have 'high or very high PMS strategies', according to data from the Employer Skills Survey<sup>4</sup>. In Greater Manchester the figure is 42%, although this is higher than other cities such as Sheffield and Liverpool.

## Labour market progression: are the low paid able to move up at work?

- Using Labour Force Survey microdata from 2011-2015, we examined a 15-month period to investigate levels of dynamism in low paid work. The research asked how many manage to move from below the low pay threshold to above it (or who fell back below it) over the time period.
- Just under two thirds of workers (61%) who were low paid at the start were still in low paid work at the end of the period, suggesting levels of upward mobility among the low wage workforce are limited. Those who 'escaped' low pay were 33% (about 53,000 people), while a small minority (6% or 10,000) left to joblessness. However, there was also a significant group (28% or 51,000) who were not low paid at the start of the observation period, but who had moved down into low paying work. Thus the escapers and decliners are close to being in balance: almost as many go down as progress upwards.
- The low paid labour market is more dynamic than the market overall. In Greater Manchester as a whole 7% changed jobs over the 15 month period. Among the low paid it was 12%.
- The majority of 'the stuck' (ie. those in low pay at the start and end of the period) were qualified no higher than level 2, but the data suggested neither training nor qualification attainment helped people advance. In the case of training this was negatively associated with pay – that is, those who received training were more likely to be stuck than those who escaped (fewer of whom received training). This could be due to the nature of the training, such as inductions or health and safety, which are mandatory rather than value adding. Although escapers' qualification levels were higher (above level 2), those whose pay declined also had higher qualification levels. Further research is needed to test this relationship more thoroughly.

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<sup>4</sup> UKCES, 2013, available at [www.gov.uk/government/collections/ukces-employer-skills-survey-2013](http://www.gov.uk/government/collections/ukces-employer-skills-survey-2013)

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## Tax Credits: what are the fiscal costs of low pay and the consequences of budget reforms?

- Greater Manchester has a higher dependence on the tax credit system (working tax credit and child tax credit) than most other comparable city regional areas and the UK as a whole. In 2012/13, 219,000 people received tax credits, with 70% being spent on people in work. Some 10.25% of residents receive tax credits – a higher share than the UK (8.43%) and the average for other metropolitan areas (9.93%).
- Per working age adult, Greater Manchester spends £715.33 compared with a UK average of £573.73. Only the West Midlands has a higher outlay (£802.69).
- In practice, tax credit spending is heavily oriented towards families with children, especially lone parent families which have a particularly high take-up of tax credits. By family type, 14.4% of families with children, 32.8% of lone parent families, and 1.5% of childless households receive tax credits. The self-employed also have a particularly high incidence of tax credit receipt in the city region (14%).
- In 2012/13, Greater Manchester spent £1.556 billion on tax credits, up from £974m in 2005/6 (a real terms increase of 29%; the UK average was 26%). Spending on tax credits rose in real terms between 2005 and 2010, but has been falling in recent years due to tightening eligibility for CTC. By contrast, WTC has been rising but accounts for a lower proportion of tax credit spending overall (in 2012/13, £65.2m WTC went to childless recipients – an increase of 100% on 2005/6; £130.4m CTC went to in work families receiving CTC only – down from £374.6m a decade earlier, a fall of 65%); and £885.4m went to in-work families receiving both types of tax credit, an increase of 34%).
- About three quarters of the recipients of tax credits are on income levels above the minimum wage. In Greater Manchester 24.15% of tax credit recipients receive the NMW (UK average: 21%). Therefore changes in the legal pay floor will not necessarily be sufficient to eliminate the need for in-work support.
- Initial analysis suggests employers 'benefit' from approximately a quarter of tax credit spending (this finding was derived by contrasting the wages of 24 year olds with 25 year olds, 25 being the age for tax credit eligibility. However, importantly, this method does not capture the higher tax credit expenditure among older people who are more likely to have children). Twenty five year olds suffered a statistically significant fall in their wages relative to 24 year olds as tax credits took effect.
- In terms of reducing tax credit dependence, programmes encouraging the labour market participation of lone parents and second earners are likely to have larger monetary effects than moving more workers up to the level of the living wage.
- The 'national living wage' of £7.20 from April 2016 for workers aged over 25 will benefit approximately 13% of Greater Manchester residents who currently earn less than this rate. The target of £9 an hour by 2020 will shift the legal pay floor to about 60% of median earnings – far higher than ever before.

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## Conclusions

- There is no one policy to address the challenges arising from low wage work in the city region. Instead, the report highlights a series of considerations that could shape future responses to low wage work across several different policy fields.
- Business Support: Noting that low pay is not solely a supply side issue, encouraging employers to adopt higher value business models through leadership and management programmes and workforce development (including apprenticeships) may also help to address low pay, albeit over the longer term. Inadequate skills utilization is also an aspect of the low pay debate.
- Skills: The city region enjoys increasing power over skills budgets. Where possible and appropriate, budgetary control can be used to support labour market progression by prioritizing skills interventions that enable individuals to access better paying jobs.
- Living wage: Through acting as a local leader (both as an employer and as a procurer of other goods and services) and by working alongside other prominent employers, the Combined Authority and other public sector organisations can support wider adoption of the living wage.
- Job security: However, wage policies (such as the living wage) are best positioned as part of a package of reforms alongside other initiatives designed to support good employment practices rather than as a 'solution' to low pay in themselves. For example, taking steps to reduce the use of some types of work associated with insecurity (such as zero hours contracts) could also help to support better jobs in a local area.
- Childcare: Supporting the ability of low paid workers to increase their hours or consider other employment opportunities implies that consideration of how to support working parents with childcare should also be part of the platform of policies to mitigate low wage work. National reforms will double the entitlement to free childcare, beginning in 2016. However, Greater Manchester may wish to test the scope for local flexibilities in this area to explore whether childcare provision could be designed in a more targeted and cost effective way so as to focus support on people earning low wages.

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# 1 Introduction

- 1.1** This is the final report of a project examining low pay and productivity in Greater Manchester. The project aimed to offer a comprehensive examination of the causes and nature of low pay, in particular the underlying relationships between productivity, skills and pay.

## Low pay in the UK

- 1.2** The British national business model generates significant numbers of jobs that do not pay well. The Organisation for Economic Co-operation and Development (OECD) ranks its 34 members by the share of low pay jobs (defined as two thirds of the median wage for full-timers): the UK sits among the countries with the highest incidence of low paid work. Some 20.5% of employment was in low wage work in 2012 – unchanged on a decade earlier and more than four percentage points above the OECD average<sup>5</sup>. Only six nations have a higher percentage: the US, Canada, Israel, Ireland, Korea and Poland.
- 1.3** In Greater Manchester, a city region that on a host of economic indicators is poorer, less productive and less skilled than the rest of the UK, between a quarter and a fifth of jobs (22.5% in 2014) paid below the low pay threshold (two thirds of the median for all workers, not just full-timers, or £7.74 an hour). On this measure, low pay in Greater Manchester directly affects 235,000 of the city region's population. Although the conurbation has a better record of job creation than the UK as a whole in recent years, the nature of those jobs is inevitably a major question with profound economic and psychosocial ramifications across health, housing and consumption. Work is neither necessarily a route out of poverty<sup>6</sup> nor a guarantee of improving wellbeing<sup>7</sup>.

## Living Standards: Can the low paid move up?

- 1.4** There has been particularly intense interest in wages since the recession of 2008-9, which has had the effect of throwing living standards into reverse and from which the UK as a whole is still in effective recovery. Since the recession, the British economy has been characterised by strong employment and weak wages, both underpinned by feeble productivity. Unlike previous recessions for which data is available, output per hour worked had not recovered to pre-recession levels over six years later, which led the Bank of England to dub the phenomenon the 'productivity puzzle'<sup>8</sup>. There has been a lengthy period of wage stagnation with above inflation rises only starting to feed into wage packets since late summer 2014. Indeed some argue a semi-conscious labour market bargain has been struck which has traded quantity of jobs for quality of work; in other words, employment has grown because people are cheap. In 2015, median wages in Greater Manchester were below the level they were a decade ago, as we show in chapter two.
- 1.5** UK labour market policy in general, and flagship interventions such as the Work Programme in particular, are oriented towards getting people into work. Whether that work matches well with skills, experience and interests, and whether individuals move easily out of low paying work and up occupational and financial hierarchies tend to be secondary (or third order) questions. Nevertheless, given the scale of low wage work in Britain, interest in labour market progression has increased in recent years. We examine progression from low wage work in detail in chapter six, but in brief, while there clearly are opportunities to move up and out of low pay in Greater Manchester, most (slightly under two thirds) of Greater Manchester's low paid workers did not 'escape' in the 15 month window of observation we examined. Meanwhile, according to the Resolution Foundation, and using a longer time period of a decade, three quarters of the low paid in 2001 were still low paid in 2011<sup>9</sup>.

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<sup>5</sup> OECD statistics, incidence of low paid work. Statistics available at [www.oecd.org/employment/emp/onlineoecdemploymentdatabase.htm](http://www.oecd.org/employment/emp/onlineoecdemploymentdatabase.htm). Given the UK's high proportion of part-timers, a better measure may be two thirds of all employees rather than just full timers

<sup>6</sup> An important psychological milestone in the nation's relationship with work was passed in 2013 with more than half of those in poverty living in a household in which someone worked. See MacInnes, T. et al, Monitoring Poverty and Social Exclusion, Joseph Rowntree Foundation, November 2014

<sup>7</sup> Butterworth, P., Leach, L.S., Strazdins, L., Olesen, S.C., Rodgers, B., Broom, D.H., The Psychosocial Quality of Work Determines Whether Employment has Benefits for Mental Health: Results from a Longitudinal National Household Panel Survey, Occupational and Environmental Medicine, 68:11, 806-812, March, 2011

<sup>8</sup> Bank of England: The UK Productivity Puzzle, 2014

<sup>9</sup> D'Arcy, C., and Hurrell, A., Escape Plan, Understanding Who Progresses from Low Paid Work and Who Gets Stuck, Resolution Foundation, November 2014



**1.6** However, it is a mistake to concentrate exclusively on wage levels without considering the wider dimensions of life on low pay. Low pay is one issue among many inter-related concerns including insecurity, insufficient hours, juggling several jobs at once, child and other caring responsibilities, 'low commitment' employment relationships, and lack of control over when and where work is done. In fact, from the perspective of workers, low pay is seldom named as the primary problem of working life, as we show in chapter one. Wages are one critical element of poor quality work, but there are many others. Although some versions of labour market flexibility are a two-way street, benefitting both employer and employee, there are regular complaints that flexibility generates asymmetrical advantages among employers and employees. Our interviews strongly support this contention.

## How to measure low pay?

**1.7** Is there more 'low pay' today in Greater Manchester than there was, say, a decade ago? The main answer of this report, which focuses on using the low pay threshold as its primary measure, is that there are more low paid in terms of numbers, but not necessarily in terms of as a percentage of the workforce. As noted, the percentage falling below the low pay threshold has been broadly stable. (It is important, though, to be careful to distinguish low paid work from imprecise analogues such as 'low skilled work', 'low productivity work', 'low paying sectors' or 'work of low value', regarding which different trends apply). Yet this answer necessitates discussion of some important technical considerations in how low pay is defined and measured.

**1.8** There is no objective measure of 'low pay'; only research conventions. The low pay threshold of two thirds of median pay is the most commonly used, but as a relative measure of low pay that tracks the median it can generate counterintuitive results that clash with other measures. For example, if median pay falls, the level of low pay will reduce too, all other factors being equal, suggesting there is less low pay when in reality most employees are poorer in general, including the low paid. A recession can thus appear to magically reduce the incidence of low pay. Averages can also have particular impacts on given geographies. For example, judged by the national median Londoners have a relatively insignificant incidence of low pay because wages are generally higher in the capital. But if we use a London earnings median, the incidence of low pay would

be much higher – in fact approximately double that compared with a national median. Nevertheless, although some researchers reject the low pay threshold as an objective measure of low pay, it remains the orthodoxy. In 2014, the low pay threshold, expressed as an hourly rate, was £7.74 an hour. Data in this report generally refers to 2014 unless otherwise stated.

**1.9** An alternative measure of low pay is the number of jobs paid the National Minimum Wage (NMW). Yet the NMW was never intended to be used for this purpose. It was introduced in 1999 as a legal floor to address the kinds of extreme exploitation that saw a factory worker earning £1.22 an hour, a residential home worker £1.66 an hour, and a chip shop worker in Birmingham just 80p an hour<sup>10</sup>. It also aimed to remain affordable for employers and without creating adverse consequences for employment levels or competitiveness. It has had the effect of reducing what might be called 'extreme low pay' (less than half the median), but it has not made significant in-roads into the proportion affected by in-work poverty, despite covering more people in recent years (the Low Pay Commission has calculated approximately 1.6 million people in the UK will be covered by the NMW in April 2016, up from 1.3 million in April 2014<sup>11</sup>). And it was never the intention that the NMW pay enough for all workers to make ends meet, as the living wage seeks to do.

**1.10** Until former Chancellor George Osborne announced plans to create a new legal minimum pay floor for adults over the age of 25 to take effect from April 2016 (confusingly called the 'national living wage', which is distinct from the voluntary or 'real' living wage), the NMW has always languished well below the low pay threshold. In 2014, the NMW of £6.50 was 53% of the median – the highest 'bite' it had ever had – but obviously much less than £7.74 an hour. Yet the NMW is highly susceptible to moves in inflation. The 'real value' of the NMW was worth less in 2013 than it was in 2007<sup>12</sup>.

**1.11** Different rates of the NMW apply for workers aged 18-20, for 16-17 year olds and (since October 2010) for apprentices aged between 16 and 18, and 19 year olds in their first year of an apprenticeship. Neither of the other low pay measures employ different rates for different age groups. This inevitably means that assessing how many people the NMW affects is more complex than measuring the scale of low pay or the impact of a living wage.

<sup>10</sup> Margaret Beckett, National Minimum Wage Bill, Hansard 16th December 1997, available at: <http://hansard.millbanksystems.com/commons/1997/dec/16/national-minimum-wage-bill>

<sup>11</sup> Low Pay Commission, The National Minimum Wage 2015, Low Pay Commission Report 2015, Department of Business, Innovation and Skills, pp 273-274

<sup>12</sup> Low Pay Commission, The National Minimum Wage 2014, Department of Business Innovation and Skills, March 2014

<sup>13</sup> Data available on this link, produced in response to a freedom of information request; <http://www.ons.gov.uk/ons/publications/re-reference-tables.html?edition=tcn%3A77-381435>, accessed 14th October 2015

**1.12** The living wage offers a third option for defining and measuring low pay. Unlike the NMW, the living wage aims explicitly to provide enough from wages for people to make ends meet rather than what is affordable for employers – a ‘basic but acceptable’ standard of living. It also takes no account of age or competence (there is no ‘apprentice living wage’, although rules of thumb apply), or indeed circumstances, such as numbers of dependents. For these reasons the case for a living wage is often advanced in moral terms. According to the Church of England, “it represents the basic principle that people are not commodities and that their lives cannot adapt infinitely in response to market pressures.”<sup>14</sup> If the living wage is used as a measure of low pay, there has been a rise in the incidence of low pay (as a proportion of jobs). According to the ONS, 23.3% of people earned less than the living wage in Greater Manchester in 2014 (£7.85 an hour; £8.25 has been the rate of the living wage, as published by the Living Wage Foundation, since November 2015), up from 21.7% a year earlier. However, it remains a sad fact about low paid work that a living wage may be relatively ‘good’ in low wage sectors. The major supermarket chains have large numbers of staff paid well below the living wage, as do restaurant chains, although some firms in these sectors use their approach to pay to support brand and workforce management strategies (including Pret a Manger which paid £7.70 in 2015 and Aldi which pays the living wage).

**1.13** There are actually two living wages – one calculated by the Greater London Authority for London, which has existed since 2008, and for the rest of the country by the Centre for Research in Social Policy (CRSP) at the University of Loughborough, which has published a living wage rate since 2011. To calculate the London living wage, the GLA calculates the wage required to meet basic living costs for a selection of household types; it then calculates the wage for 11 household types in London to attain income equivalent to 60% of median income (means tested benefits and credits are taken into account when doing so and weightings and adjustments applied). The average of these two wages is called the ‘poverty threshold wage’. The London living wage is the poverty threshold plus a 15% margin to protect against unseen events. To calculate the living wage outside London, the CRSP identifies minimum costs for

nine household types. It then works out the wage that produces enough income after taxes (benefits and tax credits are again taken into account), assuming that all adults are able to work full-time and that they claim what they are entitled to. A weighted average is calculated for the nine household types and any increase is capped at 2% above the increase in average earnings. Revisions to methodologies are currently under review<sup>15</sup>.

**1.14** Because the living wage rate depends heavily on averages, the single figure encompasses very different living costs and needs. The concept has caught on relatively quickly since 2011 and has received backing from some prominent businesses as well as being taken up by some local authorities for their own staff. Supplementing the moral arguments, the case for it is sometimes expressed in terms of a business case. Guy Stallard, Head of Facilities at KPMG, has argued “a living wage makes sense for business because to have an efficient and effective operation, firms require staff who are motivated, rewarded and incentivised to go that extra mile in servicing customer needs.”<sup>16</sup> However, it is notable that many of the businesses which have championed the living wage pride themselves on having ethical brands, do not operate in low wage sectors, and tend to have small numbers of low paid staff<sup>17</sup>, who are typically contracted out. Some surveys suggest large numbers of local authorities have either introduced or are thinking of introducing it<sup>18</sup>. In a novel twist, the London Borough of Brent has become the first to incentivise businesses to pay it with the promise of reductions on business rates.

**1.15** Thus the choice of measurement around low pay can have dramatic consequences for conclusions regarding the extent of low wage work. Assessing low pay is not an exact science. People can still be ‘low paid’ in relative and absolute terms without necessarily meeting measurement criteria.

<sup>14</sup> As reported on the BBC Website, February 23, 2014, see <http://www.bbc.co.uk/news/uk-31581524>

<sup>15</sup> See <http://www.livingwage.org.uk/living-wage-commission>

<sup>16</sup> See, Sweeney, E, Making Work Better, An Agenda for Government, Independent Inquiry Into the World of Work, Smith Institute, 2014, p51

<sup>17</sup> An exception to this was the announcement by the Coop that it intended to pay the living wage.

See <http://www.co-operativecreditunion.coop/blog/news/2015/supporting-the-living-wage-campaign/>

<sup>18</sup> A survey by Unison claims 41% of local authorities in the North West have introduced it.

See <http://www.lgcplus.com/news/third-of-authorities-adopt-living-wage/5067052.article>

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**1.16** Whatever the complexities and merits of the specific measure chosen, there tends to be much greater unity concerning the essential characteristics of the low paid. The low paid tend to be young, female, part-time, temporary, from an ethnic minority, have held a job for less than a year and work in the private sector for a small firm. They are heavily concentrated in industries such as hospitality, retail, social care, cleaning, agency work and ‘people facing’ personal services (eg. hairdressing) and leisure (eg. fitness)<sup>19</sup>. This report pays particular attention to sectors.

## Productivity and skills

**1.17** Most economists argue that pay is influenced by productivity. The low paying sectors of Greater Manchester overlap markedly with the low productivity sectors, as we explore in chapter four, although there are exceptions such as textile manufacturing, which have relatively high productivity, but are among the low paying sectors. Yet many factors affect pay alongside productivity, such as contracting arrangements, gender, firm size and employer business models, as well as considerations of how rewards are distributed. In practice, productivity within the low paying/low productivity sectors is unlikely to leap forward in the short or medium term, as the sectors in question are immemorial productivity laggards. And in any case, their post-recessionary economic performance has been relatively benign. More knowledge intensive sectors such as professional and business services lag national norms by far greater degrees.

**1.18** From a local economic development perspective, skills are at the forefront of the productivity (and pay) debate as an area that local agents and partners can affect (although there are other ‘drivers’ of productivity performance). The relationship between skills, qualifications, productivity and pay is highly complex and prone to over-simplification. The city region has improved its qualification performance in recent years in areas such as the proportion of the workforce qualified to NVQ level 4 and those without qualifications. Yet productivity data does not allow consequences to be easily drawn. As we set out in chapters three and seven, how skills are put to productive use depends in part on business strategy (the demand for skills) and how well qualifications signify ‘skills’ that employers value and can use. The argument that relatively modest demand for skills in Greater Manchester reflects employer choices around business models receives some support in the data. The product

and service market strategies of Greater Manchester employers appear to target the ‘low road’, if not to the same extent as some other comparable regions of the UK.

**1.19** The national policy debate about low pay has been electrified by the decision to introduce a national living wage of £7.20 for over 25 year olds – in effect a new adult premium rate for the NMW – in April 2016. We make some tentative observations of what this may mean for Greater Manchester in chapter nine. Yet pressure to reduce ‘welfare’, in particular tax credits, has also been a feature of the policy discussion about low pay in recent years. Do tax credits subsidise low wage work? Any state support that aims to support people in work will necessarily benefit employers to some degree, but tentative evidence suggests approximately a quarter of the value of tax credits may go to the employer<sup>20</sup>. Yet it is important not to assume the low paid that benefit from different government labour market interventions are always exactly the same people. Only about a quarter of tax credit recipients are on the NMW, for example, with recipients concentrated among lone parents and those with significant childcare responsibilities. Indeed for lone parents the threshold for receipt of tax credits is as high as £32,000 a year. Many more recipients will be on wages at levels slightly above the NMW.

**1.20** Low pay is an issue where the most significant policy responses are located at national level. Indeed, the national living wage implies the government will be directly setting the pay rates of about 13% of the workforce – an eye-opening development in an age of deregulation. However, policy at a city regional level can also have an impact, as we explore in chapter 10.

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<sup>19</sup> See LPC, *ibid*, p44. Hospitality and retail account for 45% of minimum wage jobs, while social care, cleaning and employment agencies for 6 or 7%. Just a third of hairdressing jobs are minimum wage jobs and a quarter of jobs in hospitality.

<sup>20</sup> For more on this, see chapter 8 and the accompanying report, *The Economic and Fiscal Impact of Low Pay in Greater Manchester*, National Institute for Social and Economic Research, July 2015

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## Principal data sources

**1.21** This report uses two principal sources to examine the scale of low pay.

- **The Annual Survey of Hours and Earnings (ASHE):**

Statisticians regard the ASHE as the best source of information on individual earnings in the UK. ASHE is an annual survey of employee jobs based on a 1% sample of all employees on HM Revenue & Customs Pay-As-You-Earn (PAYE) register and provides hourly, weekly and annual earnings measures. This information is reported by employers from their records and covers the individual's gender, age, industry, occupation, home postcode, work postcode and size of firm. However, ASHE does not contain information on ethnicity, qualifications or disability. The publicly available data is further limited when examining specific regional trends; for example, there is no regional breakdown of pay by age, so the very important issue of the earnings of young people in the North West cannot be investigated with this source. Furthermore, the ASHE does not count anybody outside the PAYE system – so the self-employed are excluded and so are temporary workers who are not on official payrolls. These groups are likely to have sizeable volumes of people on low incomes. The ASHE data relates to income distributions rather than employees; since one person could have more than one job, identifying proportions affected by the NMW presents a challenge. Because of such issues, the publicly available data on ASHE probably undercounts the scale of low pay. In addition, it records the information in just one month (April) – which means it could be affected by seasonal trends – and reports it several months later (December). Depending on the analysis, results also have to be adjusted for inflation and methodological changes in data collection<sup>21</sup>.

- **The Labour Force Survey (LFS):** The LFS is a large household survey that is used primarily to measure employment and unemployment, but also asks questions about earnings. A key point of difference with ASHE is that the LFS contains self-reported information from employees rather than employers and it also contains information from the self-employed. The LFS earnings data is generally regarded as less reliable due to a much smaller sample compared to ASHE. Only one out of five survey waves in one quarter will ask questions related to earnings, with some respondents answering these questions without reference to pay documentation, meaning they may not accurately report their weekly, hourly or annual pay. According to the LPC, this is likely to lead to an overestimate of people earning below and up to the NMW and low pay<sup>22</sup>. There is also a tendency to round earnings. ASHE is regarded as containing less measurement error than the LFS, but it may be less representative of the low paid in general.
- To compare incomes over time, it is common practice to take inflation into account to better be able to compare the spending power of individuals at a given point in time. The LPC compares the impact of both the Retail Price Index (RPI) and Consumer Price Index (CPI) to establish pay trends over time. This comparison shows that both indices have similar impacts when used to adjust earnings to identify the most recent spending power of wages over time<sup>23</sup>. The ONS uses the CPI to reflect the change of prices over time and with it peoples' spending power<sup>24</sup>. The analysis within this report adapts the inflation approach of the ONS and uses CPI as the respective measure.

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<sup>21</sup> The CPI measure of inflation is used to adjust ASHE throughout this report

<sup>22</sup> Low Pay Commission Report 2014, [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/288847/The\\_National\\_Minimum\\_Wage\\_LPC\\_Report\\_2014.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/288847/The_National_Minimum_Wage_LPC_Report_2014.pdf), P.22 and 271

<sup>23</sup> Low Pay Commission, Low Pay Commission Report 2014, [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/288847/The\\_National\\_Minimum\\_Wage\\_LPC\\_Report\\_2014.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/288847/The_National_Minimum_Wage_LPC_Report_2014.pdf), p12 and 97.

<sup>24</sup> Office for National Statistics, GDP and the Labour Market - Q4 2014 Quarterly Update, [http://www.ons.gov.uk/ons/dcp171780\\_395985.pdf](http://www.ons.gov.uk/ons/dcp171780_395985.pdf), p.2.

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## Report background and structure

**1.22** This report is based on analysis and research conducted during late 2015 and early 2016 and relies principally on data related to 2014. Chapters one to five report this research. Chapters six, seven and eight are summaries of three reports commissioned as part of the project and published alongside this one. The three documents are:

- *Low Pay and Progression in Greater Manchester* by Paul Bivand of the Centre for Economic and Social Inclusion;
- *Business Models, Skills Utilisation and High Performance Working Practices in Greater Manchester* by Stephen Overell (New Economy);
- *The Economic and Fiscal Impact of Low Pay in Greater Manchester* by Monique Ebell, Max Nathan and Jonathan Portes of the National Institute of Economic and Social Research.

**1.23** New Economy would like to thank and acknowledge the authors from external organisations for their contributions to this project. In addition, New Economy would like to acknowledge the financial support of the Local Response Fund, part of the European Social Fund, for its part in sustaining this project.

**1.24** The report is structured as follows:

- Chapter two examines the findings of our interviews among the low paid. It explores the themes that collectively emerge from the interviews as well as sharing a few individual stories about the nature of life on low pay in Greater Manchester.
- Chapter three contains data concerning the measurement of low pay and the characteristics of the low paid in Greater Manchester. It also looks at the fall in pay among the general population, alongside issues such as the prevalence of zero hours contracts.
- Chapter four examines the interaction of productivity with pay in both theory and practice in Greater Manchester.
- Chapter five sets out findings in respect of skill levels and explores how closely skill and pay relate to each other.

- Chapter six tackles the issue of labour market progression. It seeks to understand how many people gravitate above the low pay threshold in a 15 month period and what their characteristics are.
- Chapter seven concerns business models. To what extent is low pay a reflection of the preferences of employers for low cost, low value product market strategies?
- Chapter eight examines tax credit support to low wage workers in Greater Manchester and the likely impact of the cuts to tax credits.
- Chapter nine analyses the impact of the living wage and personal allowance changes, as well as the future of the 'real' living wage.
- Chapter ten summarises the central themes and findings of the report.

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## 2 Life on Low Pay

- 2.1** This chapter reports the personal experiences of low paid workers regarding the nature of life within Greater Manchester's low wage labour market. The findings are based on thirteen interviews with workers in the care sector, in hospitality and in logistics and no claim to be representative is made; the intention is to give a flavour of the issues rather than to precisely quantify concerns. The chapter begins by extracting the five over-arching themes that emerge from the interviews and then goes on to report the stories of five of the interviewees. In each case, names and a few minor details have been changed in order to preserve anonymity. The interviews used a semi-structured format in which certain questions were standard, but which enabled space to explore the particularities of individual cases.

### Case Studies – Five Key Findings

- 2.2** The central finding of the interviews among low paid workers was that pay was not necessarily the issue that stood out for them as the main 'injustice' that they faced. Instead, their principal complaints typically related either to insecurity (for example, not knowing where or when the next shift would occur until they received a text message) or organizational management problems such as rotas, the use of agency staff, or poor management. This does not mean, of course, that pay is unimportant for the low paid. Most of the interviewees noted, variously, that they struggled to make ends meet; sometimes worked extremely long, but erratic hours; were sometimes forced to borrow money; and one described their situation as 'desperate'. Yet as an initial response to the question of what their principal grievance was about their work, none highlighted pay. The singular issue of pay is inseparable from other aspects of low quality working life that shape the experience of work in the lower paying branches of the labour market.
- 2.3** Across the interviews, outsourcing, contracting and complex, extended supply chains emerged as prominent concerns in the experiences of the low paid. The intricate and mutable relationships between clients and suppliers meant that workers often felt caught in the middle, unsure of whose interests were paramount, or even whom, ultimately, they were working for. A common experience was of the worker wanting to offer a good service, but feeling compromised in their ability to do so by managerial imperatives, such as quick turnarounds or workload pressures, as new contracts were won or under threat of being lost. This finding was especially strong in the care sector which appears to have endemic problems with both service quality and job quality. The

interviewees felt wholly at the mercy of contract changes, with the universal view that if their current employer lost a contract to a new one, it would mean not just upheaval, as new rota patterns and organizational practices were introduced, but deterioration as the new employers would attempt to squeeze more work while trimming the workers' terms and conditions. The 'ridiculous', 'inefficient' or 'bureaucratic' nature of contract outsourcing was also often highlighted. For example, sorting out minor issues involved reference to service level agreements and could involve extended negotiation before simple issues could be resolved (changing a door handle in a care home was cited). Meanwhile, the workers sometimes felt monitored twice over – by their employer and by the employer's client. The presence of employment agencies also looms large in the low wage labour market. Some interviewees worked directly for agencies, but others worked alongside agency workers. This means that in any workplace there were a variety of employment and contractual relationships that were in operation – a common source of perceived injustice.

- 2.4** The perception that low wage workers have little or no power to alter their situations – except through the negative power of exit – was also frequently expressed. 'Take it or leave it' was what they understood to be the attitude of their employers. In exploring the origins of this perception, it was apparent that the traditional means of workplace redress (eg. trade union representation and HR presence, policy and practice) simply did not apply. Meanwhile, employment law was invoked as an abstract theory without much purchase on the real world; what employers were 'supposed to do' and what they 'do' were seen to be different. The possibility of getting promoted was not on the psychological or practical horizon for most, while for a small minority it was something to be avoided because of the additional responsibilities and stresses it would bring with only relatively small compensatory pay increases. "I wouldn't know about that," was a common reply when asked about promotion prospects; another was, "I've never been told and I've never asked." Alongside promotion, the acquisition of skills and qualifications is a traditional route out of low pay. However, the interviewees tended to regard skills issues as more or less irrelevant to their work – and most thought that their employers felt the same way. Although the workers generally took pride in, variously, "working hard", "doing a good job for the client", or "being good at what I do", gaining skills in order to be promoted and attain better pay was not a plan for any of the interviewees. In some cases, employers appear to be deliberately targeting graduates in their recruitment (for example, in the case of graduates

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- recruited abroad to work in the UK care sector), but without using 'graduate skills' in the work. The general attitude was that the worker could resign if they were unhappy; the situation from both managers' and employees' perspectives was regarded as "the way of the world".
- 2.5** In overcoming practical problems at work the challenge of identifying and reaching a manager with sufficient authority to understand and take responsibility for a particular issue was paramount. In turn, local managers also had difficulty reaching regional or head offices to resolve affairs. Although there were perceived to be occasional avenues of redress via sympathetic local managers who were able to argue a worker's case, these local managers had to make the arguments to remote and apparently 'uncaring' regional or national management teams who often over-ruled them. This façade of organisational remoteness from the front line of service activity was a very strong message across all the interviews, which meant the locus of power was often difficult to identify. In the case of complex supply chains (sometimes also involving employment agencies) this distancing mechanism was intensified because as well as a corporate hierarchy there was a commercial hierarchy in operation, in which a client wielded power over the service company. The workers often felt the supply chain meant they were unsure who to approach with questions – each organisation could argue the responsibility lay elsewhere – and felt largely powerless to put right issues in their workplace that they felt were clearly wrong. Some interviewees argued the supply chain was a means of getting the work without having to take responsibility for the worker.
- 2.6** A fourth element of the felt unfairness reported by the interviewees was that they believed they were the relatively frequent victims of underhand employment practices. Most interviewees reported that they had had experiences of not receiving what they regarded as their due for their working patterns. Some alleged their employers were consciously diddling them out of money accrued by additional shifts or hours, or were docking pay unfairly. Others tended to place the fault on informational and payroll systems not keeping up with changing hours of work. For example, overtime worked might not be reflected in a monthly payslip. The need to check and record their work time and pay documents, as well as to be regularly collecting and storing evidence related to work, was cited as a source of additional stress by low paid workers. In practice, they noted that not only were they closely monitored themselves, but that they needed to monitor their employers to ensure they received what they were entitled to. Sometimes the unfairness was not so much underhand, as deliberate. For example, the case of the care worker formally scheduled to fit three half hour visits into each hour cheats both client and worker.
- 2.7** A fifth powerful message that emerges from the interviews is that of the hand-to-mouth, ad hoc, chaotic nature of life in low wage labour markets. 'Traditional' organisational planning and resourcing techniques appear remote from this section of the business world. The workers report a perception akin to chaos among their employers as they prioritise the winning of new work, but struggle to deliver existing commitments, or as they lurch from one staffing crisis to the next. Often, according to interviewees, the employers do not appear to know what labour they need a week ahead. As a result they are almost wholly dependent on over-time, additional shifts, agencies and last-minute requests. The 'wild west' feel of life in the low wage sectors gets passed down organisational hierarchies, so that workers feel personally exposed to the ups and downs of the market. Elsewhere, the workers express a concern to safeguard clients from excessive exposure to the disorganisation they perceive at work. For example, in the care sector, carers criticise the shifting array of different faces clients are exposed to. In extreme cases, they claim there are risks that information about care needs and medication do not get passed on efficiently because of perpetual staffing changes.
- 2.8** The individual case studies offered below are intended to offer a sense of the individual, everyday perspectives of people earning low incomes.
- Brian – delivery driver**
- 2.9** Brian works as a driver for a large delivery company that holds contracts with some of the best known high street retailers. He explains his work position as "self-employed, but not really - we are effectively treated as employees and can't work for anyone else."
- 2.10** He receives 45p for each parcel delivered. On a normal day that means between 80 and 120 parcels are delivered (implying between £36 and £54 a day), but his biggest ever day was 230 parcels (£103.50). In general he reckons he earns "just about the minimum wage. The price for the parcel has not risen in my living memory."
- 2.11** The key reason behind his working patterns is the rapid expansion of e-commerce and in particular the development of next-day deliveries. In some cases, customers can order by 10pm and receive what they have bought the next day. The prospect of free delivery drives a lot of purchases, but that means additional pressure on delivery drivers in Brian's view. "I don't think anyone realises what goes on behind the scenes when they click to confirm their purchase."
- 2.12** He is required to work bank holidays without additional payment and typically works six days a week. If he is unavailable, he is expected to find someone to cover his round rather than the employer – something he feels is grossly unjust and adds to the burden of the work (favours have to be repaid, of course). But one of the

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most time-consuming aspects of the job that carries no additional payments is that he is required to sort his round out before he sets off. "Each worker does this for themselves and you're in a hurry to be off so as not to waste any time, but it's easy to make mistakes that can cost you later."

#### **Carol – domiciliary care worker**

**2.13** Carol works in the care sector visiting clients in their own homes for which she receives the National Minimum Wage and 7p a mile mileage. She has been doing it for three years, but says she is increasingly thinking of leaving because in her view the industry is getting worse. She says that the central frustration in her working life is not the pay, but that her employer schedules three half hour visits in each hour, meaning she is constantly late for each appointment and feels that she is short-changing the clients. The practice is known as 'clipping' and is common in the care sector.

**2.14** None of the visits are long enough which means she says she feels constantly criticised – by the clients, by the clients' families and by her employer when the clients complain to the company. "You always feel you are letting everyone down. You are always late and always apologising. You never get to know people as well as you could do and they have to put up with constantly changing staff."

**2.15** Some clients are elderly and have conditions such as Alzheimer's or learning difficulties and for these clients routine is important. However, due to working patterns getting into a routine is challenging. "There are always one or two who would like to talk to you while they have their breakfast or whatever, but it's not really encouraged."

**2.16** The work typically involves getting people up, getting them toileted and getting them to take their medicine. She says she has nearly left twice, but "likes being able to help people". In one case she became friendly with an elderly lady and used to take extra time with her to do her paperwork while the client did her embroidery. "Everyone knows there are major problems in this industry and I know clients do not always get what they should, but it's really not always the carer's fault."

#### **Harriet – agency-employed kitchen porter**

**2.17** Harriet is employed by a recruitment agency, but works as a kitchen porter in care homes run by a local authority. She is told where she is working for each shift at short notice, but has to cover her own travel expenses. Several times she has finished one eight hour shift and been called to work another shift immediately several miles across town.

**2.18** She says that if she refused one shift due to prior commitments, she would not get any more work that week – "a well-known practice in the agency". She says it has proved very difficult to live with because there was no security and considerable anxiety due to being unsure whether earnings would provide enough to live on due to insufficient shifts.

**2.19** While she was working for the agency a close relative died very young. Harriet called the agency to explain and let them know that she needed to take some time off. In the week after the funeral the agency called four times to ask why she was not at her shift. She explained the situation. On her return she found her tax papers in the post. She had been fired without warning.

**2.20** She says: "The system of agency work creates an army of workers with no employment rights and no security. The argument that it can provide career advancement is so rarely true. Most work is on the minimum wage and low skilled. The only people who benefit from the system are the employers."

#### **Dylan – residential care worker**

**2.21** Dylan works in the care industry for a not-for-profit organisation that provides support for adults with learning disabilities and holds contracts with local authorities and housing associations. When he joined (he says he left a well-paid career in order to find a job that helped people) in January 2012, he was paid £6.75 an hour. After six months his pay rose to £7 an hour and has been at this level ever since (there is no enhanced rate for overtime). His take-home pay is an average of £1,050 a month. He receives enhanced pay for 'waking nights' which is paid at time and a quarter, but nothing extra for working weekends and bank holidays. He is entitled to five weeks holiday.

**2.22** Although he notes pay in the industry is 'poor', his principal grievances relate to a change of employer after the company he joined lost the contract for running the home and a new company took over. According to Dylan, life in the home tends to be highly chaotic and under-managed with it being difficult to sort out everyday issues. "Higher management is very remote and take little interest in the day-to-day running of the home." This remoteness means there have been a series of ad hoc decisions taken without full thought for the consequences. For example, an overtime rate of £8.50 was introduced as a panic measure to staff one shift, but only paid to some workers – causing widespread protests regarding unfairness. In addition, the paperwork is so onerous that time spent with clients is reduced. He cites examples of meetings with psychiatrists that have been attended by one support worker without anyone with managerial authority in attendance. Vulnerable clients can thus have their medication altered without proper consultation.



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**2.23** Getting paid accurately is a problem for him. He has to check his wages every month and “seven times out of ten they are wrong”. The wait can be a month before it is corrected. He cites examples of picking up shifts at short notice that are paid at enhanced rates, but when he received his pay slip the additional shift has only been paid at standard rates. “They do not put anything in writing so it is difficult to prove.”

**2.24** Some staff in the home have NHS terms and conditions, meaning there are issues of the two tier workforce operating in his workplace. These workers are paid around £9.50 per hour as well as time and a third for working after 7pm on weekdays, and time and a half for bank holiday and Sundays. They also get full sick pay and £8.50 for overtime. Their holiday entitlement is eight weeks. However, since the new employers have arrived, these terms have been gradually eroded.

**2.25** Progression within his workplace is unlikely. Asked if there is a possibility of moving up, he says: “I have no idea and don’t think so.”

**2.26** The use of agency staff is, he says, “beyond belief”. The new company is short-staffed, but they continue to take over new care homes and win new work. The short-staffing and chaotic nature of work in the home mean that use of agencies is common to cover shortages. Dylan is dismissive of the agency labour: “90% of agency staff in all honesty are like looking after another client - harsh but true. They have no connection with the clients and have no concern for them because they are just there for a short amount of time. Generally they cause more issues for us to deal with when it would be easier for us to struggle on without them.”

### **Efigenia and Arnaldo – care workers**

**2.27** Efigenia and Arnaldo are a couple who came from Portugal to Sheffield in December 2014. They are both graduates, one in psychology and one in physical education, but struggled to find work at home. “The country [Portugal] does not have any future”, as Arnaldo puts it.

**2.28** They were recruited by an agency and did their interview by Skype. The employer was a care firm operating a local authority care contract in Sheffield. The advert offered a salary of £14,500, paid travelling time between assignments and a car came with the job provided by the company. They received one week’s training and one week shadowing a co-worker before they began.

**2.29** The wage they actually received was £6.70 an hour for a 40 hour week (effectively slightly less than £14,000 a year), but because they were paid in an hourly rate that tended to vary month-to-month, they said it was impossible to work out whether they were being paid

what they were promised. In addition, they found there were no scheduled breaks in what were often very long days. In an extreme example, a working day began at 6.50am and ended at 10.15pm without any break. Instead, they took half hour breaks in the car if they could. Despite these disappointments, they said the house in Sheffield they lived in with a group of other housemates from Estonia, Greece and Spain was pleasant and the rent reasonable.

**2.30** By February 2015, they began to hear rumours that the care company had lost the contract with Sheffield City Council. In March 2015, they were offered a transfer to Manchester to work on other contracts the care company had, and they took up the offer along with their other housemates.

**2.31** Following the move to Manchester, the nature of the work changed. They noticed that clients had to contend with much greater variety in carers. According to Arnaldo, this can cause problems because it is easy to lose track of a patient’s medication. There were also significant gaps in the schedules, but insufficient time to go home, meaning they had to sit around in their cars waiting, often for more than an hour for which they were not paid.

**2.32** There were also significant problems around pay. They were not paid for some shifts they had done in Sheffield before the transfer to Manchester. In addition, they had been offered a £150 bonus if they stayed to the end of the Sheffield contract. This bonus was not honoured, they say. After complaining, they won the agreement to be paid for the shifts they had worked, but the bonus remained outstanding for over a month. It was grudgingly paid once they found the original offer letter.

**2.33** However, the couple noticed that their wages in Manchester had plunged. A typical monthly salary in Sheffield was £1,800 a month. In Manchester it was £690. The reason was that they were not being paid for travel time in Manchester. When they complained, they were told that the contract they had in Sheffield did not apply in Manchester, even though it was the same company they worked for. Indeed, they allege that in one meeting a local manager ripped the contract they had up in front of them, saying that “if they were not happy they could resign.”

**2.34** The policy regarding cars also changed. In Sheffield, each had a car to travel between appointments. In Manchester, they had to share the car. As they lived together, the only way to make it work was for one to work the morning and the other to work the second half of the day. But this meant they could not take on additional hours because of the lack of transport. According to Efigenia: “As soon as you complain, they will remove hours from you. They can give you less hours and try to make you resign.... Only when I got another job then I resigned.” They left the company in May 2015.

## 3 Low Wage Work in Greater Manchester

**3.1** This chapter presents data on low pay in Greater Manchester, paying particular attention to the industrial sectors in which low pay is most prevalent. It is organised in the following way. First, we look at what has happened to average pay in Greater Manchester since the recession. Second, we examine the extent of low pay, using the definitions outlined in the introduction and seeking to pinpoint as precisely as is possible the characteristics of low wage workers. The chapter also covers gender, sector and hours.

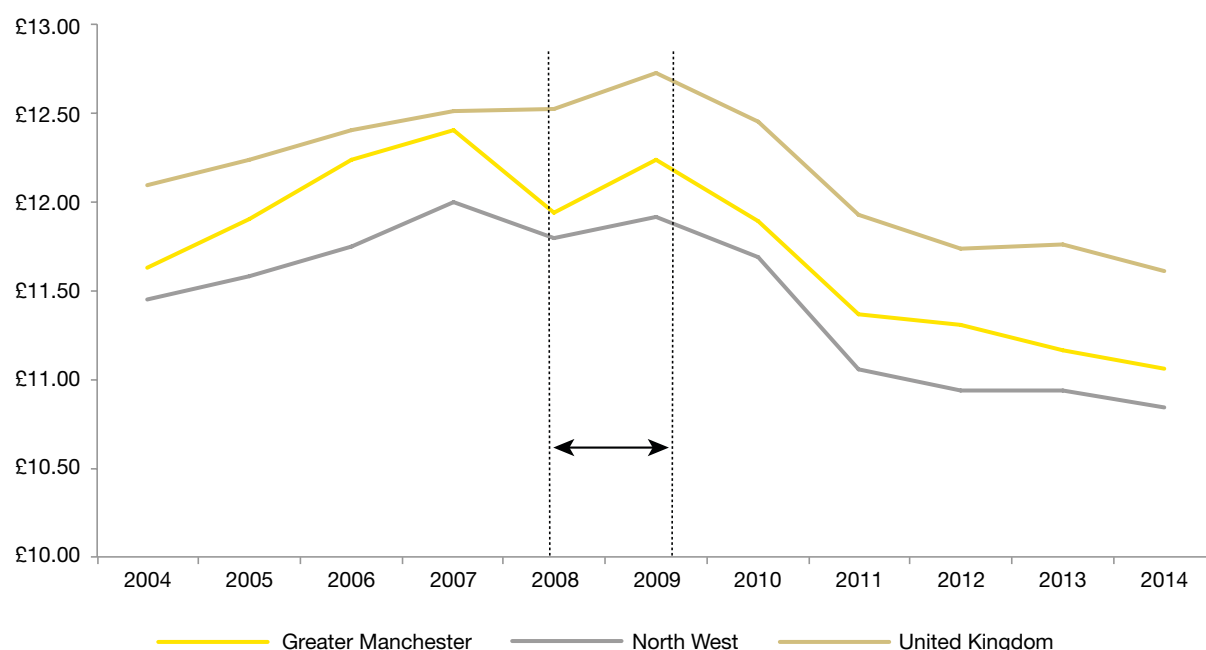
### Economic context

**3.2** As is well known, average pay in Greater Manchester is below the average for the country as a whole: workers earned 55p an hour less in Greater Manchester for each hour they worked than workers in the UK in 2014. However, the critical piece of economic context is the extent to which pay overall – and not just among the low

paid – has been trending downwards once adjustments for inflation over the period are accounted for<sup>25</sup>. In 2004, workers in Greater Manchester earned, on average, £11.62 an hour for their work. A decade later they were earning just over £11<sup>26</sup>. Living standards have thus moved backwards.

**3.3** Wages peaked in 2009, after which they fell by just under 10% in Greater Manchester, compared with a fall of 9% in the UK. Average hourly pay in 2014 was not just below the level it was prior to the recession, but below the level it was in 2002. Labour market data frequently lags other types of economic indicator, but it is clear that in terms of pay, the labour market recovery did not begin until well into 2015. Until 2007, the pay gap between Greater Manchester median earnings and UK median earnings was narrowing rapidly. The recession scotched that development. Hourly pay in Greater Manchester has sunk closer to North West levels.

**Figure 1: Median Pay in Greater Manchester, North West and UK, 2004-2014**

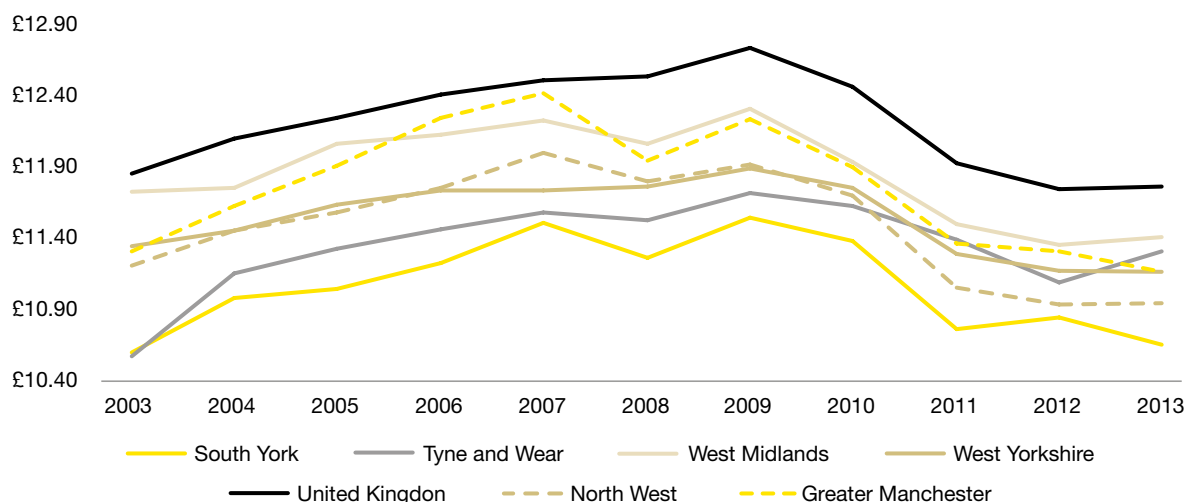


Source: ASHE, adjusted for CPI inflation

<sup>25</sup> The CPI measure of inflation is used to adjust ASHE throughout this report

<sup>26</sup> In general, hourly pay figures are used in this report, but in terms of annual wage rates, according to the ASHE, the gross annual median salary in Greater Manchester workplaces is £21,004 (men: £24,663; women: £17,709); and for Greater Manchester residents the median is £20,743 (men: £24,471; women: £17,332). These figures vary significantly by local authority.

**Figure 2: Median pay compared across different regions, 2004-2014**

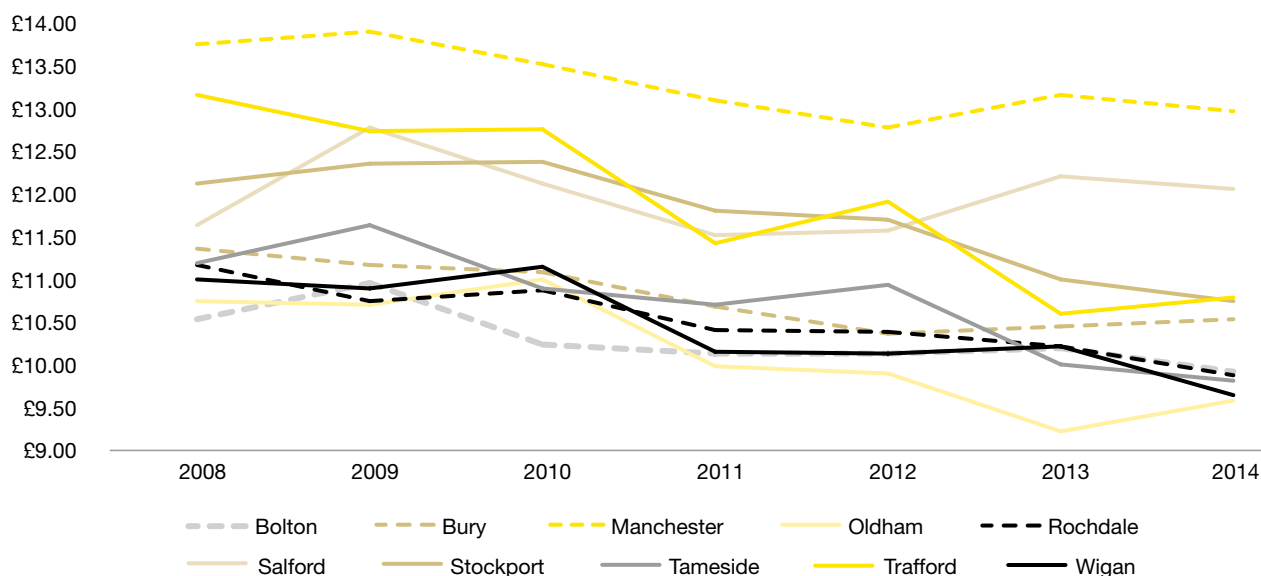


Source: ASHE, adjusted for CPI inflation

**3.4** Yet the story of how the recession has been experienced in Greater Manchester also needs to be considered alongside that of different UK regions. Greater Manchester and the North West have seen less dramatic changes in pay comparing 2004 and 2014 than some other regions. Tyne and Wear and the West Midlands have seen sharper drops in hourly pay. Meanwhile, Tyne and Wear has seen its pay levels back at 2004 levels, but pay is generally among the worst in the country.

**3.5** Looking at the recession and post recessionary period rather than the decade between 2004 and 2014, Trafford has been the district that has seen the sharpest falls in median pay, but the district remains relatively better paid overall. Tameside, Stockport, Rochdale and Oldham have also been among the worst-faring areas in terms of rapid falls in median pay. Salford appears to have had the 'best' recession and recovery, if what is meant by that is that pay in 2014 was above the level it was at in 2008.

**Figure 3: Median Pay across Greater Manchester boroughs – 2008 to 2014**



ASHE adjusted for CPI inflation

## How many low paid jobs are there in Greater Manchester?

**3.6** The table below shows that there were approximately 233,500 jobs that paid below the low pay threshold in 2014, expressed as an hourly pay rate (£7.74 in 2014 <sup>27</sup>). Their number has been growing as the workforce has expanded, but as a percentage of the overall Greater Manchester workforce this proportion has been remarkably stable over the last decade, fluctuating between highs of just under 23% in some of the post-recessionary years, and lows of just over 20% prior to the recession. This picture of outward stability, however, could be an artefact of using the low pay threshold (a relative measure) as the benchmark of low pay. Compared to 2007, there were about 2,800 more jobs that fell below the low pay threshold in 2014, an increase of 1.3%. However, overall job numbers in Greater Manchester have risen by a greater margin over the same time period, adding about 78,000 or 6.8% more employees. The table also demonstrates how, as a relative pay measure, the low pay threshold (two thirds of the median) has fallen as the median has fallen.

**3.7** Among the Greater Manchester districts, Rochdale and Oldham have the highest proportions of low paid jobs. A third of all employees earn less than the low pay threshold in these districts, closely followed by Wigan at 30%.

**Table 1: Numbers and proportions earning up to low pay threshold in Greater Manchester, 2004-2014**

	Low Pay Proportion (GM)	Low Pay Proportion (UK)	Low Pay Threshold	Nr of Jobs (ASHE estimate)	Estimate of Low Pay Jobs in GM
2004	22.4%	21.6%	£8.06	941,000	210,784
2005	21.7%	21.5%	£8.16	1,007,000	218,519
2006	21.7%	21.6%	£8.32	1,004,000	217,868
2007	20.5%	21.2%	£8.34	1,025,000	210,125
2008	22.7%	21.3%	£8.35	1,004,000	227,908
2009	22.4%	21.5%	£8.49	997,000	223,328
2010	22.6%	21.3%	£8.30	995,000	224,870
2011	22.9%	21.9%	£7.99	1,020,000	233,580
2012	21.1%	20.8%	£7.81	991,000	209,101
2013	22.9%	21.6%	£7.86	1,016,000	232,664
2014	22.5%	21.2%	£7.74	1,038,000	233,550

Source: ASHE adjusted for CPI inflation

<sup>27</sup> This estimate of low paid jobs is calculated based on ASHE job estimates, which do not correspond with other official datasets. The ONS warns these are based on the weighted ASHE survey and are rounded to nearest thousand.

**Table 2: Proportions earning up to the low pay threshold by district, 2014**

District	Proportion earning up to Low Pay threshold in 2014
Bolton	28%
Bury	27%
Manchester	17%
Oldham	33%
Rochdale	33%
Salford	17%
Stockport	25%
Tameside	24%
Trafford	25%
Wigan	30%

Source: ASHE 2014

**3.8** While we have chosen to analyse low pay principally through the low pay threshold, an alternative method is to examine a local area by the proportion of jobs falling below the level of the living wage (outside London, the rates of the living wage, as published by the Living Wage Foundation, were £7.65 in 2013, £7.85 in 2014 and £8.25 after November 2015).

**3.9** In 2013, the proportion of employees earning less than a living wage in Greater Manchester was 21.7% (approximately 230,000 jobs). By 2014, this had increased to 23.3% (approximately 252,000 jobs). In some parts of Greater Manchester, the proportion of jobs paying below the living wage is closer to a third.

**3.10** The table below shows the different proportions for the districts of Greater Manchester in 2013 and 2014.

**Table 3: Proportion and number of jobs paying less than a living wage in Greater Manchester, 2013-2014<sup>28</sup>**

District	Proportion of jobs below the living wage 2013	Number of jobs below the living wage 2013	Proportion of jobs below the living wage 2014	Number of jobs below the living wage 2014	% change number of jobs 2013-2014
Bolton	27.4%	27,000	28%	26,000	-4
Bury	21.7%	11,000	26.4%	13,000	18
Manchester	16.4%	53,000	17.2%	57,000	8
Oldham	32.3%	21,000	33.7%	21,000	-
Rochdale	26.7%	14,000	32.6%	18,000	29
Salford	16%	17,000	17.4%	20,000	18
Stockport	20.4%	22,000	23.2%	24,000	9
Tameside	25.6%	15,000	24.7%	16,000	7
Trafford	24.7%	27,000	24.7%	28,000	4
Wigan	26.4%	24,000	30.2%	29,000	21
Greater Manchester	21.7%	231,000	23.3%	252,000	9

<sup>28</sup> Data produced by ONS on New Economy request. Available at <http://www.ons.gov.uk/ons/about-ons/business-transparency/freedom-of-information/what-can-i-request/published-ad-hoc-data/labour/october-2015/index.html> ; separate calculations are available for the parliamentary constituencies of Greater Manchester at Data available at <http://www.ons.gov.uk/ons/about-ons/business-transparency/freedom-of-information/what-can-i-request/published-ad-hoc-data/labour/february-2015/index.html>; accessed 14th October 2015

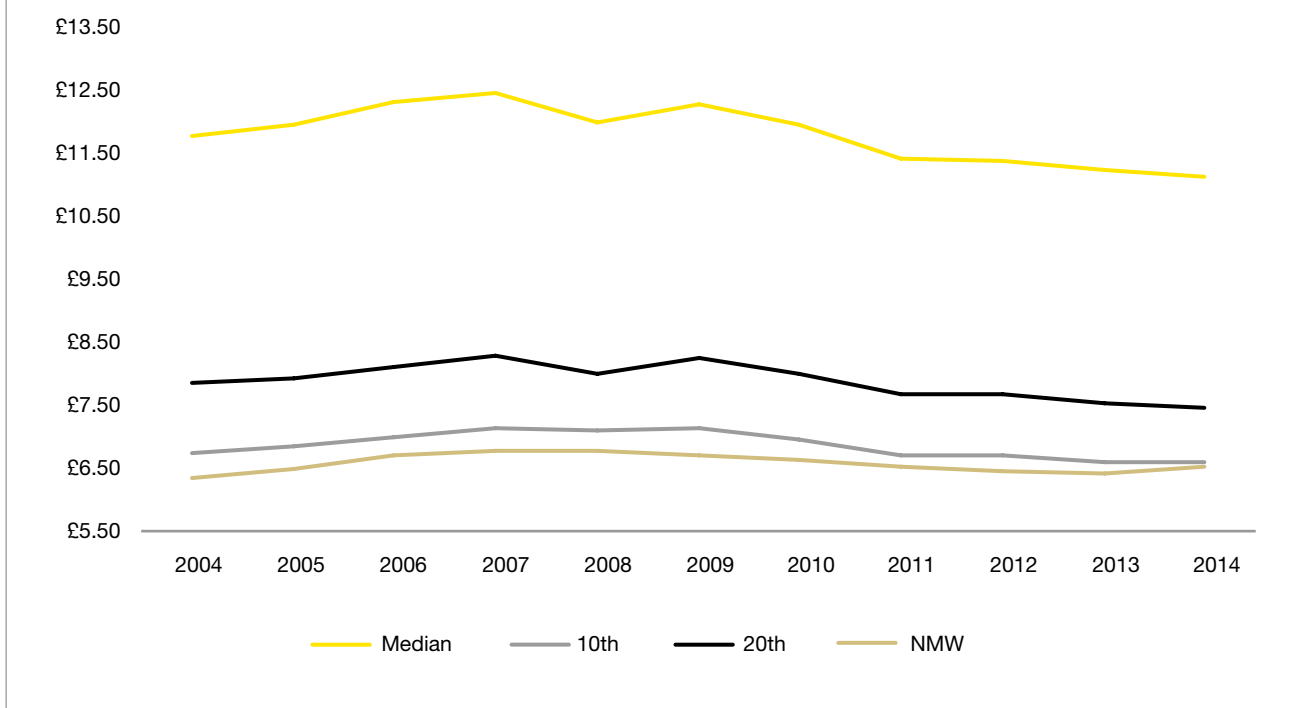
**3.11** This pattern of a rising number of jobs that pay less than the living wage is also replicated in ONS national research<sup>29</sup>. This found that in April 2012, 21% of jobs outside London paid less than the living wage at the time. This rose to 23% in April 2014. (For London, and using a longer time period reflecting the longer existence of the London living wage, the proportion was 13% in 2012 rising to 19% in 2014). Labour demand has returned following the recession especially strongly for low wage, low skill work, the ONS notes. After London (752,000 below-living-wage-jobs), the North West is the English region with the largest number of jobs that pay beneath a living wage (675,000).

### Have the low paid fared the worst from the recession and its after-effects?

**3.12** So what kinds of workers in Greater Manchester experienced the largest falls in wages in the years during and after the recession? In the chart below we show the inflation adjusted wages of workers at the 10th and 20th percentiles and the median, alongside changes in the level of the NMW for the decade between 2004 and

2014, using data from the ASHE. Workers at the 10th percentile – that is, the tenth of workers with the lowest hourly pay – had a drop in income of 2.5% between 2004 and 2014. In 2004, they typically earned £6.74 an hour; their hourly pay peaked in 2007 at £7.13 an hour. Yet by 2014 they were earning £6.57 an hour. At the 20th percentile – the bottom fifth of the labour market – the drop in income was 5.1%. For this group of workers, hourly pay in 2004 was £7.84 an hour. It peaked in 2007 at £8.26 and by 2014 it was £7.44. Turning next to the mid-point of the earnings distribution, the median, workers also witnessed a drop in their income of 5.1%, from £11.70 (2004) rising to £12.41 (2007) before wages fell after the recession to £11.06. During this period the ‘real value’ of the NMW fluctuated but by the end of the period converged with, and became virtually indistinguishable from, the wage levels of the lowest earning 10% of the workforce. In short, the lowest paid tenth are essentially paid the legal minimum.

**3.13 Figure 4: Changes in real earnings between 2004 and 2014 (adjusted for CPI inflation)**



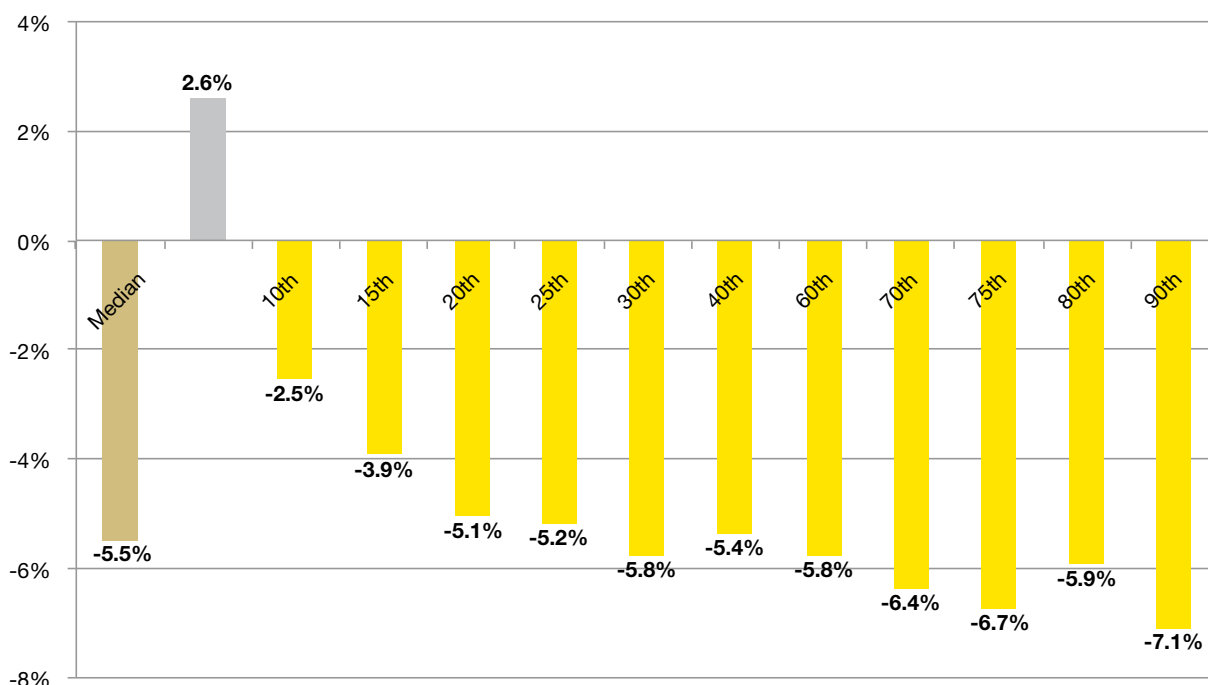
Source: Authors' calculations from ASHE

<sup>29</sup> Office for National Statistics, Estimates of employee jobs paid less than the living wage in London and other parts of the UK, ONS, October 2015

**3.14** Meanwhile, at the 90th percentile (the top decile of the pay distribution), workers saw their wages fall by 7.1% (see the chart below). In practice, falls in income for the lowest paid are likely to be relatively far harder to sustain than drops in income for better paid workers. However, the data does not support the contention that the low paid ‘lost most’ in absolute terms during the decade. A possible explanation for the pattern is that the NMW offered some protection to the very lowest paid workers and those on wage rates just above the legal pay floor, but that those at the 20th percentile actually saw drops in pay that were very similar to those earning substantially more (at the median and above). It is also noteworthy how much those on very modest hourly wages (say, at the 20th percentile or £7.44 in 2014) experienced income drops over the decade that were almost the same in percentage terms as those on much better hourly rates of pay (the 60th percentile or £12.86 in 2014). The chart below shows these changes in more detail. In short, the message is that while the very lowest paid 10% of workers certainly felt the recession in their pay packets, it was workers earning wage rates of between one and two pounds an hour more than the NMW (still low paid, of course) who had the most difficult decade.

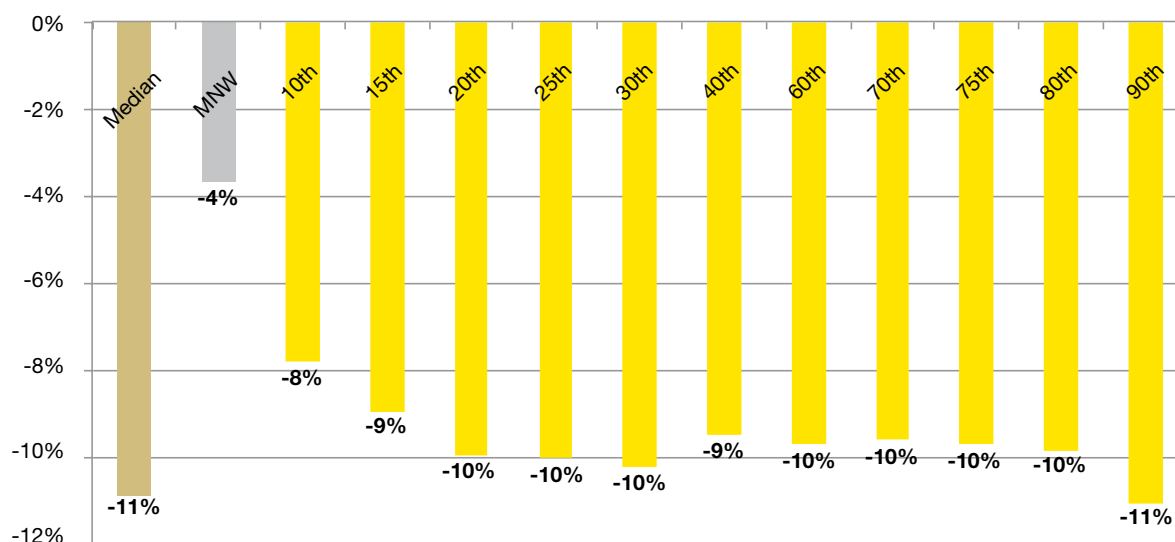
**3.15** The next chart concentrates more directly on the post-recessionary years (2007 was the year before the recession occurred) rather than over the 2004-2014 decade, and so shows much larger drops in pay. This shorter time period shows the extent to which ‘those with the broader shoulders’ did not really take the burden of wage adjustments. People earning what might be seen as extremely good salaries (the 80th percentile or £18.42 when expressed as an hourly wage rate in 2014) saw the same percentage drop (a fall of 10%) in their incomes as those on low wages (the 20th percentile or £7.44 in 2014). Only those at the very top (the 90th percentile) saw larger falls (but only by a minuscule increase in percentage terms). Again, the very lowest paid (the 10th percentile) saw less marked drops in pay, but once more it is critical to remember that a 7.1% fall in pay is likely to be immensely more difficult to bear if you are earning little to begin with. Finally, the chart shows that the real value of the NMW also fell, as policymakers constrained the rate of NMW increases in response to falls in average pay.

**Figure 5: Percentage change in earnings (using ASHE deciles) between 2004-2014 (adjusted for CPI inflation)**



Source: Authors' calculations from ASHE

**Figure 6: Percentage change in hourly pay (using ASHE deciles), 2007-2014 (adjusted for CPI inflation)**



Source: Authors' calculations from ASHE

## The Low Pay Sectors

**3.16** As might be expected, low pay is unevenly distributed across sectors and occupations. Some sectors are seen as generally low paid (cleaning) and others as generally well paying (financial services), but it is important to remember that within any one sector there will be a variety of different jobs at varying levels of seniority and responsibility, so a low paying sector will have well paid jobs within it and vice versa. Thus it is important to combine a sector or industry view of low pay with an occupational view of it too.

**3.17** Over recent years the Low Pay Commission has developed its list of the 'low pay sectors', meaning sectors with 'a high number' of jobs that pay the NMW. These sectors contain 75% of all jobs that pay the NMW, according to the LPC. The sectors also account for 34% of all jobs. Since the recession, jobs in the low paying sectors have grown at a notably faster rate than jobs in the whole economy and this growth spurt has affected how job change is perceived. Comparing 1999 with 2014, jobs in the low pay sectors have grown by 1.4

million or 17.2%. Outside the low pay sectors they grew by 1.9 million or 11.2%<sup>30</sup>. This pattern accounts for the 'increasingly bottom heavy' appearance of the British labour market.

**3.18** In this report we use a different definition of a low pay sector (using the low pay threshold rather than the NMW), but the sectors in question are almost exactly the same as the Low Pay Commission's. We define a low pay sector as a sector where 30% of the jobs fall below the low pay threshold. Meanwhile, an 'extreme low pay sector' is a sector where 50% are below the threshold<sup>31</sup>. Inevitably, given such an approach, this will exclude some sectors with significant numbers of low paid workers. For example, within the 'office administrative, office support and other business support activities sector' some 26% earn wages below the low pay threshold of £7.74 an hour. Some might observe that the sector clearly has a relatively high incidence of low paying work, but due to our definition the sector does not qualify.

<sup>30</sup> Low Pay Commission, National Minimum Wage, 2015, p81

<sup>31</sup> To compare hourly earnings across different sectors, data from ASHE has been broken down to one and two digit SIC codes. Information is not available for Greater Manchester so a north west definition has been used. For a complete list of these SIC codes, see Standard Industrial Classification of Economic Activities, ONS, 2007



**3.19** Of 20 broad sectors, more than one in three (35.7%) conforms to our definition of a low paying sector in Greater Manchester. This compares to the UK as a whole where one in four sectors is a low pay sector. The table shows the sectors with the highest incidence of low pay are hospitality, retail, hotels and cleaning (the latter forming the largest element within the 'services to buildings and landscape activities' sector). Retail is by some measure the largest of the low paying sectors in terms of the total number of employees. Just under 400,000 people work in the low pay sectors.

**3.20** The table also shows location quotients (LQs) in order to understand where Greater Manchester has a higher preponderance of employment in a particular sector relative to the UK. Any LQ above one indicates a higher concentration. As the table demonstrates, Greater Manchester is mostly fairly typical with the only significant exception being the textiles manufacturing sector, and modestly higher concentrations in 'employment activities' (mostly comprised of temporary employment agencies) and 'security and investigation services' (mostly comprised of security guards). Where Greater Manchester does stand out, however, is that almost half of all the low paid fall within the 'extreme low pay sectors', whereas in the UK the proportion is far smaller.

**Table 4: Estimates of low pay by industry, 2014<sup>32</sup>**

	Low pay industries – Greater Manchester (2014)	Proportion of low paid jobs (estimate)	Number of employees by sector	Estimate of low paid jobs	Low paid jobs as a proportion of all jobs in sector	Location quotient 2014 of low paying sectors
Extreme Low Pay Sectors in GM	Food and beverage service activities	76%	60,427	45,924	3.7%	0.87
	Accommodation	60%	12,923	7,754	0.6%	0.67
	Gambling and betting activities	58%	4,773	2,768	0.2%	1.07
	Retail trade, except of motor vehicles and motorcycles	53%	121,711	64,507	5.3%	1.01
	Services to buildings and landscape activities	53%	24,790	13,138	1.1%	0.85
	Residential care activities	53%	28,657	15,188	1.2%	0.91
Low Pay Sectors in Greater Manchester	Other personal service activities	49%	10,577	5,183	0.4%	0.82
	Security and investigation activities	48%	12,899	6,192	0.5%	1.43
	Sports activities and amusement and recreation activities	44%	14,416	6,343	0.5%	0.77
	Social work activities without accommodation	43%	35,501	15,266	1.2%	0.87
	Employment activities	39%	48,538	18,930	1.5%	1.26
	Manufacture of textiles	32%	6,141	1,965	0.2%	2.73
	Wholesale and retail trade and repair of motor vehicles and motorcycles	30%	16,363	4,909	0.4%	0.78
TOTAL Low Pay in GM			397,716	222,446		

Sources: ASHE 2014 for pay estimates and BRES 2014 for sector job estimates

<sup>32</sup> To compare hourly earnings across different sectors, data from ASHE by SIC code was used. Reliable earnings data by industry was only available on a North West level. The assumption has been made that this proportion also holds for Greater Manchester.

**Table 5: Job growth in Greater Manchester and in low paying jobs, 2007-2014**

Overall Low Pay in GM	2007	2014	Change 2007-2014	% Change 2007-2014
All Employees in GM (BRES)	1,148,917	1,226,989	78,072	6.8%
All Low Pay Jobs (ASHE)	217,300	220,056	2,756	1.3%

**3.22** Yet beneath this broad stability, there are some notable exceptions that are worth examining in greater detail, as we show in Table 6 below. The low paying sector that has added the most employees overall is the 'employment activities' sector. Indeed, between 2009 and 2013 it added more jobs than any other sector in Greater Manchester. These roles are employee jobs and not the freelance 'contract for services' that agencies traditionally offer, meaning that the agencies are taking people onto their own books as employees. One possible interpretation of this pattern of job creation could be that employers lacked the confidence to take on permanent staff and so looked to agencies to fill recruitment needs, pending growth and more economic stability. It is impossible to tell from official data which sectors these employees ended up in: there is an almost 50,000 strong shadow workforce deployed across Greater Manchester and the wider North West that is missing from the official industrial record. However, according to the Recruitment and Employment Federation, which represents the interests of employment businesses, there is a concentration in industrial 'blue collar' work, manufacturing, engineering and technical trades, as well secretarial and administrative work<sup>33</sup>.

**3.23** A further explanation for the pattern could be changes to the way employment agencies are regulated that has led more agencies to take staff onto their books as their own staff<sup>34</sup>. The incentive for the clients of the agencies to hire through an agency, rather than recruit directly (aside from the obvious advantage of labour flexibility), is that they are not obliged to offer them the same terms and conditions regarding overtime, holidays and sick pay as their own staff<sup>35</sup>. This is the phenomenon sometimes described as the 'two tier' workforce. The incentive for the client must be sufficiently compelling as a workforce management strategy to accommodate the fees that the agencies need to charge for providing the service.

**3.24** Whatever the underlying explanation, the turn to agency working in response to the post-recessionary environment represents a significant casualization of local employment prospects. Agencies have become a very prominent 'way in' to work, and especially for the low paid.

**3.25** The care sector has not seen quite such dramatic change, but is a far more significant sector in terms of overall employment. It has grown significantly both in terms of overall jobs and in terms of low paying jobs.

<sup>33</sup> Data supplied by the Recruitment and Employment Confederation, available on request

<sup>34</sup> The EU Agency Workers Regulations, which came into force in October 2011, entitles agency workers to the same basic pay and conditions as comparable employees after a 12 week qualifying period. But there is the option of the 'Swedish Derogation', which means they are not entitled to equal treatment, as long as (i) this is explained to them; (ii) they have a permanent contract of employment; and (iii) are paid between assignments. Zero hours contracts do not count as a derogation contract, but contracts for a small number of hours do. Provided an agency worker has this type of 'pay between assignment' (PBA) contract, employers are not obliged to pay them the same as their permanent staff, though other rights (eg holidays) are theoretically covered. The pay between assignments must be either at least 50% of the pay received on the last job or the national minimum wage rate for the hours worked on the last job, whichever is the greater. Data is limited on the use of PBA contracts, but a survey by BIS, which attracted only a small number of responses, suggested about a third of agencies used them and often employed significant numbers of people on them, sometimes employing people through an intermediary umbrella firm of the agency rather than directly.

<sup>35</sup> See Report of the Use of 7 Hours Mobility Worker Agreements by Prime Time Recruitment, Employment, Enterprise and Skills Select Committee, Liverpool City Council, March 2014, available at <http://councillors.liverpool.gov.uk/documents/s139836/low%20hours%20report%20final%20draft.pdf>

**3.26** The sector that has added the most low pay jobs in percentage terms is the security and investigations activities sector, although overall it remains relatively insignificant, accounting for just over 1% of all jobs in Greater Manchester. Unlike the other low pay sectors, it has not seen any changes in the overall number of jobs but a very steep increase in low paying jobs. From 2009 to 2014, it has seen an increase of about 1,675 employees now being paid £7.74 or below an hour, or a 37.1% increase of low paid employees in the sector.

**3.27** By contrast, the single largest of the low paying sectors - retail, which accounts for more than 120,000 jobs - has been shedding labour. The sector has seen falls in total employment and in the number of low paying jobs. Perhaps not unrelated to this pattern, the productivity data we analyse in a later chapter shows that the retail sector stands out among the low paying sector for having grown its productivity in recent years.

**Table 6: Employment change in low paying industries, 2009-2014**

	Greater Manchester - Employment Growth in Low Pay Industries	Change in the overall Number of Jobs (2009-2014)	% Change in the overall Number of Jobs (2009-2014)	Change in Nr. of Low Pay Jobs (2009-2014)	% Change of Low Pay Jobs (2009-2014)
Increase in low pay employees	Employment activities	15,021	44.8%	6,528	52.6%
	Residential care activities	4,210	17.2%	2,720	21.8%
	Security and investigation activities	-5	0.0%	1,675	37.1%
	Food and beverage service activities	1,875	3.2%	1,425	3.2%
	Accommodation	2,484	23.8%	760	10.9%
	Social work activities without accommodation	-1,642	-4.4%	408	2.7%
	Gambling and betting activities	307	6.9%	312	12.7%
Decrease in low pay employees	Manufacture of textiles	-118	-1.9%	-226	-10.3%
	Other personal service activities	-2,749	-20.6%	-814	-13.6%
	Sports activities and amusement and recreation activities	-4,631	-24.3%	-1276	-16.7%
	Retail trade, except of motor vehicles and motorcycles	1,524	1.3%	-5202	-7.5%
	Services to buildings and landscape activities	-8,312	-25.1%	-9371	-41.6%
	Travel agency, tour operator and other reservation service and related activities	N/A	N/A	N/A	N/A

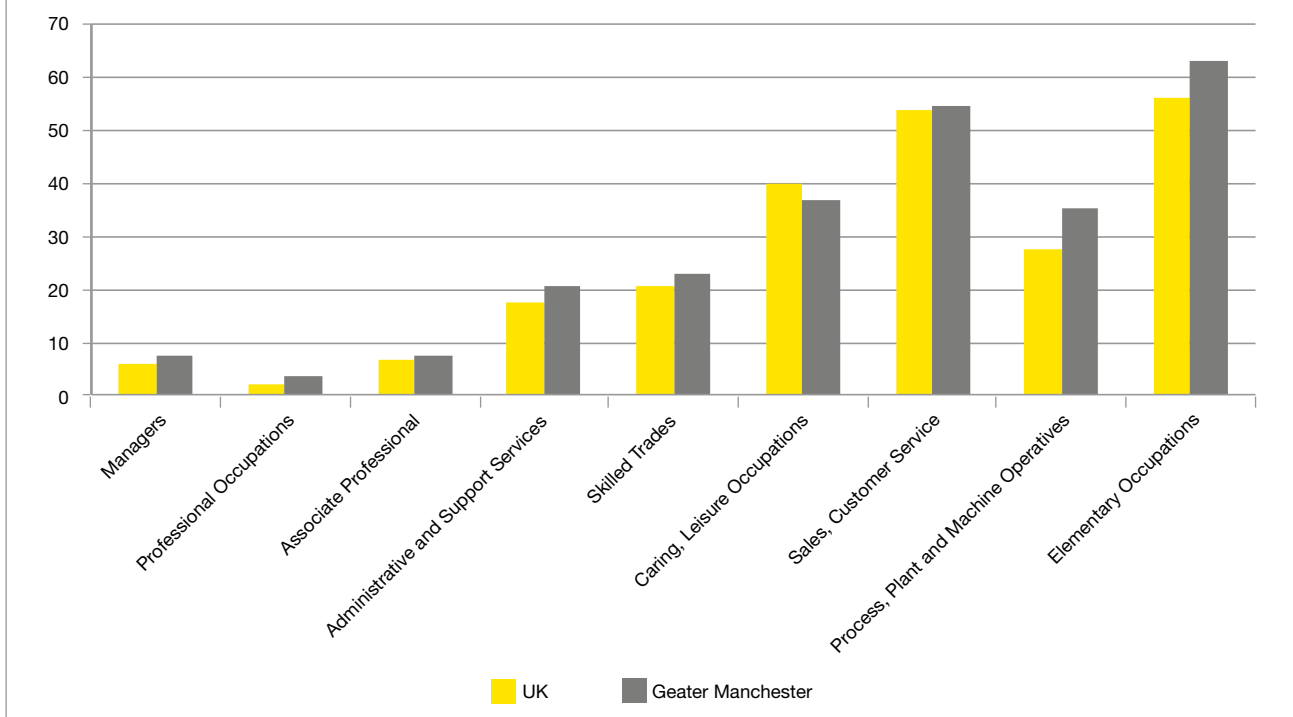
**3.28** The 'national living wage' of £7.20 for workers over 25 from April 2016 is likely to affect the low pay sectors in different ways. But since the increased pay floor is still below the low pay threshold, it will not move employees out of low pay – although if the target of £9 an hour by 2020 is reached the gap between the low pay threshold and legal pay floor will be extremely narrow. However, the make-up and extent of the low pay sectors can be expected to alter significantly because of the new 'national living wage'. The new floor will benefit employees in the low pay sectors disproportionately (and correspondingly disadvantage employers in these sectors), especially in retail, hospitality and care because of the difficulties in transferring the additional costs to consumers<sup>36</sup>. In the case of the care sector, the additional wage costs come at a time when quality of service is rising in importance: health watchdog the National Institute for Clinical Excellence has issued guidance that home visits should be no shorter than thirty minutes, for example<sup>37</sup>. However, it is worth remembering that sectors such as hospitality and retail already have large numbers of younger workers below the age of 25 who will not qualify for the higher rate. Indeed, the national living wage may encourage employers to take on more younger workers who will have lower pay minimum.

## Occupations

**3.29** Occupational categories can be complex and need to be treated carefully. Labels like 'skilled trade' and 'associate professional' cover broad areas, especially when it comes to the underlying concept of 'skill'.

**3.30** However, at the broadest level of analysis, low pay is concentrated in the three groups officially labelled 'elementary trades', 'sales and customer service' and to a slightly lesser extent the 'care and leisure sector'. If the rule of thumb of taking occupations where a third or more of the workforce earn less than the low pay threshold is pursued, then the 'process, plant and machine operatives' sector in Greater Manchester also meets this criteria (but not in the UK as a whole). The occupational groups where low pay is most prevalent are 'elementary occupations' and 'sales, customer service and other service'. The chart below shows which occupational groups have the highest incidence of workers earning less than the low pay threshold.

**Figure 7: Percentage falling below low pay threshold by occupation, UK and GM, 2014**



Source: LFS

<sup>36</sup> D'Arcy, C. and Corlett, A., Taking Up the Floor: Exploring the Impact of the National Living Wage on Employers, Resolution Foundation, September 2015

<sup>37</sup> See: <http://www.bbc.co.uk/news/health-34282423>

**3.31** The table below shows the make-up of Greater Manchester by occupation. The low paying occupations (defined as occupations where at least 30% earn less than the low pay threshold) accounted for 39.3% of all occupations in 2014. This breaks down as: 13.5% elementary occupations; 10.2% sales and customer service occupations; 9.3% care, leisure and other services and the process, plant and machine operatives group accounted for 6.3%.

**3.32 Table 7: Occupations by median hourly pay and proportion of all, 2014**

Broad Occupational Groups (1 digit SOC)	GM Median Hourly Earnings	GB Median Hourly Earnings	Proportion of all Occupations in GM
Elementary Occupations	£7.40	£7.49	13.5%
Sales and Customer Service Occupations	£7.85	£8.10	10.2%
Caring, Leisure and Other Service Occupations	£8.19	£8.47	9.3%
Process, Plant and Machine Operatives	£9.75	£10.16	6.3%
Administrative and Secretarial Occupations	£10.07	£10.77	13.7%
Skilled Trades Occupations	£10.80	£11.07	6.7%
Associate Professional and Technical Occupations	£14.52	£15.50	13.1%
Managers, Directors and Senior Officials	£18.17	£20.45	9.1%
Professional Occupations	£19.48	£20.36	18.1%
<b>TOTAL</b>	<b>£12.36</b>	<b>£13.21</b>	<b>100%</b>

ASHE 2014

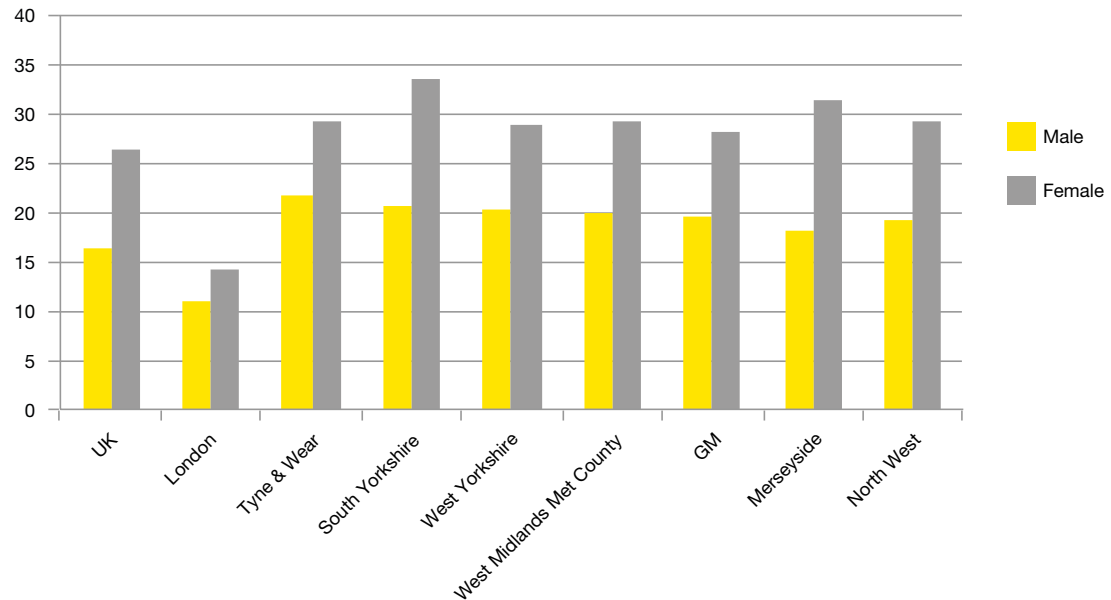
## Gender and low pay

**3.33** As is well known, women earn less than men and low pay affects women to a far greater extent than it does men. For every hour a woman works, men make at least £1.50 more. The origins of the gender pay gap are complex and hotly disputed – occupational segregation, patterns in hours, the division of labour in the home and unequal child-rearing responsibilities, motivation, attitude and psychological qualities such as ‘pushiness’, as well as plain old misogyny are typically invoked as explanations. According to ASHE, 27% of women had hourly pay beneath the low pay threshold, compared with 18% of men in 2014. The LFS has slightly different figures, but confirms the picture: 19.7% for men and 28.3% for women. To put that in context, it means that approximately 130,000 women and about 90,000 men are low paid in Greater Manchester. The chart below shows the percentages falling below the low pay threshold by region in 2014, according to the LFS. South Yorkshire appears to be the extreme case, here, with over a third of the female workforce in low paid work (33.6%).

**3.34** Yet rather more striking is the effect of the recession on the gender pay gap. The pay gap has closed sharply as male hourly pay has fallen, while women’s pay appears to have suffered less. Indeed, because of changes in the median, fewer women today earn below the low pay threshold than they did a decade ago (30%). By contrast, the proportion of men earning less than the low pay threshold has increased by four percentage points during the decade, as male hourly pay has fallen.

**3.35** The effect of the recession has been to accelerate the gradual narrowing of the gap which has been underway for some time. Yet this is not because women’s pay has been increasing relative to men’s, but because men’s pay has been levelling down to women’s. This change is more dramatic in Greater Manchester than in the rest of the UK (shown by the dotted lines in the chart). Yet it is important to remember that while the recession has spurred the trend, the inflation-adjusted gap was shrinking beforehand. For example, in 2002 in the UK, men earned £13.48 on average per hour, compared with the average for women of £9.78 (a gap of 38%). In 2014, men earned £12.92 compared with £10.37 for women (a gap of 25%).

**Figure 8: Percentage of men and women earning below low pay threshold**



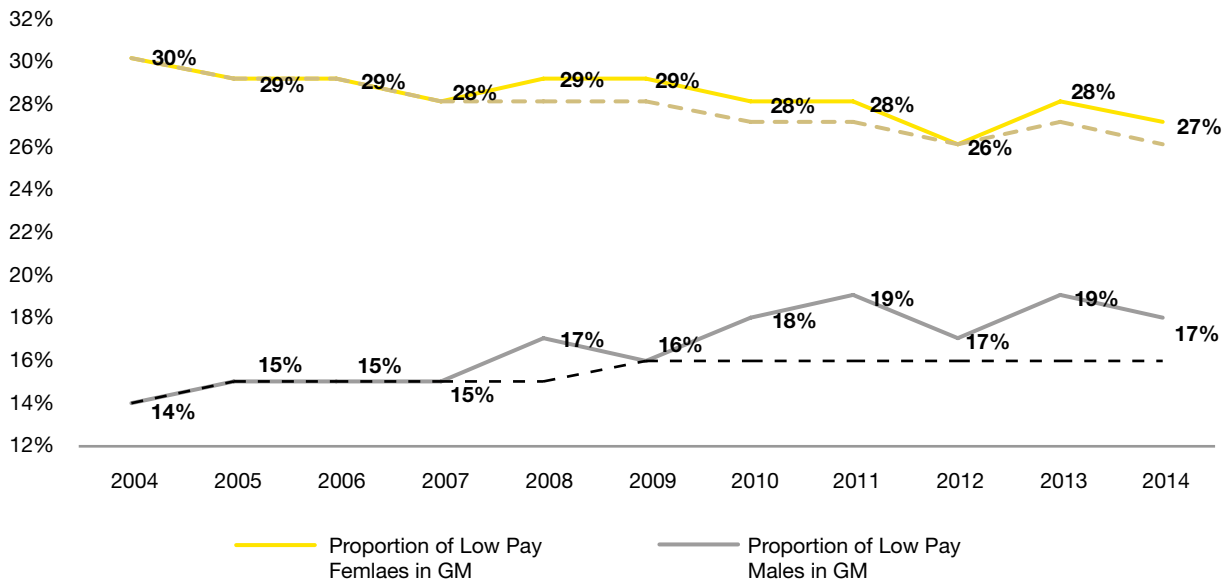
Source: LFS

**3.36** Issues of gender are inseparable from those of working patterns. For a variety of reasons, women are much more likely than men to work part-time and thus to pay a part-time pay penalty. This concept refers to a higher proportion of women than men being limited in the amount of hours they can work due to childcare and other factors. By extension, this tends to limit their choices in what kind of jobs and sectors they work in, reducing their bargaining power when it comes to pay. Nationally, some 42% of women work part-time compared with 12% of men. As the chart below sets out, many more part-timers fall below the low pay threshold than full timers – 44.3% of them, compared with 17.5% of full timers. Part-time means anything less than 30 hours a week, but the average for part-timers is about 19 hours. The vast majority of part-timers are women in Greater Manchester.

**3.37** Perhaps curiously, however, on the specific question of the gender pay gap among part-timers, there is a reverse gender pay gap. Male part-timers earn less than women (although there are far fewer of them). The median hourly pay for male part-timers in Greater Manchester was £7.84 in 2014; for women it was £8.12.

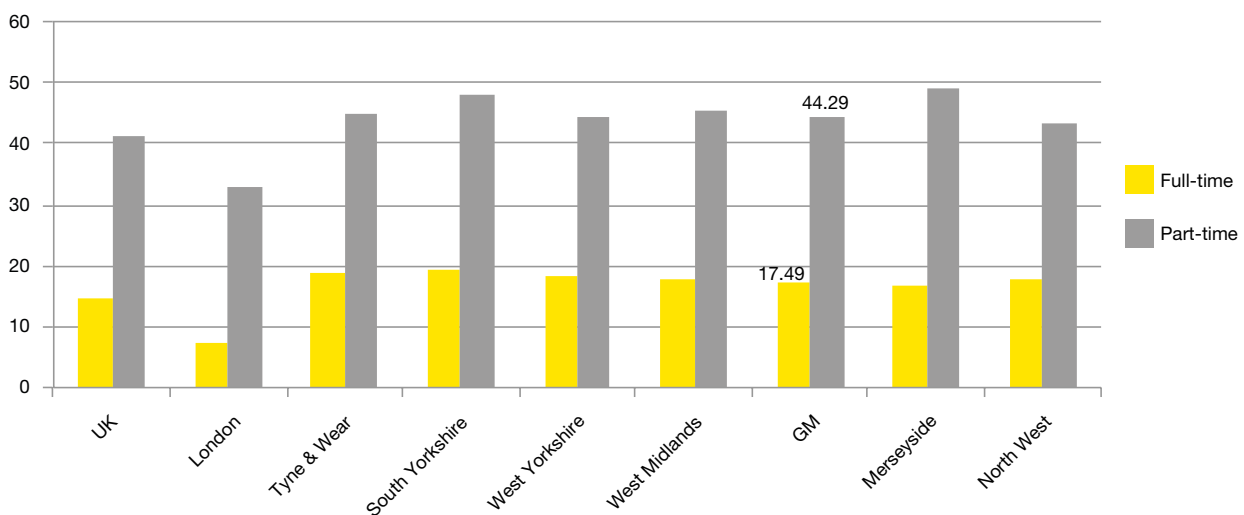
**3.38** The chapter later in this report on skills also considers the gender pay gap in qualifications attainment.

**Figure 9: Gender Pay Gap, 2004-2014**



Source: ASHE 2014

**Figure 10: Percentages of part-timers and full-timers earning below the low pay threshold, 2014**



Source: LFS

## Working time

**3.39** Hours worked in Greater Manchester have been falling in recent years, following a similar trend for the country as a whole. Mancunians worked an hour a week less in 2014 than they did a decade before. In 2004 the average was 33 hours a week in Greater Manchester. By 2014 this had fallen to 32, with a negligible gap between the Greater Manchester norm and the country as a whole.

**3.40** Generally, patterns in working time have been relatively static over the decade. But the recession appears to have triggered falls among the working hours of part-timers, while leaving full-timers' hours relatively untouched. The fall is particularly marked among men who work part-time. Between 2008 and 2015, their working time fell by 8.8%.

**Table 8: Hours worked in Greater Manchester, UK and North West, 2004-2014**

Hours and Gender		2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	Hours difference 2004-2014	% difference 2008-2015
All Hours and gender	GM	33	32.5	32.6	32.8	32.5	32.2	32	31.9	32.1	32.1	32	-1	-3.0%
	UK	33	32.4	32.6	32.6	32.6	32.4	32.3	32.1	32.1	32.1	32.1	-0.9	-2.7%
	NW	33.1	32.4	32.6	32.6	32.6	32.1	32.1	31.9	32	32.1	32.1	-1	-3.0%
All Full-Time	GM	37.5	37.4	37.4	37.6	37.7	37.6	37.5	37.5	37.6	37.6	37.6	0.1	0.3%
	UK	38	37.9	38	37.9	38.1	37.9	37.9	38	37.9	38	38	0	0.0%
	NW	37.8	37.7	37.8	37.8	37.8	37.7	37.8	37.8	37.8	37.9	38	0.2	0.5%
All Part-Time	GM	18.6	18	17.6	18	17.6	17.9	17.5	17.9	17.9	17.7	17.6	-1	-5.4%
	UK	18.2	17.6	17.4	17.5	17.4	17.5	17.4	17.3	17.3	17.4	17.4	-0.8	-4.4%
	NW	18.6	18	17.8	18	17.9	17.7	17.6	17.7	17.8	17.8	17.7	-0.9	-4.8%
Male Full-Time	GM	38.3	38.2	38.2	38.4	38.5	38.4	38.3	38.4	38.4	38.5	38.5	0.2	0.5%
	UK	38.7	38.6	38.7	38.7	38.8	38.6	38.7	38.7	38.6	38.7	38.7	0	0.0%
	NW	38.6	38.4	38.6	38.6	38.6	38.5	38.6	38.6	38.6	38.7	38.8	0.2	0.5%
Male Part Time	GM	18.1	17.3	16.9	17.2	16.7	17.2	16.2	16.8	16.9	16.8	16.5	-1.6	-8.8%
	UK	17.1	16.7	16.5	16.5	16.4	16.6	16.4	16.5	16.6	16.5	16.4	-0.7	-4.1%
	NW	17.3	17.1	16.9	17.4	16.9	17	16.7	16.7	17	16.7	16.7	-0.6	-3.5%
Female Full Time	GM	36.3	36.2	36.2	36.4	36.5	36.4	36.4	36.3	36.5	36.5	36.5	0.2	0.6%
	UK	36.8	36.7	36.8	36.7	36.9	36.8	36.8	36.8	36.8	36.9	37	0.2	0.5%
	NW	36.7	36.5	36.6	36.6	36.7	36.6	36.7	36.6	36.6	36.7	36.8	0.1	0.3%
Female Part Time	GM	18.7	18.2	17.8	18.2	17.9	18.1	18	18.3	18.3	18.1	18	-0.7	-3.7%
	UK	18.5	17.8	17.7	17.7	17.7	17.8	17.7	17.6	17.6	17.7	17.7	-0.8	-4.3%
	NW	18.9	18.2	18	18.1	18.1	17.9	17.9	18.1	18.1	18.1	18	-0.9	-4.8%

Source: ASHE 2014



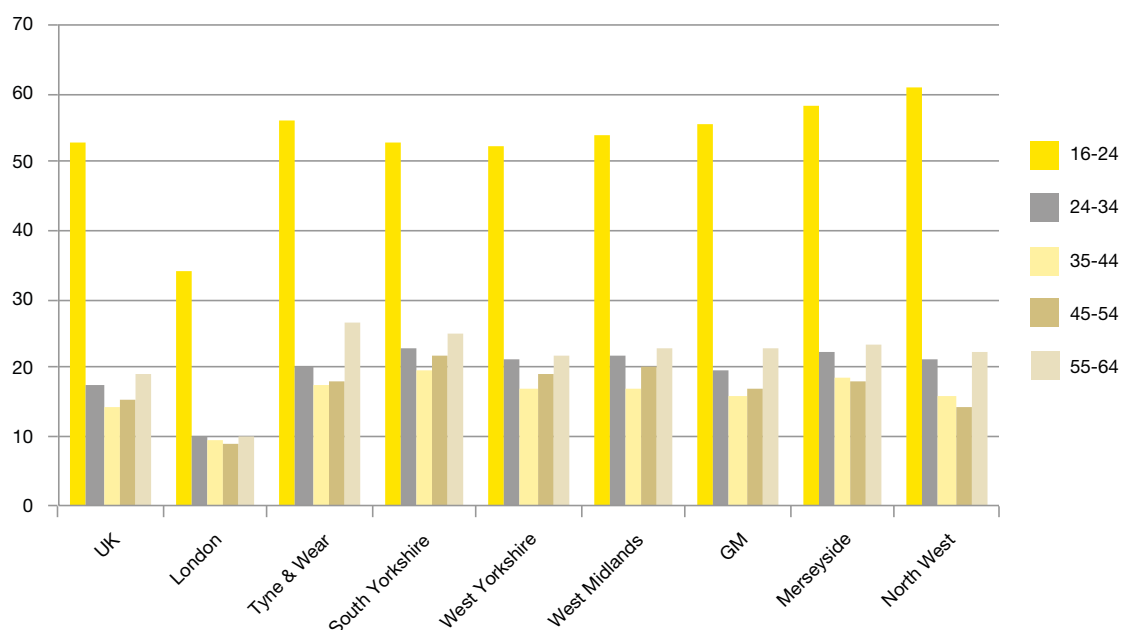
## Age

**3.41** Young and older workers are more likely to be low paid, according to the LFS. Young people under the age of 24 - and especially under the age of 21 - clearly earn the least. In fact, most local young people are low paid: 55% in Greater Manchester and 58% in the North West. The numbers of low paid begin to rise again after people reach their late fifties.

**3.42** When we switch data source to compare against the ASHE, the findings regarding age are even more pronounced. Some 78% of people under the age of 21 earn less than the low pay threshold. This is mainly influenced by much lower National Minimum Wage rates for young people under 21 years<sup>38</sup>. But 22 to 29 year olds also show relatively lower pay compared to employees who are older.

**3.43** The table below shows the data on low pay by age across the low pay sectors. In all the low pay sectors there is a marked tendency to pay the young less – and in some sectors, 80 - 90% are earning below the low pay threshold before their 25th birthday. Low pay clearly persists well into an individual's twenties, and tends to improve a little during their thirties and forties. Across some of the low pay sectors, including retail, people in their fifties tend to have worse pay than their younger peers. This trend is much more marked among the over sixties.

**Figure 11: Proportions earning less than the low pay threshold by age**



Source: LFS, 2014

<sup>38</sup> National Minimum Wage levels in 2014:

- £2.68 per hour (apprentices aged 16 to 18 and those aged 19 or over who are in their first year);
- £3.72 per hour (employees aged 16-17);
- £5.03 per hour (employees aged 18-20);
- £6.31 per hour (employees aged 21 and over).

**Table 9: Proportion of workers earning less than low pay threshold by age and sector, UK, 2014**

	SIC	18-21 years old	22-29 years old	30-39 years old	40-49 years old	50-59 years old	60+ years old
Manufacture of textiles	13		55%	29%	25%	28%	32%
Wholesale and retail trade and repair of motor vehicles and motorcycles	45	70%	35%	19%	16%	24%	42%
Retail trade, except of motor vehicles and motorcycles	47	78%	51%	36%	42%	50%	57%
Accommodation	55	> 80%	65%	47%	43%	54%	55%
Food and beverage service activities	56	> 90%	70%	56%	62%	61%	65%
Employment Activities	78	68%	42%	35%	33%	33%	25%
Services to buildings and landscape activities	81	74%	53%	51%	52%	55%	61%
Residential care activities	87	77%	61%	42%	42%	42%	36%
Social work activities without accommodation	88	73%	45%	29%	27%	27%	27%
Gambling and betting activities	92	> 75%	47%	29%	29%	41%	50%
Sports activities and amusement and recreation activities	93	73%	37%	23%	24%	25%	35%
Other personal service activities	96	> 80%	52%	35%	37%	35%	30%

Source: ASHE 2014

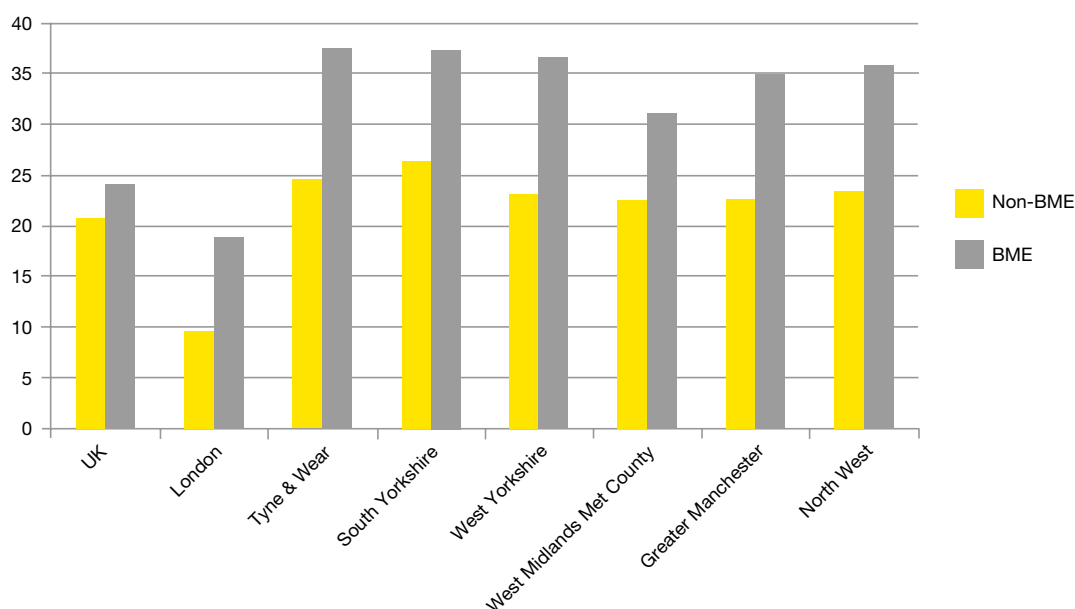
**3.44** Is this a problem? Arguably, provided young people have the opportunity to progress, starting a working life on a low wage is to some extent the natural order of things. Conversely, there are arguments that young people lack a voice at work and can be the victims of sharp employment practices and are just entitled to decent wages as any other worker. For example, zero hours contracts are known to be a particular feature of work among young people. The issue of progression is analysed in detail in chapter 3 and this shows that young people do appear to find it easier to escape low pay. There is also an issue regarding the role of the recession too. Young people may have switched into certain kinds of work during the recession and these sectors can mark their earning potential for a significant amount of time.

**3.45** It is also worth clarifying the role of students in Greater Manchester. Students are unlikely to play a significant role in Greater Manchester's overall labour market for the simple reason that as a proportion of the population they are slightly under-represented compared with the UK average (3.5% of the population compared to 3.6% in the UK). However they may well do so in Manchester itself and other central areas such as Salford where their population is concentrated. In Manchester, for example, students make up 10% of the population.

## Ethnicity

**3.46** The ASHE does not contain information on ethnicity, so to examine whether ethnic minority employees are affected by low pay to a greater extent than others it is necessary to rely on the LFS. The chart below shows that workers from ethnic minority backgrounds are far more likely to earn wages that pay rates below the low pay threshold. Just over 35% of black and ethnic minority (BME) workers earned less than the threshold in the years following the recession (ie. 2008-2014). This compares with 22.7% of non-BME workers. Some other regions appear to have higher proportions of ethnic minority staff earning below the threshold: in Tyne and Wear and South Yorkshire, more than 37% of workers from ethnic minority backgrounds earn below the threshold.

**Figure 12: Proportions of BME and non BME employees earning below low pay threshold**



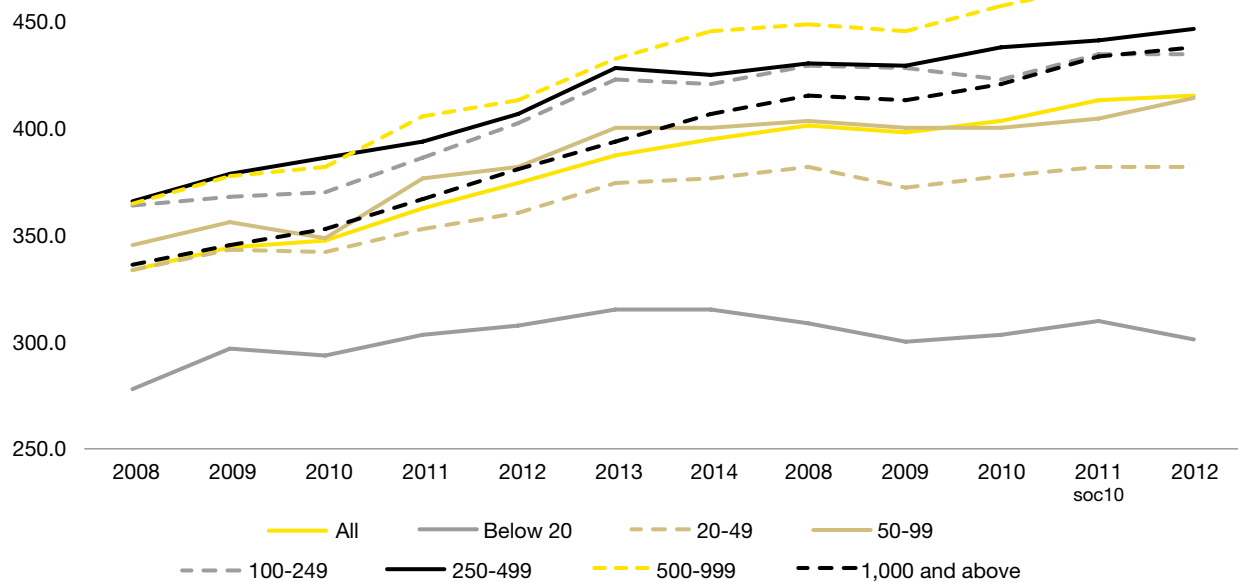
Source: LFS

## Firm Size

**3.47** In answer to the question of whether it is better for wage prospects to work in a small or large firm, the data is unequivocal: large firms pay better. This bears out the attitudes of the low paid as well in that wages and promotion prospects are seen as better among larger firms. Working for a big employer is viewed as intrinsically more desirable. The chart below shows wages over time by firm size. The chart demonstrates a significant pay penalty by firm size and a surprisingly large gap between firms with fewer than 20 staff and those with more than 20. In fact, while the pay bands by firm size have been broadly static, among firms with fewer than 20 employees, pay appears to have fallen even further behind in the last few years.

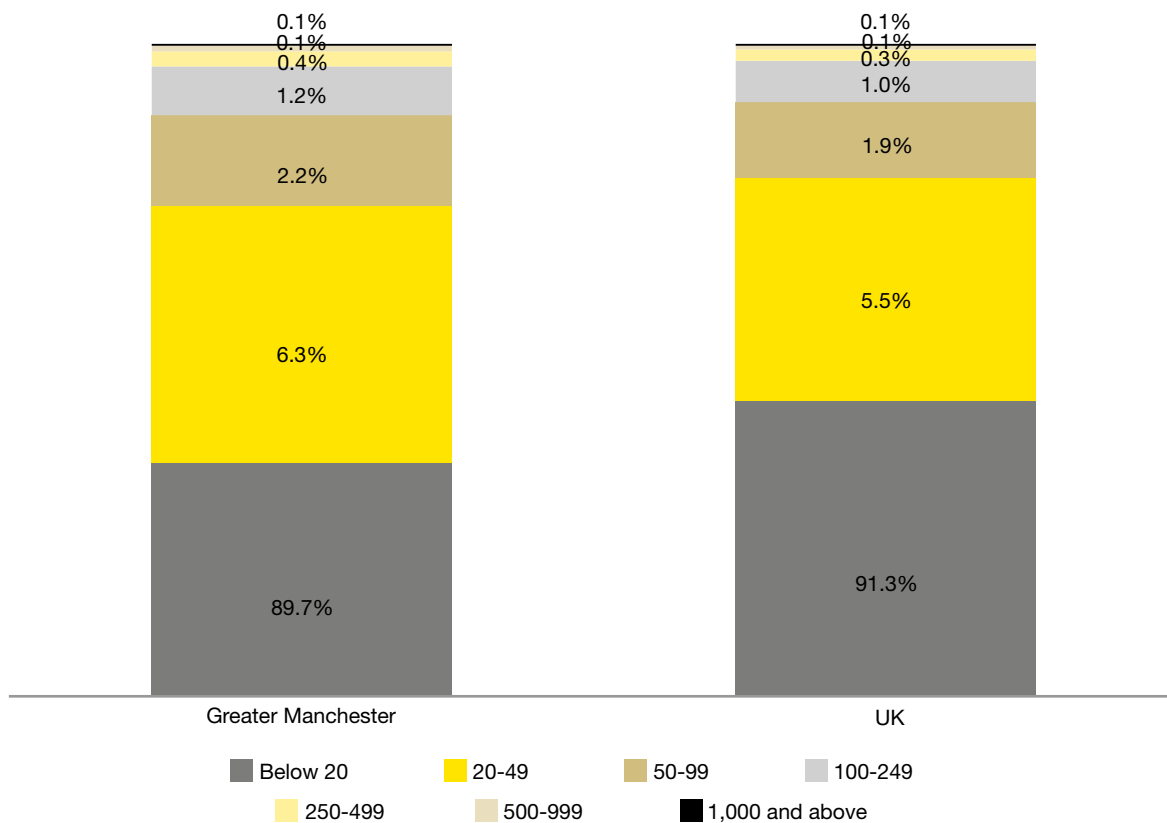
**3.48** The table below shows employment by firm size. Employment is significantly concentrated in smaller firms. Greater Manchester has a fractionally lower concentration of employment in small firms, but even so, just under 90% of workers in Greater Manchester work in firms with fewer than 20 employees.

**Figure 13: Median pay by firm size, UK, 2003-2014**



Source: ASHE 2014

**Figure 14: Employment by firm size, 2014**



Source: UK Business Count, ONS 2014

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## Zero Hours Contracts

**3.49** As we noted, it is a mistake to consider pay in isolation from other aspects of work. Yet data is not always available to make this broader understanding of job quality less abstract and the data that is available has been subject to repeat revisions<sup>39</sup>. Of all the aspects of the debate about insecurity, the use and spread of zero hours contracts is the most totemic. No data is available to investigate this issue on a city regional level. Yet data for the North West suggests 2.7% of employees are on zero hours contracts<sup>40</sup>. Greater Manchester tends to have many similarities with the characteristics of the wider North West and if we apply this percentage it would imply about 32,400 Greater Manchester employees are on zero hours contracts. The North West makes more use than the UK as a whole (2.4%) of zero hours contracts, but not to the extent of Wales, the South West, the West Midlands and East Midlands.

**3.50** According to the Office for National Statistics, there has been a very rapid rise in recent years. In 2012, it said 252,000 people nationally were on a zero hours contract in their main job. By 2015, this had risen to 744,000, due mostly to people on this type of contract for more than a year. A revision released in March 2016 put the number on ZHCs at 801,000<sup>41</sup>.

**3.51** People on zero hours contracts are more likely to be part-time. Part-timers make up 63.8% of people on zero hours contracts compared with 25% of all employees. They are also more likely to be female. The occupations in which they are most prevalent overlap with the lowest paying occupations, with particularly extensive use of the contracts in care and leisure industries and in elementary roles (less so in sales and customer service). However, by industry, there appears to be an extremely large concentration in accommodation and food (over 11%) and lesser but still significant concentrations in administrative and support work and in health and social work. Some 6.7% of 16-24 year olds are on a zero hours contract, compared with 2.4% among all age groups.

## Conclusion

**3.52** In common with other research, we find low pay to be concentrated among the young, women, and part-time, especially those working in shops, bars, restaurants and hotels, care-giving establishments and cleaning. Using the low pay threshold as the benchmark, we do not see a marked shift to low paying work in proportional terms, but there are greater numbers of low paid in the years since the recession on account of the expansion of the labour force as a whole. Using another definition of low pay (the living wage) there is a much starker trend of rising low pay in Greater Manchester. Regarding the low paying sectors, there are different trends within them. For example, employment agencies have been rapidly adding labour since the recession while the retail industry has been shedding workers.

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<sup>39</sup> See, for example, <http://www.telegraph.co.uk/finance/jobs/10798764/Employees-on-zero-hours-contracts-hits-1.4m.html>

<sup>40</sup> See ONS, 15 September 2015

<sup>41</sup> See <https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/earningsandworkinghours/articles/contractsthatdonotguaranteeaminimumnumberofhours/march2016>

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## 4 Productivity: Will higher productivity reduce low pay?

- 4.1** When challenged to explain low pay most orthodox economists would begin their answer with productivity – the quantity of goods and services produced per unit of factor input (in this case labour). The argument would be that pay reflects productivity and without underlying improvements to productivity no gains in pay can be contemplated, as every effect must have a cause. The relationship is sometimes stated as a sacrosanct economic law. Yet it is a law to which words such as mystery, paradox and puzzle are often appended – perhaps especially when it comes to productivity in the absence of a product, otherwise known as the service sector, where businesses do not necessarily prioritise productivity over other corporate virtues, such as profitability or return on investment. In many of these lines of work, the technologically induced improvements that drove productivity growth in industry are difficult to envisage without compromising service quality or customer experience: increasing the productivity of teachers or nurses would appear to imply larger class sizes or less time with a patient, while changing a hotel bed is arguably a similar job to what it was in the 19th century.
- 4.2** The chapter comes in two parts. The first discusses some of the theoretical issues involved in productivity and the views of orthodox and less orthodox economists in relation to the events since the recession of 2008 and with particular regard to low wage labour markets. The second part analyses productivity as it affects low pay in Greater Manchester.
- Economic Context:  
The UK Productivity Puzzle**
- 4.3** While UK GDP has recovered to levels above the pre-recession peak, labour productivity has experienced an unusually slow recovery, compared to previous recessions as well as to other OECD countries. The phenomenon has been dubbed the productivity puzzle. The Bank of England reports that labour productivity as measured by GDP per hour worked in the fourth quarter of 2013 was recorded at 4% below its pre-recession level. This was 16% below the level expected from the pre-crisis trend if previous patterns had endured. Pondering the national productivity puzzle has generated an intense debate, but as yet no definitive answers.
- 4.4** According to the bank, there are three principal reasons for this lag. First, that there is ‘spare capacity’ within firms. In other words, labour productivity is low because of low demand. As employers assume this a temporary phenomenon, and/or require minimum staffing levels to continue operating, there is low utilisation of labour within firms. But as productivity levels are usually procyclical and economic growth has recovered, utilization of labour and spare capacity cannot explain torpid labour productivity levels alone.
- 4.5** Second, more persistent factors may offer more powerful explanations. The recession led to underinvestment in process and product innovation, worsened by poor access to capital, thus hampering productivity growth. The authors also note the surprisingly high survival rate of unproductive firms. As a consequence, many firms are depending on labour intensive production because they have few incentives to invest in new technology. Put simply, if people are cheaper than new kit, why invest?
- 4.6** Third, measurement issues may be at work. Measurement issues might account for up to 4% of the 16% gap between actual labour productivity and the long term trend line mentioned above.
- 4.7** In a speech late in September 2014 the governor of the Bank of England, Mark Carney, identified a fourth possible cause of the lagging productivity of the UK labour market: a ‘labour supply shock’ led employees to accept work at lower real wages than before the crisis as a result of reduced levels of benefit entitlement, increased debt levels, or the need to increase pension fund savings. The ensuing decrease in the relative costs of labour led employers to reduce the rate at which capital investment substituted for labour, leading to lower labour productivity at the same time as the employment numbers reached a record high.

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<sup>42</sup> Barnett, A, et al, The UK Productivity Puzzle, Bank of England, Quarterly Bulletin, Q2,2014, <http://www.bankofengland.co.uk/publications/Documents/quarterlybulletin/2014/qb14q201.pdf>

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**4.8** The point is of profound importance for the growth of low pay sectors. According to the IMF<sup>43</sup>, the UK has seen a “redeployment of labor toward low productivity growth sectors”. Analysis by the economist John Ashcroft sectorally adjusts UK productivity data and finds that the UK productivity lag can be ascribed to high employment growth in low productivity services. He finds that almost all of the job creation over the last year has been in the service sector – particularly in leisure, hotels and restaurants – where the productivity gain is close to zero. His analysis suggests there should be less focus on the productivity gap at a national level, particularly as analysis of the UK’s poor performance compared to international comparators is also affected by differences in the mix of manufacturing and services, as well as exchange rate fluctuations<sup>44</sup>.

**4.9** However, research by Nesta returns to longer-term, pre-recessionary shortcomings in firms as being at the root of the productivity problem. Rather than a puzzle, it found a paradox: ‘good’, high-productivity firms go out of business and ‘bad’ inefficient ones survive; in other words, the exact opposite of the process of Schumpeterian creative destruction in which efficient firms gain momentum by attracting more labour and capital inputs and inefficient firms are diminished or driven out of the market. A project which examined productivity growth at firm level between 1998 and 2007 found that while new firms helped job creation, their productivity contribution was negligible and very few ever grew bigger: out of all the new firms created in Britain in 1998, only 37.5% survived for a decade and only 3.9% reached 10 or more employees<sup>45</sup>. Instead, it was the incumbents that contributed well over 90% towards productivity. Yet the mystery here was that firms with high productivity also folded as well as low productivity firms; if they had survived, productivity would be considerably higher. The result was that “more people [are] working in lower productivity firms within each sector.”<sup>46</sup> Much of the decline in efficiency was concentrated in service sectors such as the retail, wholesale, hotels and catering and post and telecommunications. In short, the authors conclude, the UK does not offer the best environment for good businesses to scale up.

## **Productivity: some insights from economic theory**

**4.10** According to the Office for National Statistics there are only two ways to improve living standards. The first is to increase the total number of people in employment (or increase the hours worked); the second is to increase the output per hour. Because British labour market participation is relatively high – indeed at its highest since the early 1990s – productivity growth is seen as the “primary route to improving our future standards of living in the long term”<sup>47</sup>. The message has become an official economic cynosure: “Productivity growth is the only sustainable source of real income growth in the long term”<sup>48</sup>, notes the Office for Budget Responsibility. Yet productivity growth in the UK has lagged comparable developed nations since the Second World War. It has thus become something of an enduring obsession of successive British governments.

**4.11** For an investigation of low pay, labour productivity is one of the key concepts, linked as it is in complex ways to individual prosperity. In orthodox economics, in conditions of perfect competition and where information is freely shared, employers have to pay the market wage and employees receive a wage that is equal to their ‘marginal revenue product’ (MRP). What this means is that the employer needs to decide how many employees they need to generate the right level of output and the highest level of profits. The marginal product is defined as the additional value created by one additional employee minus the cost of recruiting that employee (in other words the wage that is paid). The incentive for the employer to recruit the worker is if the extra output produced equates to at least the wages to be paid, thereby guaranteeing a profit. Central to this understanding is the notion that the employer does not determine wages: that is done by the laws of supply and demand operating in a free market. If an employer pays less than the rate the market decrees then the employees will look for better paid work elsewhere. Meanwhile, a firm would not hire an additional worker if the wage would be higher than the additional revenue. One should bear in mind, though, that measuring productivity for individual workers at a firm level is notoriously difficult, if not impossible, as it is not always clear what the contribution of an individual worker to firm revenue is.

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<sup>43</sup> International Monetary Fund: IMF Country Report No. 13/210, July 2013

<sup>44</sup> Ashcroft, John: The Saturday Economist. Man in Van Solves UK Productivity Puzzle. April 2015

<sup>45</sup> Bravo-Biosca, A and Westlake, S, The Other Productivity Puzzle: Business Dynamism and Productivity Growth Before the Crisis, Nesta, October 2014

<sup>46</sup> Ibid, p5

<sup>47</sup> Office for National Statistics: The ONS Productivity Handbook. October 2008

<sup>48</sup> Office for Budget Responsibility, Economic and Fiscal Outlook, December 2013, p5

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## How to grow productivity?

**4.12** So what encourages productivity growth? The paradigmatic statement of recent times was developed by the Treasury during the first New Labour government – the ‘Five Drivers of Productivity’. Published in 2000, it identified the five elements in increasing productivity as: investment (primarily in physical capital such as machinery and equipment); innovation; skills (both in terms of the quantity and quality of labour deployed in ways to complement physical capital); enterprise (including the capabilities and attitude of management); and competition (so as to create incentives to innovate and the allocation of resources to the most efficient firms). Two of the drivers (capital and skills) derive from the traditional post-war growth literature and three (enterprise, competition and innovation) have their origins in more contemporary thinking about endogenous growth.

**4.13** The drivers have been influential in terms of shaping economic policy. Yet they are hardly the last word. Furthermore, understanding of the interdependencies between the drivers is evolving and only partially understood. “A somewhat arbitrary selection of the factors that might be assumed to have an impact on performance”<sup>49</sup> was the verdict of three (more critical) economists. The same economists also observe that productivity is not necessarily a preoccupation of business leaders – particularly in services – and so the drivers lack purchase on the commercial world. Policymakers and economists care about productivity; businesspeople often care less. Instead, business leaders and their organisations typically highlight other concerns: shareholder value, profitability, customer focus and return on investment. The concept of productivity, with its roots in primary and secondary industries, can seem a little distant from life in hotels and shops, cleaning and catering, caring and serving.

**4.14** In local economic development circles, skills tend to be the driver that receives attention – arguably because they are perceived to be easier to influence than the other drivers. According to the Manchester Independent

Economic Review<sup>50</sup>, for example, a city region’s skill level (especially the concentration of skilled workers with NVQ level 4+) explain much of the productivity difference with other regions. The review concluded: “For every region (with the exception of Scotland) lower skills account for a big part of the productivity disadvantage relative to the south east.” Although ‘skills’ are often mentioned as spurring productivity growth in general, the strongest evidence of the impact of skills on regional productivity is at level 4. There is, however, little or no relationship at level 3 and even negative correlations at level 2 and below<sup>51</sup>. Furthermore, it has been noted that decades of investment in skills supply (or at least qualifications), has yet to persuade productivity trends to depart from their long-term historical growth trajectory<sup>52</sup>.

**4.15** In a review of the economic evidence for the drivers, Fawcett and Cameron note that for three of the drivers (physical investment, skills and innovation) the evidence is clear, but it is less so for the others<sup>53</sup>. Interdependencies between the drivers also cause problems in relating theory to empirical evidence. The international dimension of growth (through trade, knowledge spill-overs and technology transfer) and lack of knowledge of how changes in the channels through which the drivers affect the economy, mean understanding is inevitably “imprecise”<sup>54</sup>.

**4.16** In any case, the government’s view of productivity drivers is not set in stone. In the early 2000s, the Department of Trade and Industry claimed the five drivers operated at too general a level to be useful and sought greater detail through the ‘16 key levers of productivity’<sup>55</sup>. (These appear to have been quietly forgotten about in the years since). In the budget of July 2015 the five drivers were not mentioned and were superseded by a schema with eight points and 15 sub-headings called ‘a framework for raising productivity’<sup>56</sup>. The eight are: long-term investment; skills and human capital; economic infrastructure; ideas and knowledge; flexible, fair markets; productive finance; openness and competition; and resurgent cities.

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<sup>49</sup> See Keep, E., Mayhew, K., and Payne, J., *From Skills Revolution to Productivity Miracle – Not as Easy as it Sounds?*, Oxford Review of Economic Policy, Vol 22, No 4, 2006, p543

Keep, E

<sup>50</sup> Killop, T, Coyle, D., Glaeser, E, Kestenbaum, J, O’Neill, J: *Manchester Independent Economic Review. The Case for Agglomeration Economies*, 2009. Manchester

<sup>51</sup> Oguz, S. and Knight, J., *Regional Economic Indicators*, Economic and Labour Market Review, Office for National Statistics, February 2011; it is worth noting that one possible explanation for negative returns at level 2 could be immigration, as immigrants flock to high productivity regions, but have a higher share of ‘other qualifications or below level 2

<sup>52</sup> See Keep, E., Mayhew, K., and Payne, J., *From Skills Revolution to Productivity Miracle – Not as Easy as it Sounds?*, Oxford Review of Economic Policy, Vol 22, No 4, 2006

<sup>53</sup> Fawcett, N. and Cameron, G., *The Five Drivers, An Empirical Review*, Discussion Paper Series, University of Oxford, December 2005

<sup>54</sup> *Ibid*, p25

<sup>55</sup> Department of Trade and Industry, *The Strategy: Analysis*, DTI, 2003, p48

<sup>56</sup> HM Treasury, *Fixing the Foundations: Creating a More Prosperous Nation*, July 2015, p7



**4.17** The list is potentially open to criticism for bypassing important considerations. For example, the motivation and engagement of people at work might be thought to have an impact on performance, in part through how people are managed, led and organised around productive processes. More committed staff who are willing to deploy their discretionary effort for their employer might, in theory, lead to better corporate performance. Government publications sometimes say such factors count towards competitiveness and productivity – it supported the Employee Engagement Task Force to this end, for example<sup>57</sup>. But standardising measures of ‘psychological’ concepts can mean they struggle for attention among some, but not all, economists<sup>58</sup>.

## Productivity and wages

**4.18** Although productivity has to be seen as important to the low pay debate, it is a mistake to think it is the only relevant consideration for wage determination. The compensation of employees will also be affected by other factors related to labour supply elasticity (number of workers available with the required skills, length of training to acquire skills and the bargaining power of workers, perhaps through unionisation), or to labour demand elasticity (the ability of employers to substitute capital for the labour of a particular occupation, the market demand elasticity for the product or service for which labour is a factor input, the share of labour costs of total costs). As the labour market is intensely segmented, due to the development of the division of labour, the specific factors impacting wages and the number of jobs will differ widely between sectors.

**4.19** A central question here is whether, contrary to the assumptions of neoclassical economics, it really is markets that set wages in accordance with MRP in conditions of perfect competition and where information is freely shared. In real-world labour markets, there is seldom perfect competition and information is not always freely shared. Employment contracts are typically characterised by an imbalance of power, with the opportunities for employees to negotiate the terms of the exchange generally fairly limited; in general, they are expected to take it or leave it. During recruitment processes there is an asymmetry of information. It is generally easier for an employer to recruit workers than

it is for workers to find another job: the employer knows how much it costs to recruit and train an employee and typically where to find them. The employee, however, may not be aware of job opportunities, even after spending some considerable time looking for work, and they may also find it practically impossible to move locations to where new jobs are available (economists sometimes call such issues ‘frictions’). This means that the employer has more influence over the level of wages than is allowed for by the conventional theory. In other words, it is employers who determine the level at which wages can be paid rather than markets.

**4.20** The set of economic arguments that highlight the power of employers in labour markets where less than perfect competition and information prevail has come to be known as ‘monopsony’ (in Greek, ‘monos’ means single and ‘opsonia’ purchase). The concept originally referred to a situation where would-be sellers face only one buyer and the buyer thus has the power to determine the level of wages. The textbook example is a company town where only one employer exists and can pay the wage it chooses because workers have nowhere else to go – a ‘many nurses and one hospital’ type scenario. Obviously, this is an unlikely situation. But a variant on monopsony of a limited number of employers colluding to set wages (oligopsony) is perhaps not so impossible to imagine.

**4.21** Yet the argument of some economists is that most low paying labour markets – even those with many different employers – have large elements of monopsony which mean that the labour market has inadequate competition. As a result employers have great influence over wages, employment and skills formation, and workers face very considerable costs to changing jobs<sup>59</sup>. In what has become a famous phrase, the high degree of discretion that employers enjoy over wage levels mean that wage setting is not a precise mirroring of marginal productivity, but is subject to ‘a range of indeterminacy’<sup>60</sup>. By extension of this argument, productivity may not be the main influence on wage levels, but only one among several influences.

**4.22** As well as bargaining power, it is possible for wages to rise independently of productivity improvements in a given sector, due to improvements in other sectors. The economist William Baumol made a classic contribution to this debate in the 1960s, lending his name to a condition known as ‘Baumol’s cost disease’<sup>61</sup>. This describes a

<sup>57</sup> See Macleod, D and Mann, N, Engaging for Success: Enhancing Performance Through Employee Engagement, DBIS, July, 2009

<sup>58</sup> See Acas, Building Productivity in the Workplace, June 2015. This advances ‘seven levers of workplace productivity: high trust, strong employee voice, fairness, clarity about rights and responsibilities, managing conflict effectively, skilled managers and well-designed work. It might be observed though that some of the five drivers, such as enterprise, also suffer from the same measurement problems

<sup>59</sup> See Manning, A., Monopsony in Motion: Imperfect Competition in Labour Markets, Princeton, 2005

<sup>60</sup> Card, D. and Krueger, A., Myth and Measurement. The New Economics of the Minimum Wage, Princeton (1995); see also Card, D. and Krueger, A., Minimum Wages and Employment. A case study of the fast-food industry in New Jersey and Pennsylvania. Reply, American Economic Review 90 (2000)

<sup>61</sup> Baumol, W.J., Macroeconomics of Unbalanced Growth: The Anatomy of an Urban Crisis, American Economic Review, Vol.57, No.3 (June 1967)

situation where productivity rises in one sector leading to higher wages, but which then triggers wage rises in other sectors as they try to keep up with the offer of the more productive sectors in order to recruit and keep hold of staff. Yet there is no productivity rise in these sectors to offset the wage rise. This leads inexorably to rising costs over time without underlying productivity improvements. Baumol contrasted what he called 'technologically progressive' sectors (mostly manufacturing) which were able to increase their output per hour through technology, innovation and economies of scale and activities that were largely impervious to technologically induced productivity improvements such as many service sectors. The source of the difference was the role of labour in the production process. "In some cases [manufacturing] labour is primarily an instrument - an incidental requisite for the attainment of the final product, while in other fields of endeavour [services], for all practical purposes the labour is itself the end product...in which quality is judged directly in terms of amount of labour." His favourite example of a 'service' in which productivity improvement was unimaginable was musical live performance. "A half hour horn quintet calls for the expenditure of two man hours in its performance, and any attempt to increase productivity here is likely to be viewed with concern by critics and audience alike."<sup>62</sup> As advanced economies migrated more labour into services and away from production, growth would inevitably slow, he contended, as costs would inexorably rise.

- 4.23** We should bear in mind, however, that in many professional service jobs the productivity of workers was enhanced by the substitution of labour (secretaries and administrative assistants) by capital (especially computers), as well as their contribution to economies of scale at large industrial production sites. These developments were impossible to foresee at the time Baumol wrote his seminal article. The coordination of the increased complexity of supply chains and markets necessitated an expanded role and quantity of managerial and clerical tasks leading to increased demand for skilled white collar jobs<sup>63</sup>.

## Measuring productivity

- 4.24** Sub-national productivity measures invariably use Gross Value Added (GVA) as the central indicator of economic output, which can be referenced against other data such as GVA per job or per capita, as appropriate, to derive a productivity calculation. GVA is an economic aggregate statistic designed to reflect the value of output generated by organisations in an area minus the value of inputs used in the production and delivery process. Simplistically, GVA is calculated by adding up all profits and wages earned by people in a given area<sup>64</sup>. Greater Manchester's GVA was £56 billion in 2013.
- 4.25** However, arguably the use of GVA in measuring sub-national productivity raises an as-yet unresolved issue in how we should understand productivity. As noted, orthodox economics understands wages as reflecting MRP. Yet GVA (as conventionally used) is a measure of wages and profits. For the first, the causation runs from productivity to wages; for the second, the direction of causation is apparently reversed as wage levels can influence productivity performance. The disjuncture is potentially serious when it comes to contemplating policy interventions: higher prices and better wages are likely to boost GVA rather than underlying improvements of output relative to inputs. At the least, it is advisable to be cautious about reading too much into regional productivity estimates when using GVA as there is a degree of uncertainty around measurement issues.
- 4.26** Nevertheless, GVA has become an important indicator for local economic development. Although there are many different approaches to measuring labour productivity at a regional/GM level - GVA per capita, GVA per worker and GVA per hour, to name three - it is ultimately a policy choice which measure is chosen. Each has strengths and weaknesses. Economists tend to prefer GVA per hour worked, as this it is not influenced by demographic or labour market participation factors and it also takes into account different working patterns, for example a predominance of part time jobs, low hours, student jobs, or zero hour contracts. However, data availability is poor at a Greater Manchester level. This report uses two measures: in general, GVA per job data is the productivity measure that has been used when discussing low productivity sectors. In addition, we use GVA per capita to enable analysis of the productivity impacts of economic inactivity and joblessness.

<sup>62</sup> *ibid*

<sup>63</sup> See Frey, C.B. and Osborne, M., *The Future of Employment: How Susceptible Are Jobs To Computerisation*, Oxford Martin School, September 2013

<sup>64</sup> It is calculated based on the workplace where GVA is created, not the residence of where the employee may live. It is important to note that some types of income (primarily benefit payments) are not included in this calculation as they are a redistribution of existing incomes

## Greater Manchester's economic performance and the productivity gap

**4.27** In terms of productivity performance, Greater Manchester is a double-lagger: a lagging region within a lagging nation. It has been this way ever since consistent records were established in 1997 - and probably before as well. The gap between Greater Manchester and the rest of the country has remained broadly constant on a GVA per capita basis since 2007 (Greater Manchester's GVA per capita fell slightly from 90% of the UK figure to 89% in 2013).

**4.28** New Economy has calculated that if Greater Manchester's per capita GVA was the same as that of the average for Great Britain, its total output would be £8.2 billion greater. The research finds demographic and labour market participation factors account for around a fifth of the gap (or £1.6 billion), due in part to lower employment rates, while in-work factors account for four fifths of the gap (or £6.6 billion). The reason is that not only are the sectors relatively lower value, but less

is achieved by each job within the sectors: in only one sector (arts and entertainment) is GVA higher in Greater Manchester than elsewhere. We turn next to consider productivity in a Greater Manchester context.

## Sector productivity in Greater Manchester – identifying the low productivity sectors

**4.29** The table below shows the calculations for labour productivity in Greater Manchester and identifies the five 'low productivity sectors'. The five lowest productivity sectors in Greater Manchester, which we have defined as below £30,000 GVA per job, are: accommodation and food services; arts and entertainment; health and social care; administrative and support service activities; and retail. The most productive of these five sectors is retail and the least productive is accommodation and food services. All fall a long way below the average level of productivity per job of approximately £39,300 in Greater Manchester which is itself below the UK level. Table 11 shows the substantial overlap between low productivity sectors and the low pay sectors.

**Table 10: Productivity by sector in Greater Manchester, 2000-2014**

Sectors (excluding primary sector)	GVA per job 2014	GVA per job change 2013-14	GVA per job change 2000-7	Number of jobs 2000-7	GVA per job change 2007-14	Number of jobs 2007-14
<b>L: Real estate activities</b>	£208,327	0.4%	-15.6%	70.7%	-12.0%	42.5%
<b>E: Water supply; sewerage, waste management</b>	£78,656	3.4%	4.4%	-8.0%	-11.0%	36.8%
<b>J : Information and communication</b>	£66,334	-1.9%	64.7%	12.6%	11.2%	-19.0%
<b>K: Financial and insurance activities</b>	£65,075	2.4%	39.9%	7.7%	-23.2%	11.2%
<b>C: Manufacturing</b>	£64,127	2.9%	77.7%	-34.6%	23.9%	-15.3%
<b>S: Other service activities</b>	£38,582	5.7%	4.6%	-10.5%	24.7%	-5.1%
<b>F: Construction</b>	£37,789	4.5%	-0.5%	46.9%	-1.0%	-17.8%
<b>O: Public administration and defence; social security</b>	£36,058	-3.8%	3.0%	5.4%	8.5%	-20.0%
<b>H: Transportation and storage</b>	£34,516	7.7%	-7.0%	7.5%	-12.2%	9.6%
<b>G: Wholesale and retail trade; repair of motor vehicles</b>	£32,795	6.9%	22.8%	1.6%	7.7%	0.0%
45 & 46: Wholesale and motor vehicles trade	£44,705					
47: Retail trade	£25,319					
<b>P: Education</b>	£31,832	1.5%	-10.5%	2.3%	-13.0%	6.3%
<b>M: Professional, scientific and technical activities</b>	£31,776	11.7%	49.3%	34.9%	-17.2%	42.2%
<b>N: Administrative and support service activities</b>	£24,332	14.1%	21.8%	14.7%	1.9%	25.4%
<b>Q: Human health and social work activities</b>	£23,532	4.5%	19.0%	20.6%	-2.2%	14.5%
<b>R: Arts, entertainment and recreation</b>	£21,934	4.9%	15.9%	21.5%	6.7%	8.5%
<b>I: Accommodation and food service activities</b>	£19,169	-0.7%	19.7%	11.1%	2.0%	1.4%
<b>GM total</b>	£39,328	4.1%	22.0%	5.2%	-1.2%	5.4%
<b>UK total</b>	£45,093	3.3%	17.2%	7.5%	-0.6%	1.0%

Source: Authors' calculations using GMFM 2014

<sup>65</sup> In the case of the wholesale and retail sector we have subdivided the sector into its constituent parts - wholesale and motor vehicles trade on the one side, and retail trade on the other. While the wholesale and motor vehicles GVA per job of £44,700 and therefor above average productivity, in retail a job generates in average only £25,300

**Table 11: Correspondence between low pay sector and low productivity sectors, 2014**

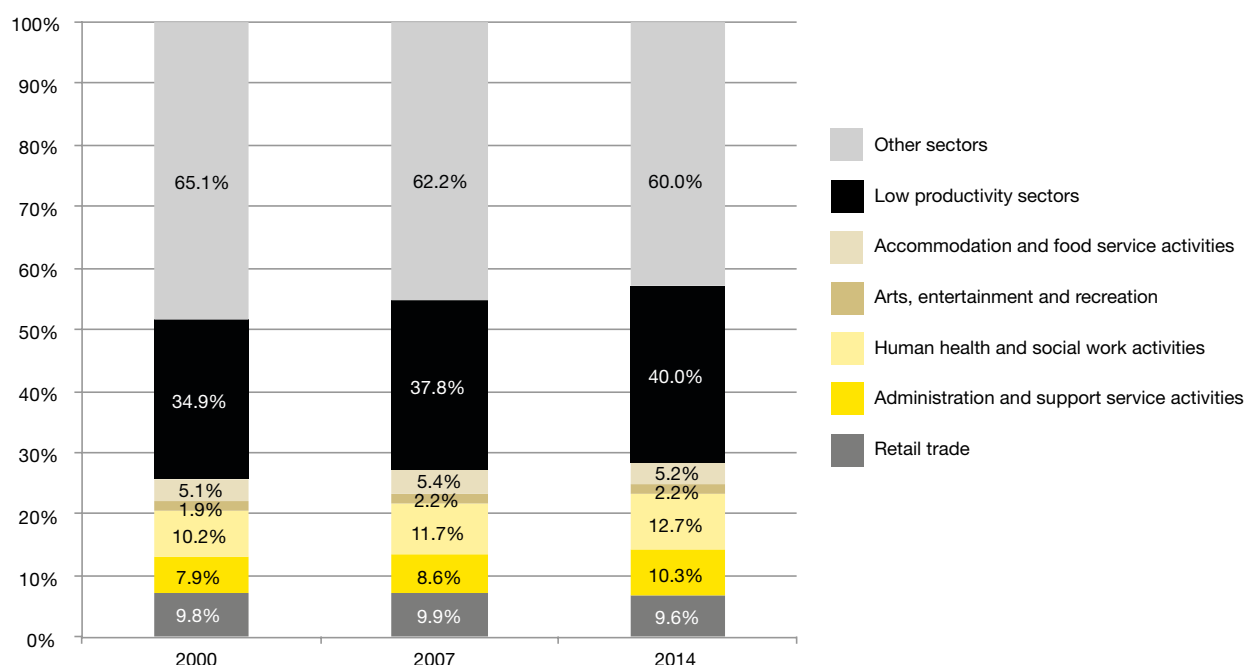
Greater Manchester - Employment Growth in Low Pay Industries	Proportions of jobs paying up to the low pay threshold	Proportions of all Em- ployees in GM (BRES 2013)	Growth in employees between 2007 and 2013	Sector Size ranking
56: Food and beverage service activities	76%	4.9%	-3%	Accommodation and Food Services
55: Accommodation	60%	1.0%	17%	Accommodation and Food Services
92: Gambling and betting activities	58%	0.4%	-18%	Arts, Entertainment and Recreation
81: Service to buildings and landscape activities	53%	2.0%	14%	Administrative and Support Services
47: Retail trade, except of motor vehicles and motorcycles	53%	10.0%	0%	Wholesale and Retail Trade
87: Residential care activities	53%	2.3%	-24%	Human Health and Social Work
96: Other personal service activities	49%	0.9%	-14%	Other Service Activities
80: Security and investigation activities	48%	1.0%	18%	Administrative and Support Services
93: Sports activities and amusement and recreation activities	44%	1.3%	6%	Arts, Entertainment and Recreation
88: Social work activities without accommodation	43%	2.9%	20%	Human Health and Social Work
45: Wholesale and retail trade and repair of motor vehicles and motorcycles	43%	1.4%	-21%	Wholesale and Retail Trade
78: Employment activities	39%	3.8%	13%	Administrative and Support Services
<b>Total</b>	<b>52%</b>	<b>31.9%</b>	<b>1%</b>	

Source: ASHE

## Sector trends in Greater Manchester – share of the economy

**4.31** The chart below shows that the low productivity sectors in Greater Manchester have been adding labour in recent years. The low productivity sectors accounted for just under 40% of all employment in the city region in 2014. Go back to 2000 and the same sectors accounted for just under 35% of employment. Related to this, the ‘other sectors’ – meaning all sectors other than the five low productivity sectors with GVA per job of below £30,000 – have been declining in terms of the proportion of jobs, shrinking from 65% to 60%. This represents a significant shift of the share of jobs towards sectors which could be considered to generate low productivity. The rise of this type of work is almost entirely due to the disproportionate increase of two sectors: administrative and support service activities (from 7.9% in 2000 to 10.3% in 2014); and human health and social work activities (rising from 10.2% to 12.7%).

**Figure 15: Employment share of low productivity sectors in Greater Manchester, 2000-2014**



Source: Authors' calculations based on GMFM 2014

**4.32** Greater Manchester has experienced sharper growth in these sectors than the UK as a whole. Comparing Greater Manchester's low productivity sectors with the same sectors at a UK level shows that the city region's share grew faster than nationally – by 5.1 percentage points compared to 3.6 percentage points for UK. Compared to the UK as whole, the administrative and support service sector's share also grew more (by 2.4 percentage points, compared to 1.4 percentage points), possibly a reflection of the city region's strength in back office and corporate support service activities. Meanwhile, in comparison with national figures, the share of retail workers did not decrease as rapidly as was the case nationally (by 0.2 percentage points compared to 0.8 percentage points in the UK). Most other sectors' trends were roughly in line with the national figures. It is important to remember, however, that these are very broad, often highly heterogeneous sectors in which lines of work have been combined into potentially misleading averages. In health, for example, kitchen porters and brain surgeons are brought together, even though they inhabit completely different labour markets. In addition, as there is no market for large parts of the health sector (eg. NHS workers), productivity data is somewhat dubious.

**4.33** There are two obvious interpretations of this shift. The expansion of employment in low productivity sectors could be due to low skilled workers who were previously unemployed or economically inactive finding work (in which case the increase in the low productivity sector could be even said to have positive implications). As the Institute for Fiscal Studies noted on the UK productivity gap: "It is often argued that part of the explanation for the UK's relatively low level of productivity is that it manages to employ a high proportion of less-skilled individuals, who tend to have lower productivity. This tends to reduce average GDP per worker, even though it increases GDP per person of working age. It is certainly the case that much of the expansion of employment in the UK over the last 10 years has been in service sectors with low average productivity."<sup>66</sup>

**4.34** By contrast, the other view is that the shift towards low productivity employment is a manifestation of structural change in which middle and high productivity (and pay) work is gradually eroded by lower productivity jobs. In this latter case, this trend could be seen as problematic. According to the ONS economic activity has roughly remained stable (leaving aside the recession): it was recorded at 74% in 2004, growing to 74.4% in 2007,

<sup>66</sup> Institute for Fiscal Studies: Productivity Policy. Election Briefing 2015

and finally to 74.7% for the year ending September 2014. The ILO unemployment measure (unemployed as a proportion of those who are economically active), meanwhile, was recorded at 5.2% in 2007 and 7.5% in the year ending in September 2014. However, over the time period the population of Greater Manchester has grown from 2.516 million in 2000 to 2.715 million in 2014 – a growth of almost 8%. While further data analysis would be needed we could assume from the increase in the number of residents and a small increase in the rate of economic activity that some of the additional jobs are in the low productivity sectors rather than replacing existing ones.

## Sector productivity trends

**4.35** Greater Manchester's low productivity sectors have an intriguing story to tell of their fortunes since the millennium. When the economy was expanding before the recession, the low productivity sectors grew more slowly than the average. Since the recession, however, productivity performance has been so weak in the economy at large that the (unimpressive) performance of the low productivity sectors actually appears to be relatively strong.

**4.36** In the years between 2000 and 2007, productivity grew slightly less fast than in other sectors, perhaps partially explaining the wage gap over time. As can be seen in the table below the annual productivity (GVA per job) of four low-productivity sectors grew at a rate below or equivalent to the average annual rate for all sectors (between 2.1% and 2.9% per year; retail and wholesale grew fractionally faster). This means that productivity in the four sectors was increasing at a lower rate than in the city region's economy as a whole. We should, however, bear in mind that productivity growth in Greater Manchester during the pre-recession period was driven by only a few sectors – namely manufacturing, ICT, financial and insurance, and professional and scientific services. This slow productivity growth might lead to wages at the bottom of the labour market increasing less rapidly over time and resulting in an increase in wage inequality.

**4.37** However, during and after the recession – a period which witnessed an average annual decline of productivity of 0.2% in Greater Manchester – the productivity performance of the low productivity sectors mostly outpaced the conurbation's average. In comparison to many other sectors the low productivity sectors have arguably had a relatively benign post-recessionary period.

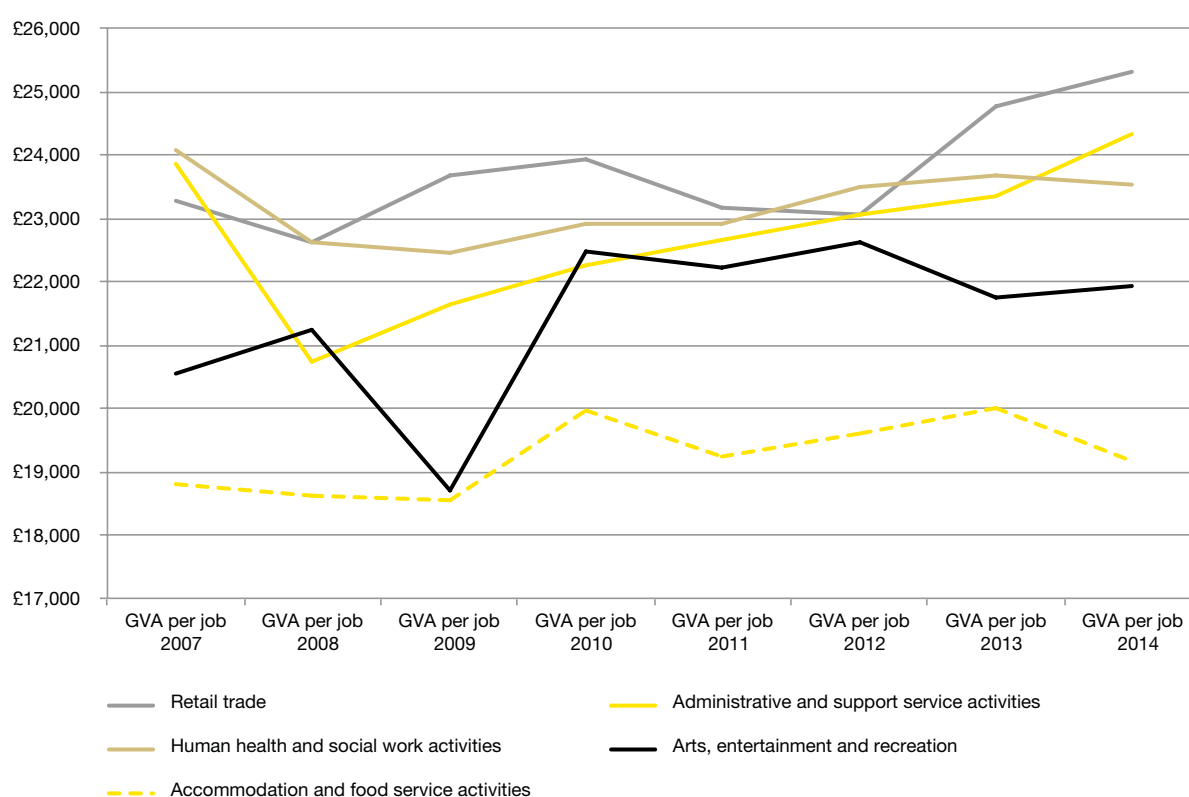
**Table 12: Productivity performance by sector**

Sectors (excluding primary sector)	Annual GVA change 2000-7	Annual GVA change 2007-14	Annual GVA change 2000-14	Annual GVA per job change 2000-7	Annual GVA per job change 2007-14	Annual GVA per job change 2000-14
<b>L : Real estate activities</b>	5.4%	3.3%	4.3%	-2.4%	-1.8%	-2.1%
<b>E : Water supply; sewerage, waste management</b>	-0.6%	2.9%	1.1%	0.6%	-1.6%	-0.5%
<b>J : Information and communication</b>	9.2%	-1.5%	3.7%	7.4%	1.5%	4.4%
<b>K : Financial and insurance activities</b>	6.0%	-2.2%	1.8%	4.9%	-3.7%	0.5%
<b>C : Manufacturing</b>	2.2%	0.7%	1.4%	8.6%	3.1%	5.8%
<b>S : Other service activities</b>	-0.9%	2.4%	0.7%	0.6%	3.2%	1.9%
<b>F : Construction</b>	5.6%	-2.9%	1.2%	-0.1%	-0.1%	-0.1%
<b>O : Public administration and defence; social security</b>	1.2%	-2.0%	-0.4%	0.4%	1.2%	0.8%
<b>H : Transportation and storage</b>	2.1%	-2.6%	-0.3%	-1.0%	-1.8%	-1.4%
<b>G : Wholesale and retail trade; repair of motor vehicles</b>	3.2%	1.1%	2.1%	3.0%	1.1%	2.0%
<b>P : Education</b>	-1.2%	-1.1%	-1.2%	-1.6%	-2.0%	-1.8%
<b>M : Professional, scientific and technical activities</b>	10.5%	2.4%	6.4%	5.9%	-2.7%	1.5%
<b>N : Administrative and support service activities</b>	4.9%	3.6%	4.2%	2.9%	0.3%	1.6%
<b>Q : Human health and social work activities</b>	5.3%	1.6%	3.4%	2.5%	-0.3%	1.1%
<b>R : Arts, entertainment and recreation</b>	5.0%	2.1%	3.6%	2.1%	0.9%	1.5%
<b>I : Accommodation and food service activities</b>	4.2%	0.5%	2.3%	2.6%	0.3%	1.4%
<b>GM total</b>	3.6%	0.6%	2.1%	2.9%	-0.2%	1.3%

Source: GMFM 2014

**4.38** Although growing productivity in people-facing services may be difficult, it is clear that in modest, dilatory fashion, the low productivity sectors have been finding ways to become more productive. This is especially the case for the retail sector which witnessed an increase of its GVA per employee from just over £23,000 in 2007 to over £25,000 in 2014. While we have no information on what has caused this performance, the answer might lie in the increase in automation in some retail segments over the period, as well as in the growth of online shopping and self-service. The performance of these sectors contrasts with an annual decline in productivity overall of 0.2% over the same time period. However, caution is needed when interpreting time series analysis of sub-regional productivity data, as the data is regarded as somewhat volatile<sup>67</sup>.

**4.39 Figure 16: Productivity trends in five low productivity sectors, 2007-2014**



Source: GMFM, 2014

**4.40** A further point worth noting here is that the low productivity sectors are relatively competitive compared to the country as a whole. While the 'productivity gap' between Greater Manchester and the country as a whole is well-evidenced, the gap is not at its widest in the five low productivity sectors. Instead, the more knowledge and capital intensive sectors of professional services, financial services, property and transportation are the sectors with the greatest gap and where the need for productivity catch-up is at its most acute. In these sectors the gap is well into double digits. Meanwhile, in the low productivity sectors, it is generally lower (although there are some exceptions). On average the gap is 10%. The table below demonstrates the productivity gap by sector.

<sup>67</sup> Office for National Statistics: Subregional Productivity – February 2015

**Table 13: Productivity gaps across sectors in Greater Manchester, 2014**

Sectors (excluding primary sector)	GVA per job 2014	% of jobs total 2014	% of GVA total 2014	GVA per job difference between GM and GB
<b>L: Real estate activities</b>	£208,327	2.3%	11.9%	-22.8%
<b>E: Water supply; sewerage, waste management</b>	£78,656	0.6%	1.2%	-11.8%
<b>J : Information and communication</b>	£66,334	2.6%	4.4%	-6.7%
<b>K : Financial and insurance activities</b>	£65,075	3.8%	6.3%	-36.1%
<b>C: Manufacturing</b>	£64,127	7.9%	12.9%	11.7%
<b>S: Other service activities</b>	£38,582	2.6%	2.5%	-3.9%
<b>F: Construction</b>	£37,789	5.9%	5.7%	-2.1%
<b>O: Public administration and defence; social security</b>	£36,058	3.8%	3.5%	-16.4%
<b>H: Transportation and storage</b>	£34,516	5.5%	4.8%	-16.0%
<b>G: Wholesale and retail trade; repair of motor vehicles</b>	£32,795	15.6%	13.0%	-7.8%
<b>45 &amp; 46: Wholesale and motor vehicles trade</b>	£44,705	6.0%		-8.7%
<b>47: Retail trade</b>	£25,319	9.6%		-8.7%
<b>P: Education</b>	£31,832	8.3%	6.8%	-8.0%
<b>M: Professional, scientific and technical activities</b>	£31,776	9.9%	8.0%	-22.7%
<b>N: Administrative and support service activities</b>	£24,332	10.3%	6.3%	-14.7%
<b>Q: Human health and social work activities</b>	£23,532	12.7%	7.6%	-6.7%
<b>R: Arts, entertainment and recreation</b>	£21,934	2.2%	1.2%	-7.3%
<b>I: Accommodation and food service activities</b>	£19,169	5.2%	2.5%	-2.4%
<b>GM</b>	£39,328	100.0%	98.7%	-10.0%

Source: GMFM 2014

**4.41** A critical implication of this data is that the outcome of possible policies that endeavour to address the productivity gaps of Greater Manchester's economic sectors would be expected to be very limited in respect of the low productivity sectors. The gap to be covered by potential productivity increases is relatively small and most unlikely to be realised on any significant scale. There appear to be much greater potential opportunities for closing the productivity gap in the more knowledge-intensive, technology-dependent sectors. Most workers on low pay, working predominantly in one of the five low productivity sectors, would be least affected by potential productivity increases by GM firms, which would most likely be realized in higher productivity sectors. As the scope for productivity improvements in the low productivity sectors seems rather limited, the challenge of low pay might be better addressed by increasing labour mobility out of these low productivity sectors rather than progression within them. This policy perspective would engender two challenges.

**4.42** Firstly, there would be a challenge in training the labour force so they have the skills required for the higher productivity sectors. While many of the low productivity sectors require only low or intermediate skill levels, knowledge intensive sectors (primarily financial services, the professions and communications services) need predominantly highly skilled workers as these roles consist mostly of non-routine knowledge intensive activities. Many of the medium-to-low skilled workers would face barriers when trying to progress into these economic sectors.

**4.43** The second policy challenge stems from the relatively low number of jobs available in these economic sectors. We should bear in mind that the three knowledge intensive sectors provide for just over 190,000 jobs, or less than 14%, of the total jobs in Greater Manchester. The five low productivity sectors, in contrast, provide almost 560,000 jobs - 40% of jobs within the city region. However, as noted above, not all occupations in the low productivity sectors can be regarded as low skill/unproductive jobs.



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**4.44** The administrative and support service sector is an exception to the pattern of lower productivity gaps among the low productivity sectors. While considered a low productivity sector, its productivity gap is 15%, a markedly larger gap than the average (10%). This is a fairly large sector whose GVA share of Greater Manchester's economy has risen over time from 7.9% in 2000 to 10.3% in 2014 (indicating a faster than average growth of that sector). This sector employs more than 10% of the Greater Manchester workforce. It requires mostly medium skilled labour and pays low-to-middling wage levels. The fact that this sector exhibits a productivity gap above the average, has some education requirements and pays wages that are not at the very bottom might make the sector a possible growth area for career progression out of other low productivity sectors. Many workers in the low productivity sectors might meet the skills requirements of this sector, unlike other lines of work such as professional services. Additionally, research conducted by IPPR shows that typical career progression out of low skill/pay sectors is into middle skilled/paid sectors, rather than high skilled/paid ones<sup>68</sup>.

## Conclusion

**4.45** Will productivity growth improve the wages paid at the bottom levels of the labour market? The evidence suggests that although there remains a clear overlap between low productivity sectors and low wages, productivity growth is unlikely to moderate poverty pay in the near future. The issues affecting the low productivity sectors have a long history. Yet these sectors have arguably had a 'better' recession and recovery than many other sectors. This is surely more a testament to the difficulties of the post-recessionary years than these sector's inherent economic growth potential. In addition, because of the nature of the low-productivity sectors, economic theory suggests that the conventional means to boost productivity – capital substitution, innovation and economies of scale – may be difficult to implement. The important exception may be retail, which has seen dramatic technological development which has transformed both customer experiences and logistics and supply chains. As might be expected, productivity has also been better in retail than in some of the other low productivity sectors, and, equally unsurprising, job growth has been much lower. Nevertheless, the low productivity sectors overall are finding ways to grow and there is a relatively small gap between their productivity performance in Greater Manchester and equivalent sectors in the rest of the country – something that cannot be said for higher value industries. In short, the city region's low productivity sectors are relatively competitive. Given this evidence, we believe that reducing low pay to a discussion of productivity is something of a red herring.

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<sup>68</sup> Thompson, S. and Hatfield, I.: Employee Progression in European Labour Markets, Institute for Public Policy Research, 2015

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# 5 Skills and Low Pay

**5.1** One of the loudest messages about the contemporary workplace is that skills are the source of labour market power. Amid talk of a global skills race supplanting the old arms race, skills, in alliance with attitude and initiative, are held to be not just a means of gaining a better job, but also a source of resilience against the many vicissitudes of working life in general, especially against the background of the transformation of work by technology. As the Wolf Report puts it, there is a necessity to equip “young people for a world in which their education makes a critical difference to their future lives and for an economy undergoing constant and largely unpredictable change”<sup>69</sup>. In an environment of low regulation, a diminishing role for trade unions and barriers to enforcing rights, what sources of support do people at work have? Skills are self-help.

**5.2** By extension, a popular observation on low pay is that it reflects low levels of skill. This chapter investigates the debate about skills and its relationship to the issues of low wage work. First, we examine available data that sheds some light on the skills-pay relationship, drawing on national and North West level data due to the poor quality of Labour Force Survey data at a Greater Manchester level. We also look at evidence regarding the hourglass model of labour market change and question its city regional relevance. Second, we discuss what is meant by the vexed concept of ‘skill’. Because they are measurable the focus tends to be on qualifications, but many people without qualifications can be highly skilled, while the well qualified can be poorly skilled. Finally, we touch on skills utilisation and the charge of over-qualification in the UK. As some see it, why upskill the worker when the work doesn’t need it?

## Returns to qualifications?

**5.3** To the question of whether the low paid have lower skills – or rather lower qualifications – than others who have higher pay, the answer is a qualified ‘yes’. The chart below shows average hourly pay by qualification level at a national level<sup>70</sup>. In general, and with some exceptions (particularly at lower qualification levels), median wages rise by qualification level.

**5.4** As this data is a snapshot taken at a certain point in time, it ignores the effects of qualifications over a longer time period, as qualifications interact with experience and other matters to help shape wage levels; other research analyses this question which we discuss below. Nevertheless, using a linear regression model, it is clear that qualification level does appear to affect pay. A regression found that the factors that influenced pay were qualification, area of residence, gender, whether a person worked for an employment agency and whether they were on a zero hours contract. It was not possible to state with confidence whether qualifications outweighed these other issues in significance for determining low pay.

**5.5** Returning to the exceptions, the chart suggests a person with a level 2 qualification cannot expect to earn more from their qualifications than someone whose highest qualification is level 1. It is also worth noting that gains in hourly pay across the lower levels of the qualifications spectrum are often extremely modest and may provide inadequate incentives on their own for skills development. These types of qualification offer poor illustrations of the value of qualification attainment.

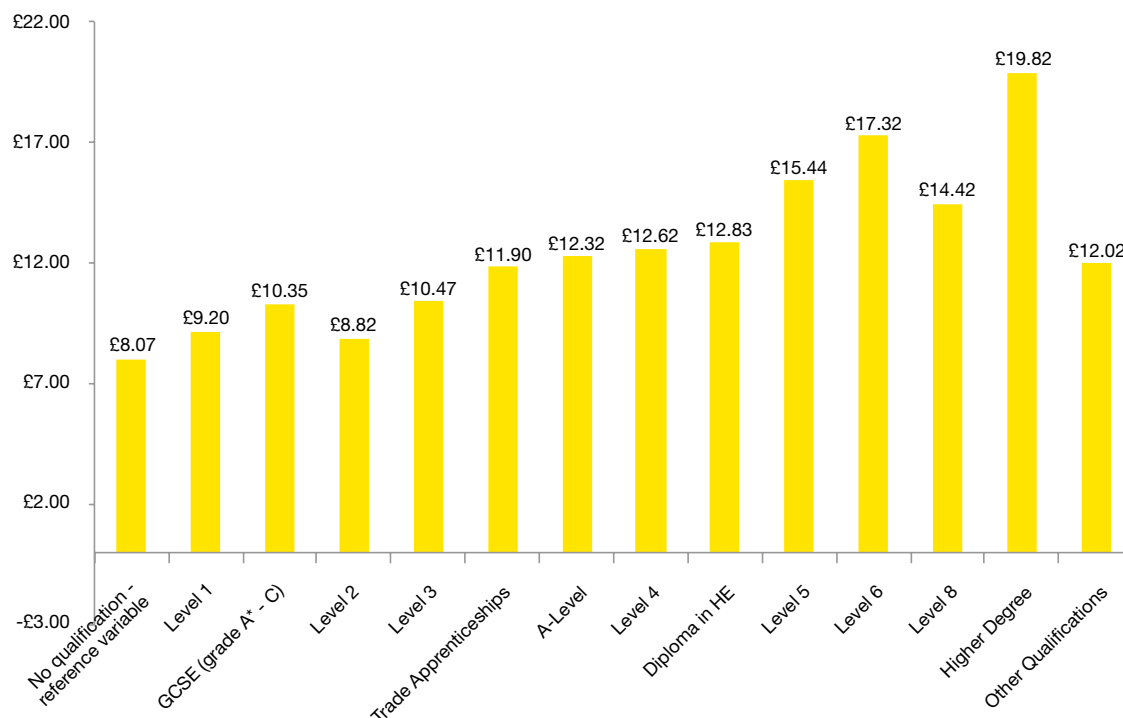
**5.6** Despite many years of support for the rhetoric of ‘parity of esteem’ the labour market judges academic qualifications to be of higher value than their theoretically equivalent vocational counterparts. For example, the gap between academic GCSEs and a vocational level 3 is only 12p an hour, while A-levels attract higher median hourly pay than a vocational level 3 which is supposed to be of the same level, albeit more practically applied. Meanwhile, the academically highly significant distance between possessing no qualifications and A-levels is apparently ‘worth’ the wage equivalent of £3.25 an hour. The wage data appears to emphasise the high labour market value of a university education, but obviously, as the chart uses averages it will mask very substantial dispersion in wage effects among graduates and others.

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<sup>69</sup> Review of Vocational Education – The Wolf Report, Department for Education/Department for Business, Innovation and Skills, March 2011, p31

<sup>70</sup> Data is not sufficiently robust at a Greater Manchester level. In this chapter we use LFS data at a national and North West level due to poor quality data more locally.

**Figure 17: Average hourly pay by level of highest qualification held**



Source: Labour Force Survey

**5.7** The finding regarding lower returns at level 2 has been well established through other research, but it remains counterintuitive and somewhat controversial. The Wolf Report into vocational education criticised the weak labour market currency of many lower level vocational qualifications, while reinforcing the message about the value of apprenticeships and the centrality of English and maths across many different lines of work. The report notes: “Occupationally specific level 2 vocational awards (NVQs) generally offer poor or even negative returns, and are of particularly low value to males who obtain them in college or on public training schemes, and whose wages are on average 12% or 23% lower than those of matched contemporaries who are ‘less’ qualified.”<sup>71</sup>

**5.8** Meanwhile, also in line with our findings, apprenticeships have been widely endorsed as valuable not just for improving employment prospects, but also for having positive wage effects, especially at advanced level<sup>72</sup>. The data above shows that trade apprenticeships are far superior to other vocational pathways to skills development in terms of delivering wage gains – an important finding as apprenticeships are often the focus of local economic development strategies.

**5.9** However, there is an important distinction between those who undertake a qualification, but do not fully achieve it and those who do. For example, research has highlighted the statistically significant difference (of between 2.5% and 5%) between full achievers and those who do not fully achieve at level 2 and at level 3<sup>73</sup>. And in addition, there is substantial variation in the type of qualification held; for example City and Guilds qualifications tend to prove more valuable than NVQs<sup>74</sup>.

<sup>71</sup> Review of Vocational Education – The Wolf Report, Department for Education/Department for Business, Innovation and Skills, March 2011, p31. However, the jury remains out on this point. For example, using matched education (ILR) and salary data (from HMRC), Peter Urwin and colleagues demonstrate strong returns at level 2. See Further Education, Social Mobility, Skills and Second Chances, Centre for Employment Research, November 2015

<sup>72</sup> What Works Centre, Review of Apprenticeships, September 2015

<sup>73</sup> Buscha, F., Urwin, P., Thomson, D., Bibby, D., Knight, T., Speckesser, S., Estimating the Labour Market Returns to Qualification gained in English Further Education Using the ILR, Department for Business, Innovation and Skills, Research Paper, 13/849, April 2013

<sup>74</sup> Department for Business, Innovation and Skills, Returns to Intermediate and Low Level Vocational Qualifications, Research Paper 53, Sept 2011

**5.10** Other research also supports the significant advantage of holding a degree. One report found degree holders had a 27% advantage overall compared to the possession of two or more A Levels<sup>75</sup>, with women having a marginally higher return than men. The value of degrees appears to have held up well despite the expansion of higher education in recent decades, suggesting that demand and supply are not demonstrably out of balance.

**5.11** Although the debate about qualifications is typically carried out using references to ‘levels’ as if these were wholly standardized and universally accepted ‘facts’ about a taxonomy of learning difficulty. But skills levels are mutable and opaque and are used more for the convenience of the education and skills establishment than employers. What constitutes a ‘level 2’ in particular tends to be subject to revisions. According to Lorna Unwin, a vocational education academic, “there is only one real level 2: English and Maths A\*-C”.<sup>76</sup>

**5.12** The Low Pay Commission also endorses this picture of a qualifications hierarchy in pay, using national level LFS data. Those without qualifications constitute 19.8% of jobs paid at the level of the National Minimum Wage. Those whose highest qualification is a level 2 make up 11.5%, while those with a level 3 make up 8.9%. Workers with an apprenticeship constitute 5.8% of jobs paid the NMW.<sup>77</sup>

**5.13** The returns to qualifications remain highly gendered with gender pay gaps across all qualification levels. Among young people the gap peaks around level 3 or 4 – A level, and foundation degrees and certifications – but tends to be lower both at low qualification levels and at degree level. Among older people the gaps are larger and are dispersed across many different qualification levels. Overall, the most substantial pay gap among people from their late thirties to retirement age is among the holders of A level or equivalent intermediate qualification levels.

**Table 14: Gender pay gaps by qualification, 2014**

	20-35	36-65
Gross hourly pay in main job – median (Jan-Dec 2014)	Difference Female & Male	Difference Female & Male
Degree or equivalent	-12%	-19%
Higher education	-20%	-22%
GCE, A-level or equivalent	-17%	-26%
GCSE grades A*-C or equivalent	-12%	-23%
Other qualifications	-12%	-20%
No qualification	-10%	-18%

Source: LFS

<sup>75</sup> Conlon, G., The Returns to Higher Education Qualifications, Research Paper Number 45, Department of Business, Innovation and Skills

<sup>76</sup> See Wolf Review, p32

<sup>77</sup> The National Minimum Wage Report 2015, Low Pay Commission, Department of Business, Innovation and Skills, 2015

**5.14** As noted in the previous chapter, the low paid occupations are concentrated in the three broad occupational groups – ‘elementary occupations’, ‘sales and customer service’ and ‘caring and leisure’. Over a third of the people working in these occupations earn less than the low pay threshold. In addition, low pay is also a significant issue for many people who work in the ‘process, plant and machine operatives’ category – typically manufacturing workers - in Greater Manchester (but wages in these types of process jobs are higher elsewhere). Are these large occupational groups also ‘low skilled’?

**5.15** The table below shows the qualification levels of different occupational groups at a North West level. There are no standard definitions of a ‘low skilled’ occupation, but a common rule-of-thumb among socio-economic researchers is to take the bottom three (and sometimes the bottom four) broad occupational groups (numbers 7-9 and sometimes 6) and label these as ‘low skilled’.

**5.16** In the case of two of the occupational groups – ‘elementary occupations’ and ‘sales, customer service and other services’ - it seems to us to be justified to categorise these as ‘low skilled’: a majority have a highest qualification level of GCSE A-C or below. The ‘process, plant and machine operatives’ are also legitimately labelled low skilled. However, ‘caring, leisure and other service occupations’ stands out as being a sector that is low paid, but not necessarily low skilled.

**5.17** As the table below (see table 15) makes clear<sup>78</sup> nearly two thirds or 64.5% of the employees in ‘caring, leisure and other service occupations’ (SOC code 6) in the North West are either educated to degree level, hold other higher education qualifications or have a level 3 equivalent qualification (13.4% degree or equivalent, 11.3% higher education, 39.8% level 3). This contrasts strongly with the (better paid) ‘process, plant and machine operatives’ (SOC code 8), where only one in four (27.4%) hold level 3 or above qualifications. The ‘care and leisure workers’ have a higher proportion of level 3 or above qualifications than the ‘administrative and secretarial workers’ (SOC code 4). One should bear in mind, though, that there are relatively fewer employees than in the secretarial and administrative group who are educated to degree level (a level 6 qualification), as the majority of carers and leisure workers hold level 3 and 4 qualifications.

**Table 15: Qualification level by broad occupational group**

Highest qualification (detailed grouping)	Degree or equivalent	Higher education	GCE, A-level or equivalent	GCSE grades A*-C or equivalent	Other qualifications	No qualification	Did not know
1 ‘Managers, Directors and Senior Officials’	34.8%	13.8%	23.0%	18.3%	6.2%	2.9%	1.0%
2 ‘Professional Occupations’	72.2%	12.6%	8.7%	4.9%	1.1%	0.1%	0.3%
3 ‘Associate Professional and Technical Occupations’	39.2%	12.7%	22.5%	19.9%	2.9%	1.4%	1.3%
4 ‘Administrative and Secretarial Occupations’	21.0%	8.1%	27.3%	35.3%	4.9%	1.9%	1.5%
5 ‘Skilled Trades Occupations’	4.9%	6.6%	46.5%	24.1%	8.6%	8.0%	1.1%
6 ‘Caring, Leisure and Other Service Occupations’	13.4%	11.3%	39.8%	24.0%	7.6%	3.3%	0.5%
7 ‘Sales and Customer Service Occupations’	13.7%	4.4%	29.7%	32.7%	8.4%	8.6%	2.5%
8 ‘Process, Plant and Machine Operatives’	5.9%	4.4%	17.1%	33.2%	25.7%	11.4%	2.4%
9 ‘Elementary Occupations’	8.1%	3.3%	23.9%	31.4%	17.1%	15.8%	0.5%
<b>Total</b>	<b>28.7%</b>	<b>9.1%</b>	<b>25.1%</b>	<b>22.8%</b>	<b>7.9%</b>	<b>5.2%</b>	<b>1.1%</b>

Source: LFS

<sup>78</sup> ONS (2014): Quarterly Labour Force Survey, July - September, 2014

**5.18** There are further reasons why we think the caring and leisure occupations belong in the medium skill rather than low skill bracket. Many of these occupations require minimum entry level 2 qualifications, as well as training progression towards a level 3 qualification while on the jobs (for example, teaching assistants<sup>79</sup>, nursery nurses<sup>80</sup>, veterinary nurses<sup>81</sup> or dental nurses<sup>82</sup>).

**5.19** For these types of worker there appears to be a discrepancy between their skill level – which, in theory, would imply they should earn rather more – and their pay level. Wider factors may help explain the discrepancy. Leisure and care occupations are also the occupational grouping with the highest proportion of women. Women constitute 81.7% of employees in the sector in the North West. Additionally, almost half of the workers in care and leisure occupations workers (46.6%) are part-time employees. And only one in six (7.8%) of the part time employees in the sector stated that part-time work was involuntary, as they were not able to secure a full-time position: most workers in the sector want to be part time. One of the reasons could be that the employees in the caring and leisure sector are among the most likely of all the occupational groups to have dependent children younger than 19. Around 47% have children, compared to the average of 42% across all employees.

**5.20** The caring and leisure workers represent just under 10% of the labour force and account for one in three low paid workers. They are low paid not on account of their skill level, but due to other cultural, market and personal factors. We might characterise the relationship between skills and pay as broadly robust, but with some profound caveats. Where work is ‘people-facing’, involves giving care and developing health and well-being, it is likely to be undervalued relative to qualification level.

## Polarization, the hourglass and the skills-pay mismatch

**5.21** The notion that labour markets in the UK are ‘polarizing’ with more high skilled jobs and more low skilled jobs, but fewer jobs in the middle of the skills spectrum, has become such a commonplace as to be almost received wisdom. The pattern is sometimes referred to through the metaphor of an ‘hourglass’, although the economists Maarten Goos and Alan Manning prefer the language of growing numbers of ‘lovely’ and ‘lousy’ jobs<sup>83</sup>. Some also link the high skill and the low skill elements together: the expansion of a well-educated, but time-poor workforce increases the need for a range of services involving caring, leisure and ‘lifestyle support’ at lower skill levels<sup>84</sup>. The decline among ‘middling’ kinds of work may in theory make it harder for workers to progress up the skills hierarchy and into higher skilled and better paying work, effectively constraining their opportunities. It may also be a toxic source of rising social inequality. In the light of the pay and skill mismatch in some areas of the low paying occupations (especially ‘care, leisure and other services’) does the hourglass metaphor work well with what has occurred in the North West?

**5.22** In our view, and in the light of our positioning of ‘care and leisure’ as a medium skilled occupational group, it does not. Certainly, there has been a decline in medium skilled work. Intermediate skilled work is hollowing out in the North West as it is elsewhere. But it is important to distinguish between skills and pay. The fall in medium skilled work is not as sharp as the fall in medium paid work, if judgements are made at the level of broad occupational groups. The strongest growth trend appears to be in ‘high skilled’ work which has seen a 3.3% increase overall in a decade. Yet low skilled work has also declined as a share of the overall workforce – at the same time as low paying work has grown. The hourglass metaphor is a fairly gross oversimplification of the evidence of labour market change once skill and pay are separated, as the chart below shows. In short, this confirms low paying occupations are indeed growing (albeit not as forcefully as high paying and highly skilled occupations); and that skill levels in the bottom half of the labour market do not precisely determine pay levels. The implication is that additional skill inputs for some occupational groups may not significantly help to lift pay levels.

<sup>79</sup> National career Service (2015): <https://nationalcareersservice.direct.gov.uk/advice/planning/jobprofiles/Pages/teachingassistant.aspx>

<sup>80</sup> National Careers Service (2015): <https://nationalcareersservice.direct.gov.uk/advice/planning/jobprofiles/Pages/nurseryworker.aspx>

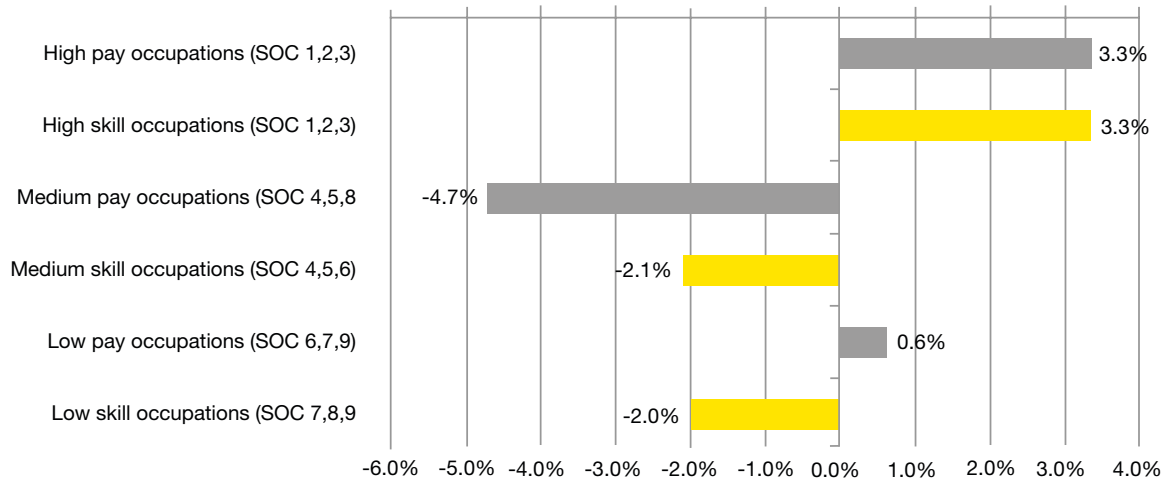
<sup>81</sup> National Careers Service (2015): <https://nationalcareersservice.direct.gov.uk/advice/planning/jobprofiles/Pages/veterinarynurse.aspx>

<sup>82</sup> National Careers Service <https://nationalcareersservice.direct.gov.uk/advice/planning/jobprofiles/Pages/dentalnurse.aspx>

<sup>83</sup> Manning, A. and Goos, M. Lousy and Lovely jobs: the Rising Polarization of Work in Britain, LSE Working Paper, 2003

<sup>84</sup> See, for example, Clayton N., Williams, M. and Howell, A., Unequal Opportunity: How Jobs are Changing in Cities, Centre for Cities, September 2014; See also Autor, D., The Polarization of Job Opportunities in the U.S. Labor Market: Implications for Employment and Earnings, Centre for American Progress, The Hamilton Project, April, 2010, p2

**Figure 18: Change in occupations, by pay and skill, 2004-2013**



Source: LFS

**5.23** In summary, the situation of the North West corresponds to one of increasing skill levels among the population. There have been falls in the numbers of workers operating at lower skill levels. Regarding pay, however, there has been a growth of low paid work, alongside a growth of high paid work.

## What is a skill?

**5.24** So far in this chapter, we have discussed aspects of the interaction of pay and skills, as proxied by qualifications. But how valid is this proxy?

**5.25** To ask 'what is a skill' is to enter a venerable philosophical debate about the distinguishing characteristics of human beings and what it is that separates them from other animals; contrasts such as that between 'skill' and 'instinct' are sometimes invoked, as is the inseparable bond between skill and the origins of technology. "Man is a tool making animal," as Benjamin Franklin put it.

**5.26** Francis Green, a leading academic on skills, defines a skill through an acronym: PES<sup>85</sup>. Skills are personal qualities with three components:

- Productive: using skills at work are productive of value
- Expandable: skills are enhanced by training and development
- Social: skills are socially determined

**5.27** Skills are properties belonging to individuals. They can be employed to produce added value in production and services and can be fostered through both formal and informal learning. Similarly, the acquisition, utilisation and valuation of skills are determined by a social process, whereby skills formation choices (by prospective workers, employers and training providers/the state) can be negatively affected by informational limitations. Green goes on to link skills to a closely related concept in labour economics – that of autonomy. As the complexity of work increases it implies greater use of employee discretion. In turn, higher discretion (or lower levels of monitoring and direction from the perspective of employers) demands higher skills.

**5.28** In the UK's market-oriented system of National Vocational Qualifications, the term 'skill' is used to narrowly refer to whether a worker is able to perform a specific set of tasks<sup>86</sup>. This is mirrored by the different meanings that economics and vocational and educational psychology attribute to skills. While economics is mostly concerned with the market valuation of skills and their implications for distribution and growth, psychology's focus is on the 'generation and function of competence'<sup>87</sup>. The latter can be regarded as more expansionary and implies a focus on the system of skills formation.

<sup>85</sup> Green, F: Skills and Skilled Work: An Economic and Social Analysis, 2013. Oxford University Press

<sup>86</sup> Green, F: Skills and Skilled Work: An Economic and Social Analysis, 2013. Oxford University Press

<sup>87</sup> Green, F: Skills and Skilled Work: An Economic and Social Analysis, 2013. Oxford University Press

**5.29** Skills are inherently difficult to measure and therefore to assess. This makes the skills formation system difficult for workers to navigate when making a decision about training courses and for employers when making recruitment decisions. Hiring an employee is a classic example of an information asymmetry as the skill levels and other properties (perseverance, loyalty, self-discipline) of the worker are unobservable characteristics. The worker will have better information about his or her own properties than the prospective employer. In order to mitigate for the challenge of accessing information on the unobservable characteristics, the employer will use proxies for observable skills – generally qualifications – as a signalling mechanism for skills.

**5.30** But the question inevitably arises as to whether these formal qualifications actually express the skill levels they are supposed to – which returns us to the question about the value of and returns to qualifications at lower labour market levels.

**5.31** An employer is not interested in a qualification in itself but only in its assurance. It shows that the prospective worker has successfully participated in a process of skills formation that in turn is expected to be related to the tasks that he or she has to perform in the work environment. And yet “neither the supply of skill formation services, nor the demand for learning can be readily observed directly”<sup>88</sup>. Furthermore, employers are not always looking for skills which align in a one-to-one way with qualifications: much of the time they use qualifications as signals of general rather than highly specific skills<sup>89</sup>. They also necessarily rely on those with which they are familiar, and which they can interpret, either in terms of content or as an indicator of someone’s likely relative ability. In the context of a vocational education landscape that is subject to frequent change this can be a particular problem.

**5.32** The issue is complicated by the contention that employers are not always as interested in skill per se, as they are in qualities such as ‘attitude’, ‘initiative’, ‘enthusiasm’, ‘the ability to think on one’s feet’ or the knack of relating to others – a point often made forcefully in respect of the low pay sectors. These kind of ‘soft’, personality-related factors are difficult to learn whereas ‘hard’ skills are often relatively cheap to train for. But the attempt to re-label as ‘skills’ what are, in effect, a collection of personal attributes is not without its problems. Is communication ability really ‘a skill’? To

argue so is not obviously more persuasive than arguing that physical strength amounts to a skill for a miner or that ‘looking good’ or ‘fitness’ is a skill in a nightclub, gym or department store. Caroline Lloyd and Jonathan Payne claim the inclusion of personal and interpersonal capabilities into our conception of skills fuels claims that, “we are witnessing a general trend towards universal up-skilling in a ‘knowledge-driven economy’, while also allowing a convenient veil to be drawn over the dull, monotonous reality of much service sector work”.<sup>90</sup>

**5.33** Data from the Organisation for Economic Cooperation and Development’s (OECD’s) mammoth study known as Programme for the International Assessment of Adult Competencies<sup>91</sup> (PIAAC) suggests that the UK, far more than other countries, has vastly expanded its profile of formal qualifications in circulation, but without necessarily improving its underlying skills. The study is the largest of its kind with a sample of 166,000 respondents in 24 advanced economies. It measured skills through standardised tests in literacy, numeracy and problem solving. England was the only country in the whole study in which the younger generation (16-24 year olds) showed weaker reading and maths proficiency than the 55-65 year old age group. The contrast is particularly stark in comparison to the general pattern exhibited by most other countries where the youngest cohort exhibits stronger proficiency in literacy, maths or ICT problem solving skills than older people aged between 55 and 65.

**5.34** Over the time period, in all developed countries forming part of the sample, the share of the population having attended (upper) secondary and tertiary education has increased significantly. In the 1971/72 school year only 28% of the cohort of 17 year olds in England and Wales were in full-time education (those who are now 60-61 years old). This rose to 71% in 2009/10<sup>92</sup>. This was mirrored by the increase in the share of students gaining formal qualifications – the share of those achieving 5+ GCE ‘O’ level passes/GCSE grades A\*-C or equivalent increased in England and Wales from 22.1% in 1970/71 to 81.1% in 2011/12<sup>93</sup>. More recently, in England participation in higher education has increased from 30% in the late 1990s to 38% in 2012 of the relevant cohort<sup>94</sup>. Yet this expansion of education provision and formal qualifications seems, however, not to have translated into greater literacy and numeracy skills. Arguably, younger people are entering an extremely demanding labour market worse prepared than people who are retiring.

<sup>88</sup> Green, F: Skills and Skilled Work: An Economic and Social Analysis, 2013. Oxford University Press

<sup>89</sup> Wolf Report, *ibid*, p32

<sup>90</sup> Caroline Lloyd and Jonathan Payne, What is a skilled job? Exploring worker perceptions of skill in two UK call centres, SKOPE Research Paper No 81, July 2008, p21

<sup>91</sup> OECD: OECD Skills Outlook 2013. First Results from the Survey of Adult Skills, 2013

<sup>92</sup> House of Commons Library: Education: Historical statistics. November 2012, SN/SG/4252

<sup>93</sup> House of Commons Library: Education: Historical statistics. November 2012, SN/SG/4252

<sup>94</sup> Higher Education Funding Council: Trends in young participation in higher education. October 2013



**5.35** In contrast to other advanced economies, formal qualification levels seem to not be very closely related to the underlying skills they are supposed to express. Taken together with the finding about a lack of progress in skills over time, this points towards potential shortcomings in the education system. “The data... raise questions about the relevance and quality of formal education in some countries... This is important because the level and type of formal learning completed, and the qualifications earned, are indirectly related to individuals’ proficiency in information processing skills: they determine access to the jobs and further education and training that could help individuals maintain and develop their skills.”<sup>95</sup> In short, qualifications in the UK offer relatively weak skills signals.

**5.36** What seems to matter more than formal qualifications are information processing skills. Following research undertaken by Hanushek and Woessman<sup>96</sup>, academic Francis Green assumes that cognitive abilities - essentially the ability to process information - are much more important than a formal qualification from a school, university or college. Information processing skills form the basis for acquiring occupation specific skills or functional skills later in life and also enable people to

cope better with technological and workplace change in a typical working life of more than 40 years. “Cognitive skills... have a more impressive effect than education per se. Studies that include measures of the cognitive skills of the population find that educational attainment is only a loose indicator of a nation’s skill.”<sup>97</sup>

**5.37** Therefore, one possibility why wages across the lower levels of the labour market do not track qualification level consistently is not just because the qualifications lack labour market currency, but because their relationship to skill is in doubt. Rather than the conventional approach of analyzing pay by qualification level, is it possible to analyse ‘skill’ by wage level?

**5.38** The PIAAC study also produced data for the regions in England. The table below shows educational competence mean scores across the three areas of literacy, numeracy and ICT problem solving. It demonstrates that across all three areas the North West lags the proficiency of England as a whole, especially in literacy (5 points under the England norm). However, the gaps, are not as large as in some other areas, in particular the North East and West Midlands (for example, the North East has a 15 point lag in numeracy scores).

**Table 16: Average Scores in Literacy, Numeracy and Problem Solving by English Region, 2012**

Region	Literacy	Numeracy	Problem solving
South East	282	274	286
Eastern	279	269	289
South West	279	270	284
East Midlands	274	263	280
London	270	256	282
Yorkshire and Humberside	269	258	275
North West (including Merseyside)	268	258	279
West Midlands	264	251	271
North East	259	247	268
<b>ENGLAND (overall)</b>	<b>273</b>	<b>262</b>	<b>281</b>

Source: OECD, PIAAC.

<sup>95</sup> OECD, op cit

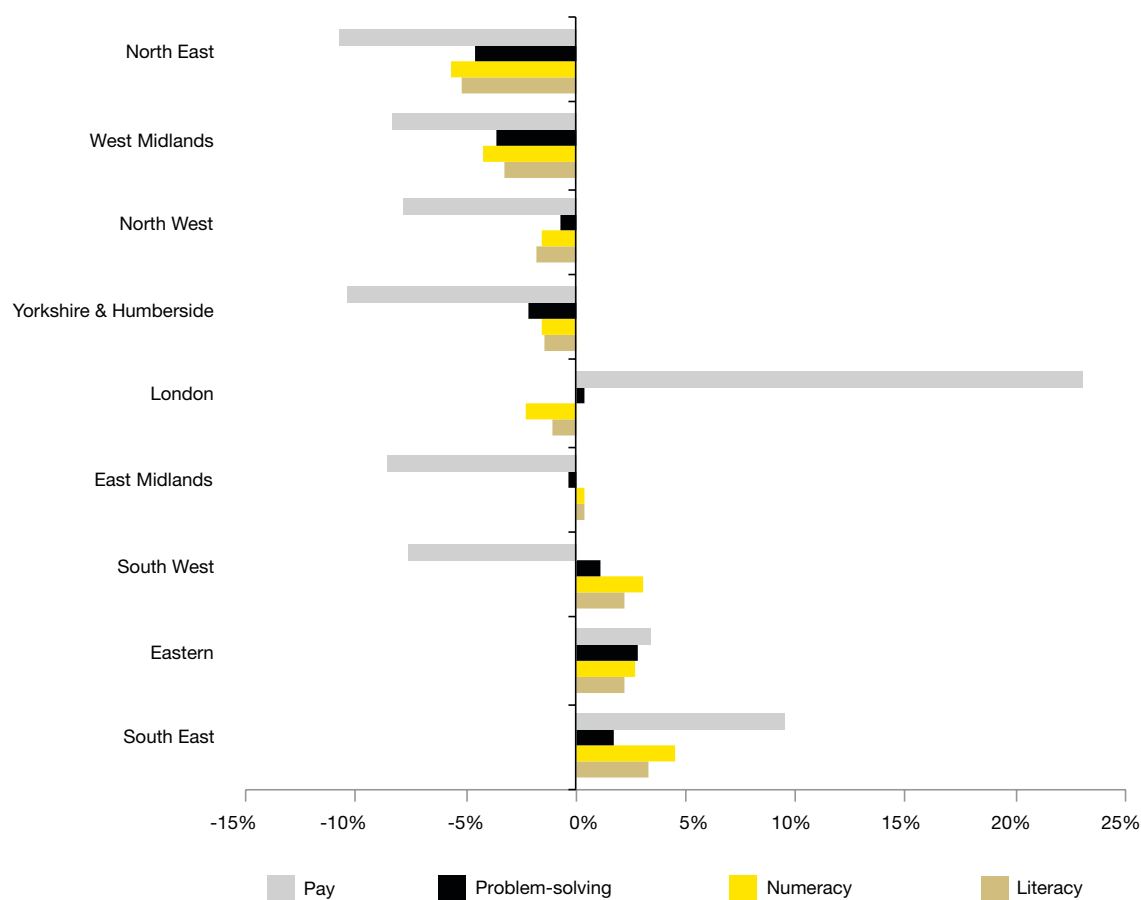
<sup>96</sup> Hanushek, E. and Woessman, L., The Economics of Differences in Educational Achievement, NBER Working Paper, 2010

<sup>97</sup> Green, F., Skills and Skilled Work: An Economic and Social Analysis, Oxford University Press, 2013

**5.39** The PIAAC study allows us to improve on qualification-based analyses and instead look at whether actual 'skill' (provided we trust the OECD's standardised tests) has an impact on pay. Do we have evidence that skills or educational attainment are associated with pay?

**5.40** The chart below plots the percentage difference of each English region from the national average for hourly wages, alongside how well the region fared in ICT problem solving, numeracy and literacy in PIAAC mean scores. As can be seen, the results suggest there is (in our view) a reasonably strong degree of correspondence between skill and pay. In most cases, where the information processing skills are recorded above the average, average wages are also higher (the only region exhibiting higher than average scores in skills while falling below the national average hourly wage is the South West. The results for London, however, are inconclusive. While it has by far the largest average pay (23.1% higher than the national average), its information processing skills are merely average – arguably a simple reflection on the fact that pay is higher in the capital.

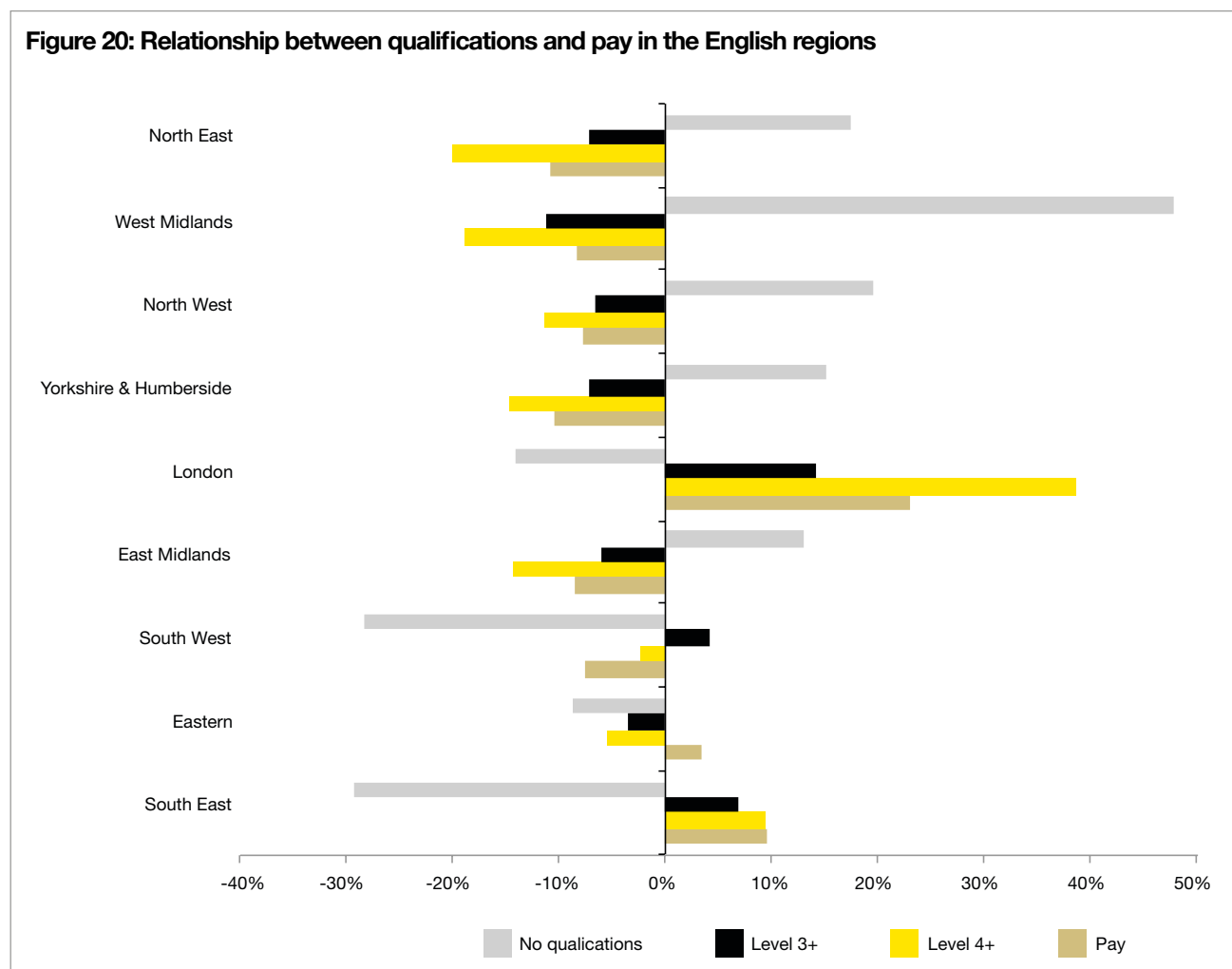
**5.41 Figure 19: Relationship between wage and skill across English regions**



Source: New Economy calculations, based on OECD (PIAAC) and ONS (ASHE) data

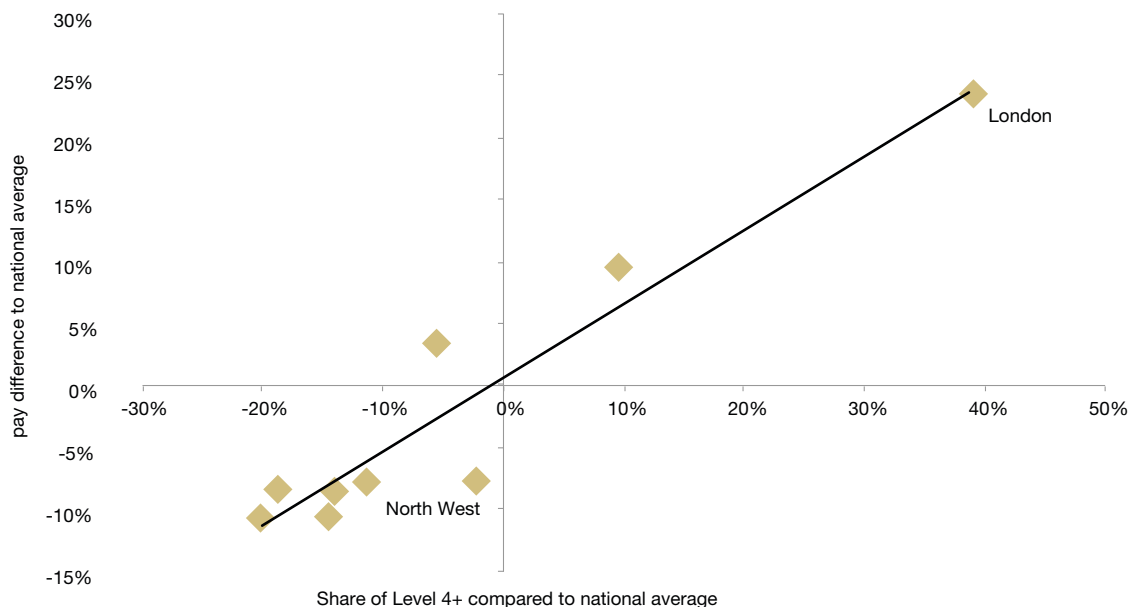
**5.42** The chart below performs the same exercise, but this time swapping the measure of skills for formal qualifications. It plots the share of people without any qualifications, with level 3 or higher, and with level 4 (for example, certificate of higher education) or higher as a proportion of the region's population, as well as regional pay differentials. The chart shows that pay is higher in regions with an above average concentration of residents holding level 3+ or level 4+ qualifications. At the same time, the share of people with no qualifications is associated with lower average wages. Compared to information processing skills, the relationship between formal qualifications and hourly pay appears stronger. While it is not feasible to determine the reasons from our data, it is possible that formal qualifications act as a more appropriate signaling device to employers than unobserved characteristics of prospective employees such as their information processing skills. In the absence of an employer's ability to directly test the information processing skills of a prospective employee, their formal qualification is generally considered as an appropriate proxy.

**5.43** The best fit can be observed between the difference between the region's resident's share of level 4+ qualifications and the national average, and pay, as the chart below shows (Figure 21). This could be interpreted as indicating robust returns to higher education, as discussed above. While data limitations (only nine cases) preclude using appropriate statistical data analysis methods, the association between higher education and regional wage data does appear to be particularly strong.



Source: New Economy calculations, based on OECD (PIAAC) and ONS (ASHE) data

**Figure 21: Relationship between share of population with level 4+ qualifications and pay**



Source: New Economy calculations, based on OECD (PIAAC) and ONS (ASHE) data

## What is the evidence around over-qualification?

**5.44** Formal qualification levels have been rising rapidly over recent decades. Yet the contention that increasing formal qualifications enhances economic performance logically depends on how employers seek to use those skills in practice. It is not obvious that improving skills supply on its own necessarily enhances productivity without parallel effort aimed at ensuring jobs are designed in such ways that skills can be put to productive use.

**5.45** According to the Skills and Employment Survey series (SES)<sup>99</sup>, the demand for qualifications has been moving upwards since 1986 with a particularly sharp increase between 2006 and 2012. Around a quarter of jobs now require a degree. Meanwhile, jobs without any qualification requirements have been trending down: 38% of jobs did not require any qualification in 1986; by 2006, the figure had decreased to 28%; and by 2012 to 23%. Even so, that figure is worth noting. A little under a quarter of jobs in the UK do not require any qualifications.

**5.46** But what of the contention that one of the by-products of this growth in qualification requirements by employers is increasing levels of 'over-qualification'? The charge has been common in recent years and most typically focusses on graduates. (We lack evidence specifically about over-qualification among relatively low skilled workers.)

**5.47** For example, in 2006, a report using the SES found a third of graduates were overqualified, a figure that the authors said had increased by 50% in the previous 20 years, with particularly rapid growth in the first decade of the 21st century<sup>100</sup>. As what is meant by 'a graduate' can be varied, it follows that there has been some dispersion in graduate experiences. Francis Green and Yu Zhu report increased dispersion amongst graduate pay and career prospects, which they attribute to over-qualification. The argument runs that the increase in the supply of graduates has merely devalued their degrees, rather than created more 'lovely' jobs. Research has found that overqualified graduates suffer a pay penalty of between 10% and 25%<sup>101</sup>. Related to this argument has been a debate about the term 'graduate job'.

<sup>99</sup> Information on this survey is available at <http://www.cardiff.ac.uk/research/projects/view/117804-skills-and-employment-survey-2012>

<sup>100</sup> Felstead, A., Gallie, D., Green, F., Zhou, Y., Skills At Work, 1986-2006, ESRC/SKOPE, 2007

<sup>101</sup> Francis Green and Yu Zhu, Overqualification, Job Dissatisfaction, and Increasing Dispersion in the Returns to Graduate Education, University of Oxford, Oxford Economic Papers, 2010, p9

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For example, in a study of two major retail organisations the work carried out by ‘managers’ (typically graduates) was found to be heavily prescribed: stock levels, ordering, product ranges, store layouts, pricing, special offers and staff policies were all determined by head office. Managers were also monitored to ensure they met a number of demanding performance targets, which they had very little if any control over. Far from ‘entrepreneurial visionaries’, they were more like ‘links in a chain with little real influence over policies and procedures’ despite the fact that the retail organisations concerned stressed managerial leadership and ‘the importance of people’ as crucial factors in their competitive advantage.<sup>102</sup>

**5.48** Yet the most recent evidence from the SES indicates a decline in levels of over-qualification (defined as entry requirements which are not ‘essential’ to do the job)<sup>103</sup>. Levels of over-qualification have thus gone into reverse since 2006 having risen in the twenty years prior to that point. But despite the trend, over-qualification remains significant with a third of respondents nationally reckoning their skills (or qualifications) are not put to productive use at work.

**5.49** However, a criticism of almost all the research on over-qualification is that it is based on individuals reporting on themselves. They may be ‘esteem biased’ when it comes to analyzing their skill levels (or perhaps levels of boredom in their jobs). A source that avoids this pitfall is PIAAC. It claims, according to its tests, that self-reported over-qualification (which is high in the UK) is not born out by over-skilling. When workers’ proficiency in numeracy and literacy was compared to respective job positions (and their proficiency requirements), researchers found that “the incidence of over-skilling (when a worker’s proficiency in literacy is above the minimum required for the job) in England and Northern Ireland is actually low, and below the average observed among participating countries. In fact, fewer than 10% of workers are over-skilled, based on the OECD measure of skills mismatch in literacy.”<sup>104</sup> This would imply that the narrative of mass over-qualification among UK workers (or of the 30% who self-reported their over-qualification) could be regarded as questionable. While it might hold true in terms of formal qualification and assessed through the self-reports of workers, self-reports are open to question.

**5.50** It would be rash to dismiss the literature regarding over-qualification on the basis of a single study (albeit a huge one), especially, as noted, when we lack insight into over-qualification perceptions among the low paid. There will always be those who do not find work that is commensurate with their abilities. Here we can do no more than note that the jury is clearly still out on this point.

## Conclusion

**5.51** In general, qualifications clearly have an impact on pay levels. Especially relevant for this study on low pay, however, is the finding that at the lower levels of the skills spectrum, qualifications appear to have relatively modest links with wage levels – and in some specific cases (vocational level 2), mysteriously negative returns. Qualifications are one of several factors that influence pay. Yet it is important to remember that the connection between qualifications and the underlying skills they signify is weak by international standards. In the UK, qualifications have been growing – but ‘skills’ (as measured by standardised proficiency tests) have not followed the same growth trajectory. In as far as we can judge the relationship between ‘skill’ and pay (using the OECD’s PIAAC data), it also appears to correlate well with pay levels. Unfortunately, although we lack data on the specific levels of over-qualification of the low paid, it is quite possible the situation of possessing skills that the labour market cannot find use for is a relatively common experience, affecting perhaps a third of workers. Yet due to the demanding nature of work, over-qualification has been affecting fewer people than in previous eras.

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<sup>102</sup> Irena Grugulis, Ödül Bozkurt and Jeremy Clegg, op cit, p1

<sup>103</sup> Felstead, et al, 2012, ibid

ESRC Centre for Learning and Life Chances in Knowledge Economies and Societies (LLAKES), 2013

<sup>104</sup> PIAAC, ibid, p5

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## 6 Progression and the Low Wage Labour Market

- 6.1** Recognition of the scale of low pay in recent years has brought with it a rise of interest in the subject of labour market progression. One of the articles of faith concerning the UK's flexible labour market model is that it enables relatively easy transitions for employers and employees, which for low paid workers can mean the possibility of moving up out of low pay provided the requisite skills, attitude and initiative are held. To some extent, the possibility of progression may represent something of a 'plea in mitigation' concerning the levels low pay: a dynamic, flexible labour market is the trade-off for extensive low pay.
- 6.2** To date, the literature on progression is relatively modest with no more than a handful of reports available on the subject – and none that we could find on progression within local labour markets. To fill this gap, New Economy commissioned its own research on progression within Greater Manchester and this research is available in the report, *Low Pay and Progression in Greater Manchester*, published alongside this report. In this chapter we summarise some of the key findings and insights of that report.
- 6.3** The research uses pooled Labour Force Survey datasets from 2011-2015 to examine a fifteen month 'window', identifying what happened to respondents over that period – how many were 'stuck', how many 'escaped' and how many declined into low paid work, and what, if any, are their distinguishing characteristics. This approach was influenced by data availability and is open to the charge that 15 months is a fairly short period of time to assess whether people are 'stuck' in their jobs. Nevertheless, the data does afford relatively precise insights into the dynamism of low paying labour markets.
- 6.4** Previous research has tended to find progression opportunities do indeed exist for a minority, but the vast majority of low paid workers are low paid for a substantial amount of time. Where there are possibilities for moving up, the jobs on offer carry relatively modest pay rises or status progression. For example, according to the Resolution Foundation, which looked at progression among low paid workers between 2001 and 2011, just one in four 'escape' low pay over that period. Of the three quarters who are 'stuck', some two thirds fluctuate around the level of the low pay threshold (two thirds of median earnings), earning sometimes above the low pay threshold and sometimes below, but without earning consistently more<sup>105</sup>. Our findings, using the shorter time period, are in line with these findings: most low paid are low paid for considerable amounts of time.
- 6.5** But 'progression' cannot be reduced to pay alone. Progression in terms of hours, contract type (for example, temp to perm) and other areas such as 'status' are also relevant. According to an IPPR report<sup>106</sup>, progression opportunities are often conditioned by labour market norms in different countries. For example, countries with large numbers of non-permanent staff offer relatively fewer opportunities for progressing to permanent contract work. Workforces, such as those of northern Europe with substantial numbers of part-timers exhibit lower levels of part-to-full-time conversion.

### Research context

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<sup>105</sup> 102 D'Arcy, C., and Hurrell, A., *Escape Plan, Understanding Who Progresses from Low Paid Work and Who Gets Stuck*, Resolution Foundation, November 2014

<sup>106</sup> IPPR, *op cit*

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**6.6** A widespread assumption is that if an employee moves up from a low paid position into a role with more responsibilities, they can expect to be getting close to, if not moving above, the low pay threshold. But qualitative research suggests that in many instances this does not actually occur. Just under half of the low paid staff the Resolution Foundation interviewed were earning within 30p of the National Minimum Wage (NMW). In most firms, an employee who remained in their role for five or ten years was unlikely to be earning significantly more than those who had started recently. For many workers, the only time they saw a wage increase was just before the NMW rose and the rise would generally be in line with the size of the NMW increase (10-20p and below the rate of inflation). The next step on the ladder was usually a supervisor position. In the eyes of most employees and managers, the step up from these basic roles to supervisory positions brought with it increased stress levels, pressures upon a person's work-life balance with demands to work longer hours and no guarantee of further progression<sup>107</sup>.

**6.7** In addition, job satisfaction exhibits a U-shaped relationship with being stuck: those who are most satisfied are more likely to be stuck.

**6.8** Some employers pay particular attention to progressing staff. McDonald's, for example, has developed a detailed prospectus of progression opportunities – outlining the responsibilities associated with each role, the skills required and the rewards associated with each step<sup>108</sup>. Thrifty car rental is also often cited by the European Commission in its analysis of skills transferability in the European Union. The company arranged opportunities for employees to move across departments within the company to learn skills not directly relevant to their role<sup>109</sup>. According to Inclusion, important drivers for progression are management and support systems; a systematic approach to HR (ie induction and appraisals which are aligned to a progression structure); spending money on training; peer support; and ensuring employees understand processes and opportunities.

**6.9** Yet there have been relatively few public programmes that aim explicitly at enhancing labour market progression. The largest of its kind has been the Employment, Retention and Advancement demonstration project (ERAD) which ran between 2003 and 2007<sup>109</sup>. The project was aimed at long-term unemployed jobseekers (New Deal 25+ customers), lone parents on Income Support, and lone parents receiving Working Tax Credits and operated through a mixture of face to face support, money for training, and cash bonuses for staying in work. An evaluation found that ERAD did produce some short-term improved retention and earnings for all groups, and that these held over the longer term for the long-term unemployed group<sup>110</sup>. However for lone parents, earning gains tended to fall back again once the support had finished. (It is also important to note that in all cases the gains were fairly modest.)

## Progression in Greater Manchester

**6.10** In Greater Manchester, 61% of those in low pay at the first observation were also below the level of two thirds of median hourly pay 15 months later. In other words, just under two thirds are 'stuck'. Some 33% increased their pay and moved above the low pay threshold during the observation window. The remainder (6%) move into worklessness.

**6.11** However, the research shows that the numbers of those who escape low pay by moving upwards is fairly evenly balanced by those who move backwards into low pay. The proportion who were in low pay at the start but moved out of it by the end (33%) were only slightly higher than those who were not in low pay at the start, but were at the end of the observation window (28%).

**6.12** So how do the escapers and decliners differ in their characteristics? Although low pay is heavily concentrated among the young, older people also appear to be prominent among the stuck. The data below divides the subjects into two groups at age 30. The group who are stuck in low pay has the lowest proportion of younger workers of all the three groups. Decliners into low pay have the closest balance between younger and older workers, while escapers are more likely to be younger than older. The differences between all three groups are not, however, large. The strongest finding is that low pay in Greater Manchester is not confined to the young<sup>111</sup>.

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<sup>107</sup> Resolution Foundation, *Escape Plan*, op cit

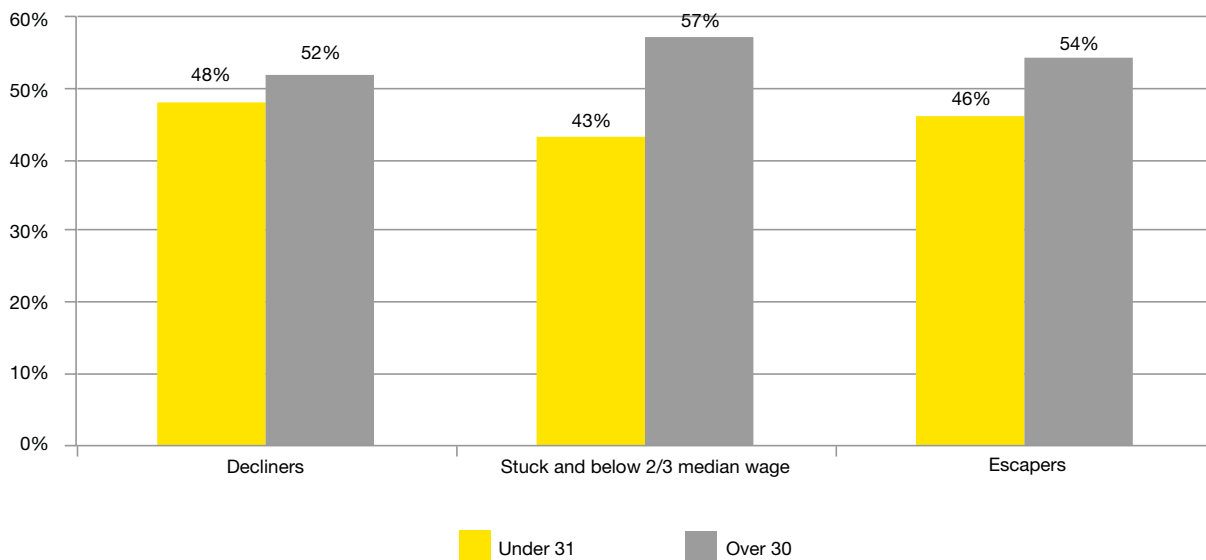
<sup>108</sup> McDonald's 2012 Prospectus

<sup>109</sup> European Commission (2011) *Transferability of Skills across Economic Sectors: Role and Importance for Employment at European Level*

<sup>110</sup> Hendra, R. et al. (2011) *Breaking the low-pay, no-pay cycle: Final evidence from the UK Employment Retention and Advancement (ERA) demonstration*, Department for Work and Pensions Research Report No.765

<sup>111</sup>This point is born out by our analysis of age and pay; see figure 11

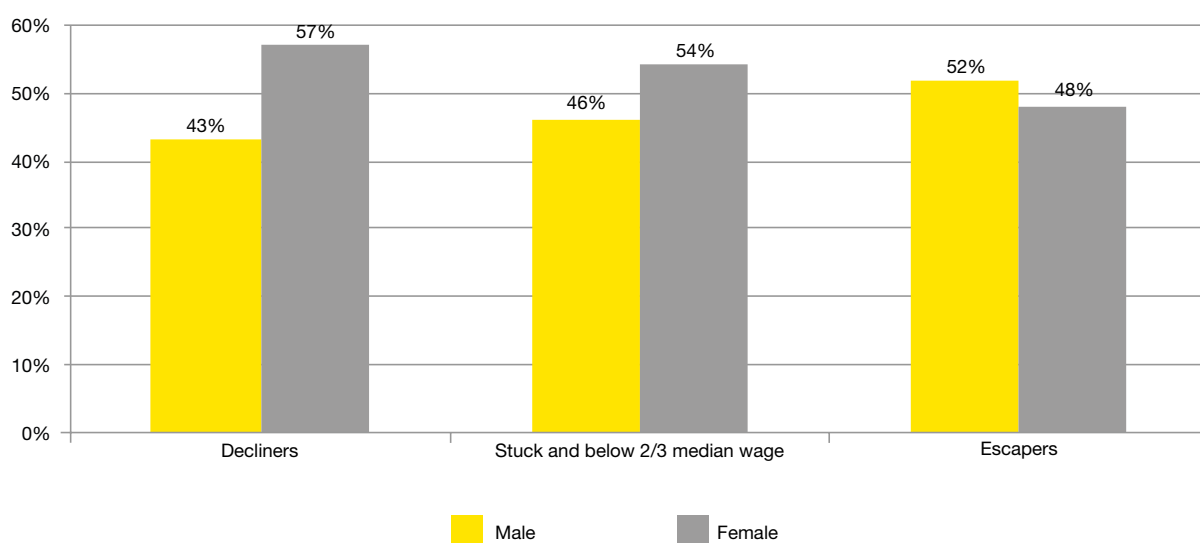
**Figure 22: Progression by age**



Source: LFS

**6.13** Women are more likely to be stuck in low pay – and indeed are also more likely to see their pay decline, a finding in line with other research<sup>112</sup>. The chart shows that women are 54% of those stuck in low pay, while men are the remaining 46%. Men, meanwhile, do find it fractionally easier to move out of low pay.

**Figure 23: Progression by gender**



Source: LFS

<sup>112</sup> See Thompson and Hatfield, IPPR op cit



**6.14** Low paid people who have children are more likely to be stuck than either decliners or escapers. However, they are still a minority among the stuck. Some 45%, nearly half, of the stuck in low pay group, are in families with dependent children. This compares with 28% of decliners and 30% of escapers. However, only 37% of those in low pay in Greater Manchester have children.

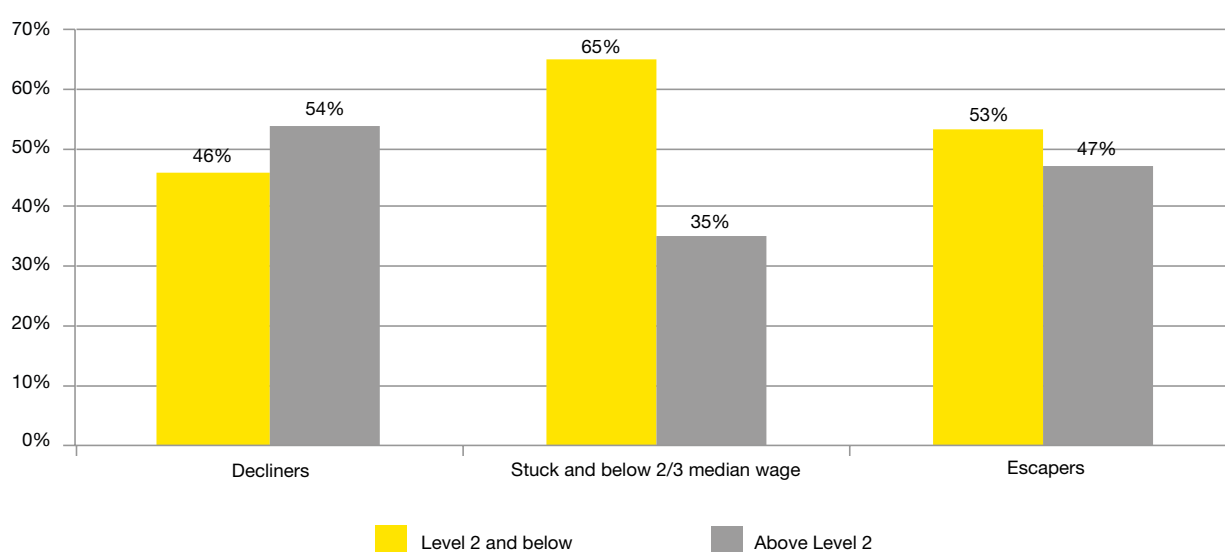
**6.15** The research found that people from ethnic minority groups are less likely to be stuck, although they are much more likely to be low paid than white employees. Some 41% of BAME employees are low paid, compared to 20% of white employees. However, 82% of low-paid people in Greater Manchester were white. The remaining 18% were BAME.

**6.16** People who are low qualified are more likely to be low-paid. The low-qualified form 61% of the low paid, compared to being 36% of the workforce as a whole, although there are many who are low paid who are qualified at level 3 and above. These will include those who are doing low level jobs while studying for a higher qualification and those who have completed a higher level qualification but not yet moved into a career job. The majority (65%) of the stuck were qualified at or below level 2. Those declining into low pay were closer to balance between higher and lower qualified people, as were the escapers. This is shown in the chart below. Some 14% of those who had qualifications below level 2 at the beginning reported achieving them by the end of the 15-month observation window.

**6.17** Some 54% of those who were stuck in low pay had a level 2 qualification as their highest qualification at the end of the period. There are several possible reasons that lie behind this data. Both care work and retail have training programmes (some of which are apprenticeships) aimed at Level 2 qualifications for low-level workers. There are similar programmes in cleaning that are used by some employers such as health services. In these cases the low-paid people could acquire a Level 2 qualification that helped them to remain in work and increase their productivity, without necessarily increasing their pay. In short, there does not appear to be a neat and consistent relationship between qualification attainment and pay increases.

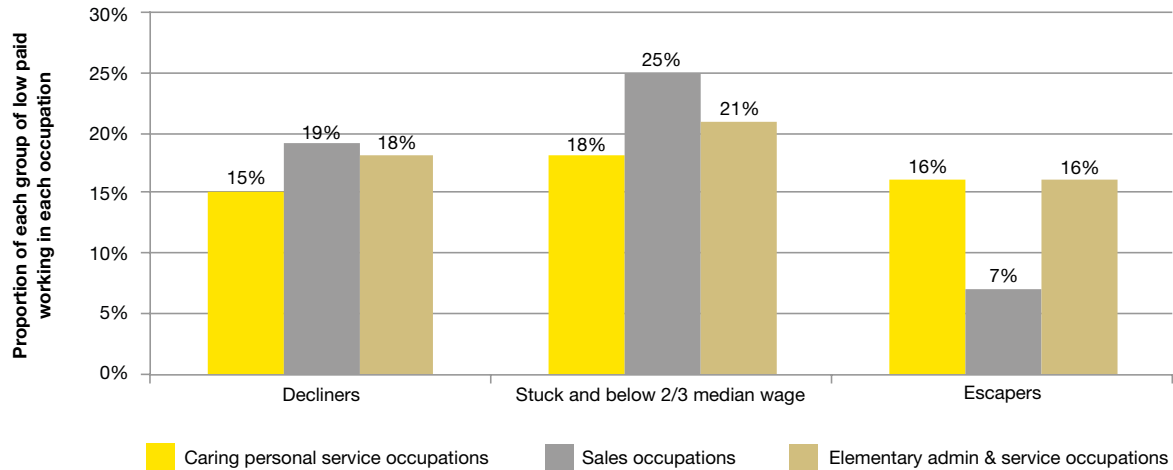
**6.18** Some three quarters of those who are stuck work in areas such as sales, elementary administration jobs or care and personal service. Sales jobs in particular show a stable pattern of low pay, from which it appears to be especially difficult to escape. This suggests that in the lowest paying occupations there are often the lowest opportunities for advancement.

**Figure 24: Progression by qualification level**



Source: LFS

**Figure 25: Progression by Occupational Group**



Source: LFS

**6.19** A majority (56%) of workers in Greater Manchester reported receiving some form of in-work training over the 15 months covered by the Labour Force Survey interviews. This is, however, lower for low-paid employees with 43% reporting some training over this period. Training was lowest for those stuck in low pay, with 40% reporting receiving some training within the 15-month window. Perhaps surprisingly, decliners into low pay reported the highest training proportion at 58%, higher than the entire Greater Manchester workforce. This requires further research to validate this result.

**6.20** The number of escapers who had received training was smaller than that of either those stuck in low pay who had been trained or the decliners who had received training. This is a somewhat bizarre finding, as training might be expected to be related to escaping from low pay. Yet there is some support for the lack of a link between training and pay improvements among other research which has found very limited effects of training on wage levels<sup>113</sup>.

**6.21** In total, 7% of the overall Greater Manchester workforce changed jobs within the 15-month window analysed in this report. A higher proportion of the low-paid (12%) had changed jobs than other types of workers. Many of the jobs done by low-paid people (in Greater Manchester as elsewhere) are known to be high-turnover jobs. These include those in the hospitality sector in particular, but this pattern of higher turnover than in better paid jobs is general. Therefore, we should not be surprised that low paid people change jobs more often than higher paid people.

**6.22** So what best explains progression? These are some of the factors drawn from the literature that have been found to affect progression – either positively or negatively.

- Working for a large employer. Because large employers will normally be spread across a number of sites, a person who is keen to escape low pay is unlikely to have a long wait until a suitable vacancy opens up. Vacancies can be easily internally advertised, for example in the staff room; and employee's experience and knowledge of their organisation's processes can be highly transferrable. Large employers are more likely to have HR departments which can focus on the needs of staff and put best practice into place. Reputational effects were also important in helping shape pay levels.
- The more years a person has been spent working part-time, the less likely they were to progress. While being female was not in itself found to be a negative factor for pay progression, it is difficult to ignore the highly gendered impact which low progression out of part-time jobs demonstrates. As of October 2014, 77% of all part-time roles were filled by women. From the point of view of managers, having two part-timers rather than one working full-time was more work for them, as they had to manage two people instead of one and coordinate their schedules and responsibilities.

<sup>113</sup> See Resolution Foundation, op cit

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- Training was a factor which emerged as consistently insignificant for progression. Despite this finding, it should be acknowledged that a number of other studies have found positive wage returns to training. The training that is currently offered to low paid workers at risk of being stuck in low paid jobs may not be high quality training of the type that would assist progression out of low pay. For those who had progressed, training was a step on the path once moving up had been set in motion. Even in industries like childcare, within which training and qualifications are more common, completing training or acquiring a degree were not seen as a guarantee of higher earnings. Across many retail and hospitality positions, the skills required to progress were seen as those for which it is difficult to train, with 'people skills' and personality ranking highest. For many low paid employees, training primarily functioned as a break from their everyday routine and an indicator that the company was willing to invest in them.
  - Having a 'fair' manager. Managers who encouraged and respected the employee's contribution in the workplace was a prerequisite to progress. Many of the managers who had escaped from low pay themselves credited helpful and understanding management for assisting them. There were a number of softer, implicit approaches that employees held in high regard such as being acknowledged for good work (most contact with senior staff was being told off for mistakes) and managers who were willing to 'get their hands dirty' on the shop floor.
  - The 'right' attitude. Almost universally, when asked what was the most important characteristic needed to progress, employees and managers both said 'the right attitude'. Maxims such as 'employ for attitude, train for skills', 'you can teach people anything' and 'you can't coach character' were frequently cited. Quality management was seen as one way to develop a positive attitude and stronger work ethic in someone who showed little interest in progressing.
  - Being female – especially older and female. Research by CIPD/Tooley Street found that for those who started a period in low pay, the likelihood of being 'stuck' is strongly correlated with being female and increases with age, with outcomes worst outside London. In addition, working part-time, in a small workplace, or in a low-wage industry are strongly associated with being stuck in low pay once the person has had this status for more than one year.

## Conclusions

**6.23** Most people who were low paid at the start of our period of study were low paid at the end. Our findings are in line with others that suggest that in many low wage labour markets, there is very limited scope for progression to better paid work. There appear to be substantial numbers cycling in and out of low paid work as they change jobs. Yet a relatively small minority show a clear sense of moving up out of low pay. In practice, in some sectors, moving up may mean moving out of employment in particular industries. Those stuck in low pay tend also to be low-qualified. Yet there are limits to assuming further qualifications improvements will dramatically enhance wage levels. Skills interventions are weakly associated with progression in the data. People who have been low-paid for a long time may not believe that progression is possible so they may just accept the situation.

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# 7 Business Models and Employer Perspectives on Pay, Productivity and Skills

**7.1** This chapter draws on the findings and arguments of an accompanying paper, *Business Models, Skills Utilisation and High Performance Working in Greater Manchester*, to examine whether a contributory cause of low pay in Greater Manchester may be the choices made by employers concerning how they compete. If a business can generate sufficient returns from business models that involve low quality products and services supplied by relatively low skilled staff, what incentives are there to move upmarket and in turn offer better quality work opportunities? The chapter draws on evidence about product market strategy developed by the UKCES in its Employer Skills Survey series to examine the competitive strategies of firms in Greater Manchester. The chapter goes on to consider the views of employers about low pay, business models and how skills are put to use inside organisations.

The ‘product market strategy’ (henceforth, PMS – which obviously includes services, too) shapes the approach to how an organisation manages the skills of a workforce. Research suggests the direction of causation is that PMS determines skill need.

**7.4** Geoff Mason, an academic who has pioneered the analysis of the links between strategy and skill has argued that PMS choices within firms reflect their decision-makers’ evaluations of external market opportunities and how best to seek to exploit them<sup>115</sup>.

**7.5** Mason’s series of studies has established that there is a firm statistical link between PMS (measured by a series of survey indicators) and the stock of skill levels in a workforce (proxied by qualifications). “All else being equal, high (low) workforce skill levels are positively associated with high (low) value added product strategies.”<sup>116</sup> Using the Employers Skills Survey in different years he has developed this correlation to make several interlinked points:

## What is the relationship between low pay and business models?

**7.2** ‘The low road’ is a shorthand term for describing a competitive strategy based on low value, low quality, and low skill business models. It may offer an important part of the explanation for low skills, and why skills in general tend to be a relatively low priority among business leaders<sup>114</sup>. In turn, this may help explain the incidence of low pay. Low skills in a particular area may flow from the preferences of businesses for how they compete – or at least their reactions to the constraints they face. Skills thus reflect demand alongside supply-side constraints.

**7.3** For example, firms competing on the basis of premium quality, customized goods and services with limited price dependence are more likely to need highly developed skill levels among their labour force. Meanwhile, firms pursuing a low road approach are more likely to need lower skill levels and to treat their workforces as relatively interchangeable, reducing skills development costs.

- PMS is typically extremely diverse even within the same industry, but also between industries;
- Where firms are part of a larger group and competing through high value added skill-intensive product strategies, further efforts to move up-market in response to competition were associated with disproportionately large increases in employers’ demand for skills;
- Where firms competed through low value added PMS then when they up-graded their skills the impact on the demand for skills is relatively modest;
- High spec PMS tended to be linked to exposure to international competition;
- The type of market and establishment size both related to PMS;
- The direction of causation went from PMS to skills strategy.

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<sup>114</sup> See Mayhew et al, op cit; see also Keep, E. and Mayhew, K Was Ratner Right: Product Market and Competitive Strategies and their Links with Skills and Knowledge, Employment Policy Institute, 1998

<sup>115</sup> Mason, G. In Search of High Value Added Production: How Important are Skills?, DfES Research Report RR.663(2005).

<sup>116</sup> Mason, G. Product strategies, skill shortages and skill updating needs in England: new evidence from the National Employers Skills Survey, 2009. Report for UKCES, 2010; see also Mason, G. (2004) ‘Enterprise Product Strategies and Employer Demand for Skills in Britain: Evidence from the Employers Skill Survey,’ SKOPE Research Paper No. 50, 2004

**7.6** Other studies have added some additional details to this picture. Dench et al studied 13 companies in food manufacturing and found PMS were constantly being modified<sup>117</sup> in response to evolving market conditions. In addition, a new factor was found to be important in shaping PMS: the role of technology. The nature of the product determined the technology used, and this in turn was responsible for the use of employee skills. In other words, the deciding factor was PMS, but the determination and introduction of strategy was mediated by the type of technology in use in a workplace.

**7.7** Although Mason's earlier work established that the direction of causation went from PMS to skill, some of his more recent work (with Susannah Constable) has served to finesse this finding<sup>118</sup>. The study again confirmed the interdependence of PMS and skills – especially in firms serving national and international markets rather than those serving local or regional ones; a relatively small move upmarket by a firm had far larger impact on the skills needed. And the scale of the difference was also emphasised: establishments serving the upper quartiles of markets had mean skill levels between level 3 and level 4. The mean level of skills of firms outside the top quartile were some way below level 3. But Mason and Constable also discovered reverse causation in operation too. The ability to move upmarket in reaction to changes in PMS depended somewhat on skills: "High current levels of skills contribute positively to the development of high-end product strategies."<sup>119</sup> Where a firm decides to shift to more complex and demanding PMS, the skills required will increase, too".<sup>120</sup>

**7.8** Business models may in turn explain three further widely discussed contentions about British corporate life: that businesses are not good at using skills even when they develop them; that corporate deployment of human capital in organisations is not oriented towards 'high performance'; and that there is a lack of management and leadership ability within UK firms, especially when it comes to motivating and engaging people<sup>121</sup>.

**7.9** The UKCES, the government's skills advisory body, says that the UK's 'skills problem... lies largely on the demand side'<sup>122</sup>. Meanwhile, in its most recent analysis of UK firms, it found just under a third of employers could be considered 'high performance work organisations'<sup>123</sup>.

**7.10** If its judgement is correct, the vast majority of employers in the UK do not pursue strategies that necessitate workforce organisation approaches that motivate and get the best out of people. This could be read either as a huge untapped opportunity for boosting productivity or as a reflection of the previous point that skills and workforce organisation issues are not a priority among employers and their role can be too easily overstated. Research has evidenced a degree of management inertia about HR practices; management has been reluctant to accept evidence around high performance working practices, let alone act on it. In turn one of the aspects that may lie behind this resistance has been around management skill. According to a research report published by the Department for Business Innovation and Skills, for example, among small and medium sized UK firms, knowledge of management skills is under-developed and there is a 'long tail' of firms acting in ignorance of management best practice<sup>124</sup>.

**7.11** These kinds of somewhat torpid managerial cultures around workforce skills indicate that simply building the evidence base and expecting employers to respond could be considered naïve.

## The product market strategies of Greater Manchester firms

**7.12** So what kinds of strategies are firms in Greater Manchester pursuing? The analysis below draws on the indicators of a company's approach to PMS that have been developed by the UKCES in its Employer Skills Survey (ESS)<sup>125</sup>. The indicators (as developed by Geoff Mason in the studies described above) are seen to be as close to a standard approach to understanding PMS as

<sup>117</sup> Dench, S., J. Hillage, P. Reilly and J. Kodz, Employers' Skill Survey: Case Study – Food Manufacturing Sector, Institute for Employment Studies, 2000

<sup>118</sup> Mason, G. and Constable, S., Product Strategies, Skills Shortages and Skill Updating Needs in England: New Evidence from the National Employer Skills Survey, 2009, Evidence Report 30, July 2011, p66

<sup>119</sup> Ibid, p67

<sup>120</sup> Ibid

<sup>121</sup> See, for example, Keep et al, op cit

<sup>122</sup> UKCES, Ambition 2020: World Class Skills and Jobs for the UK, UKCES, p10

<sup>123</sup> UKCES, Skills for the Workplace: Employer Perspectives, Evidence Report 1, 2008

<sup>124</sup> The research covers leadership, organisation, strategy, entrepreneurship, human resource management, turnover, productivity and growth in 250 UK SMEs. See Department for Business, Innovation and Skills, Leadership and Management Skills in SMEs: Measuring Associations with Management Practices and Performance, Research Paper 211, DBIS, March 2015

<sup>125</sup> Data used in this section of the report is taken from the UKCES Employer Skills Survey 2013. It can be found at <https://www.gov.uk/government/statistics/employer-skills-survey-local-data>

is currently available. The PMS indicators are based on respondents' answers to questions which invited them to estimate where their establishment was positioned on different four- or five-point scales - as compared to other establishments in the same industries - in respect of the following characteristics:

- the extent to which the establishment competed in a 'premium quality' product market as compared to a 'standard or basic quality' product market;
- the extent to which competitive success depended on price;
- the extent to which the establishment 'tend(ed) to lead the way' in the development of new products, materials or techniques;
- the extent to which they provided customised (one-off or low volume) products or services as compared to engaging in high volume or 'mass' production; and
- the extent of accreditation for the Investor's in People Standard (treated as a mark of organisations that endeavour to develop their workforces).

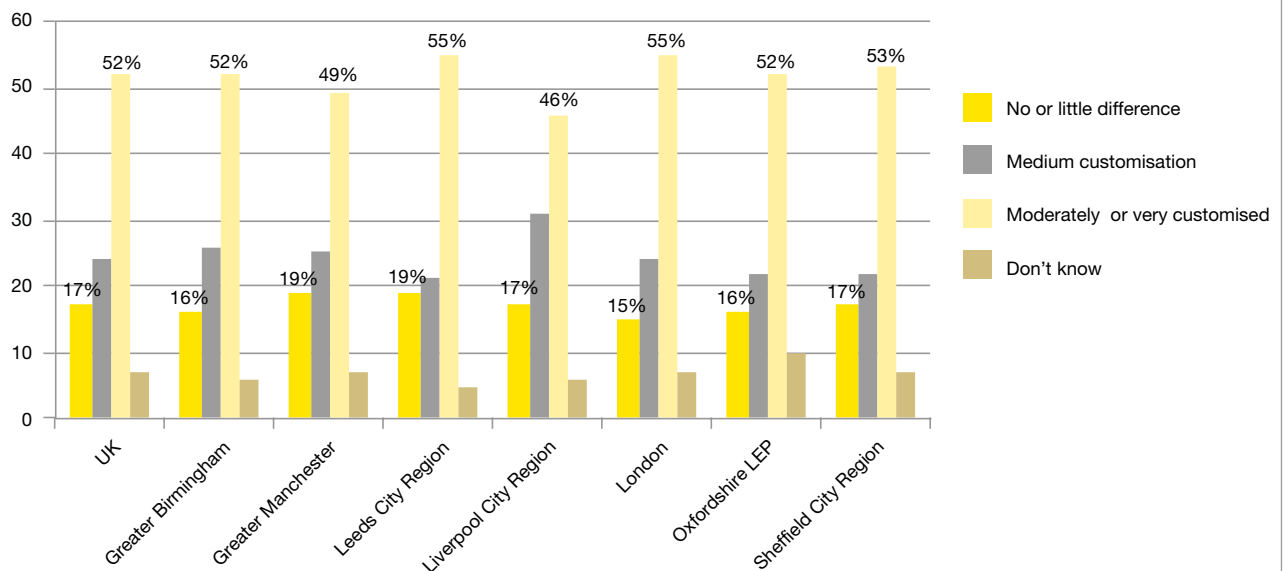
**7.13** The results from these questions can be aggregated together so as to form an overall PMS specification summary (see table 6 below), reflecting the overall

approach of businesses within different LEPs regarding how they position themselves around PMS.

**7.14** The series of charts that follow show how Greater Manchester places on the particular question vis a vis a selection of six other LEPs and the national average. Some response types have been aggregated, so, for example, firms which had 'moderate' levels of customisation have been grouped with those whose products and services are 'very' customised.

**7.15** The first chart below shows how businesses responded on the question of customisation in products and services. In Greater Manchester 19% of businesses said there was no or very little degree of difference to distinguish their products from others in the marketplace – more than in the UK and joint highest on this question with Leeds City Region. By contrast 49% said their products were highly customised, a response rate which is on the low side, but not as low as Liverpool City Region. In general, Greater Manchester employers appear to compete at the basic end of the customisation spectrum with low levels of differentiation in goods and services.

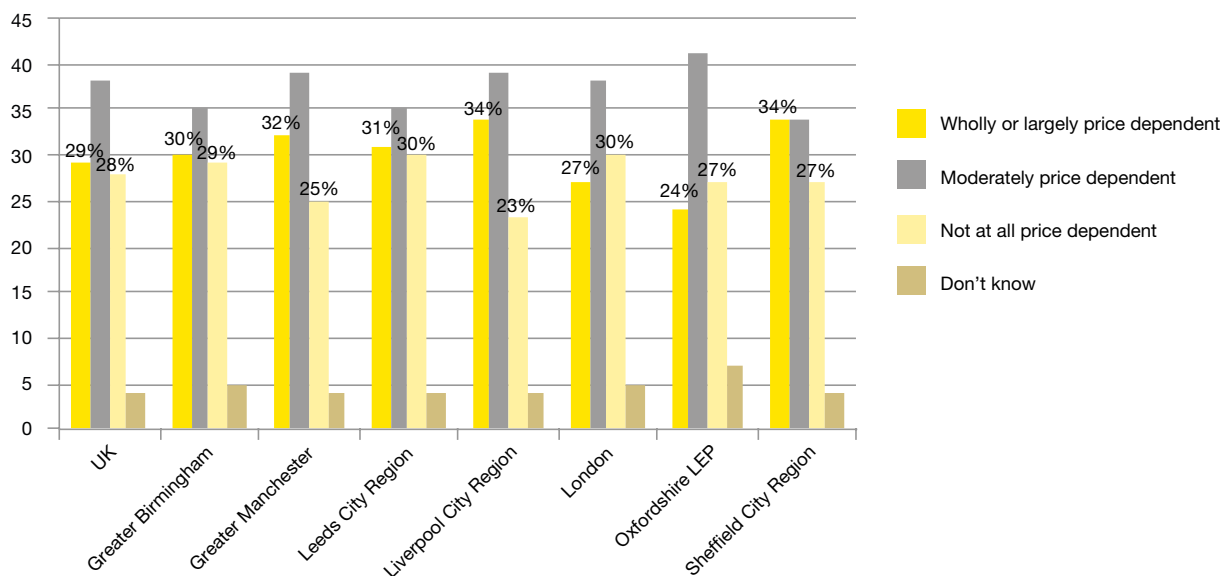
**Figure 26: Description of establishment's business or service in terms of degree of customisation**



Source: Employer Skills Survey 2013

**7.16** The chart below measures the price dependence of businesses. Price dependence reflects the degree to which a business sees itself as competing on the basis of lower costs than rivals or whether its products or services can command higher prices, reflecting added value. The chart shows that in Greater Manchester, just under a third of businesses felt that their products were price dependent, which is not as high as Liverpool or Sheffield (34%), but again higher than the national norm. A quarter of businesses felt that price was not a factor in how they market goods and services – 3% lower than the average UK proportion.

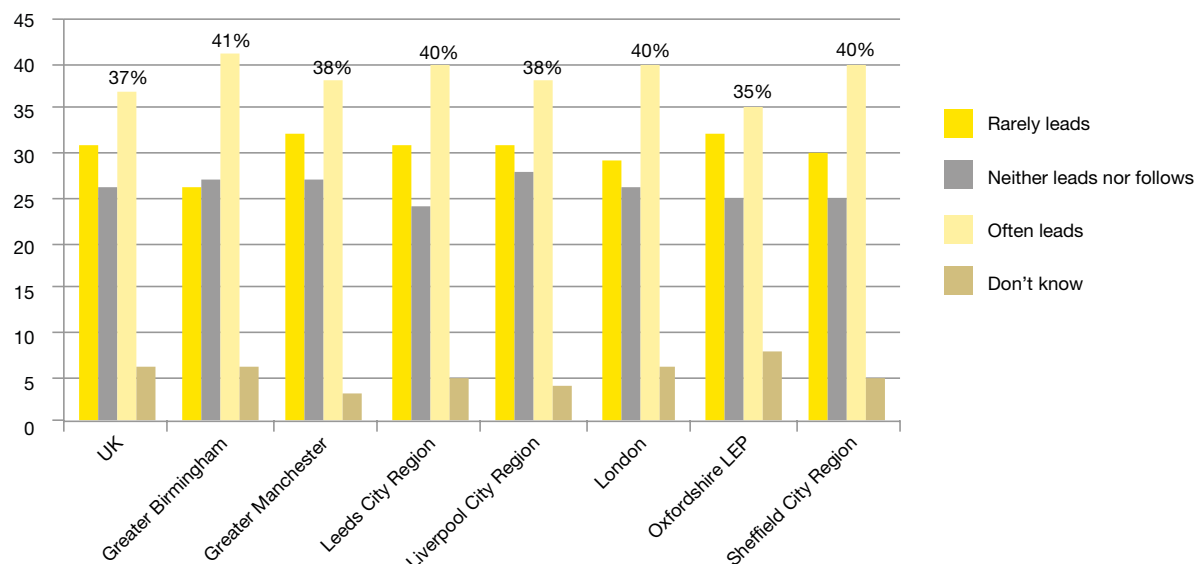
**Figure 27: Degree of price dependence in product offering**



Source: Employer Skills Survey 2013

**7.17** The ESS endeavours to measure perceptions of innovation in part through a question about whether business leaders regard themselves as 'leading the way', ranking responses as to whether they 'often' or 'rarely' do so. Naturally, respondents may interpret this question slightly differently. On this particular measure, Greater Manchester employers responded that they felt they led the way more often than is typical in the UK. As regards those who seldom lead the way, 32% of GM businesses responded this way compared with 31% nationally.

**Figure 28: Perceptions of whether businesses ‘often’ or ‘rarely’ lead the way**

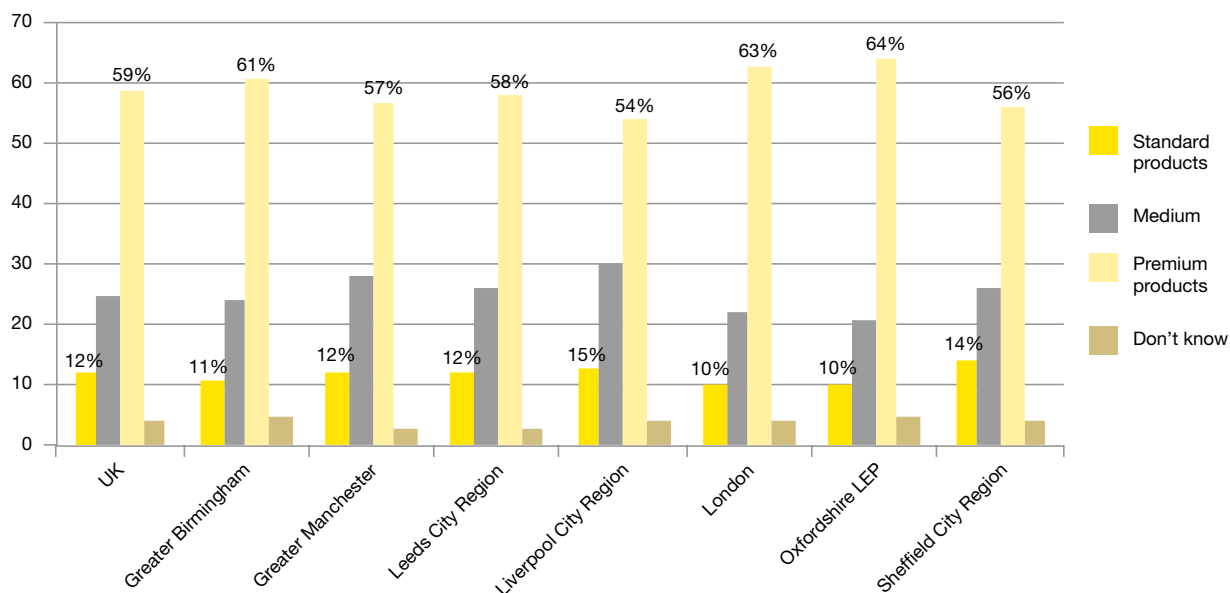


Source: Employer Skills Survey 2013

**7.18** Whether the products sold are seen as high quality or more basic is a further reflection on PMS. The question asked by ESS attempts to get employers to rank whether they offer premium or more basic products. The Greater Manchester answers were on the low side compared with some other LEPs, but were in line with the results for the UK as a whole. As regards premium products, the percentage of firms responding that they targeted premium markets was slightly lower than the national norm, but not as low as several other northern LEPs, including Liverpool and Sheffield. Some 57% of firms in Greater Manchester offered premium products compared with 59% in the UK as a whole.



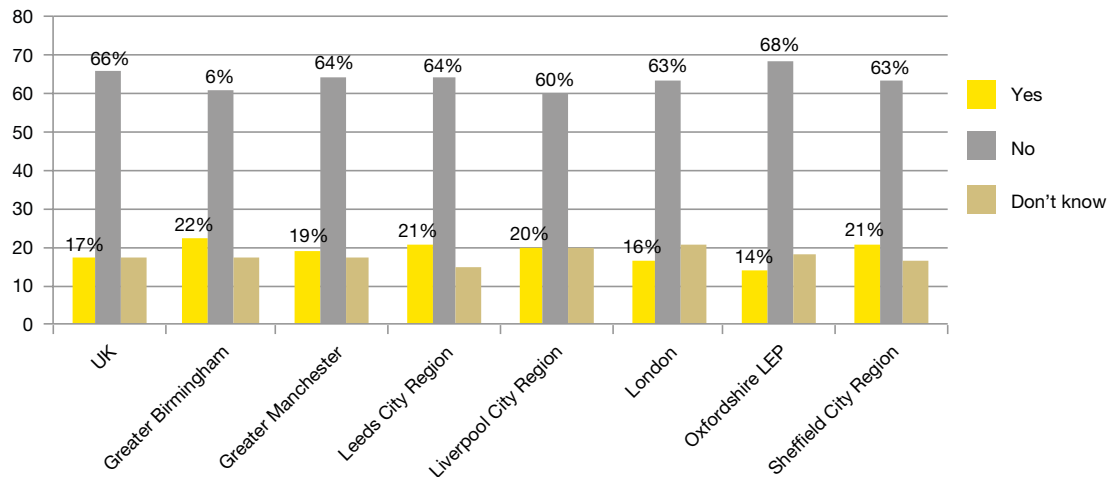
**Figure 29: Perceptions of whether the business offers standard or premium products**



Source: Employer Skills Survey 2013

**7.19** A final reflection of the approach to skills within the framework of PMS is the extent to which there is take-up of the Investors in People (IIP) scheme. Investors in People is a government backed programme that aims to encourage and accredit good practice in people management and development. Greater Manchester endorsement of IIP appears to be above what is typical for the UK as a whole (19%), but some other LEPs had higher rates of firms which had the standard (such as Birmingham). Anecdotally, it is felt that take-up of IIP may have reduced due to the burdens of accreditation which companies felt were an expense that could be eliminated during the recession.

**Figure 30: Does the business have investors in people accreditation**

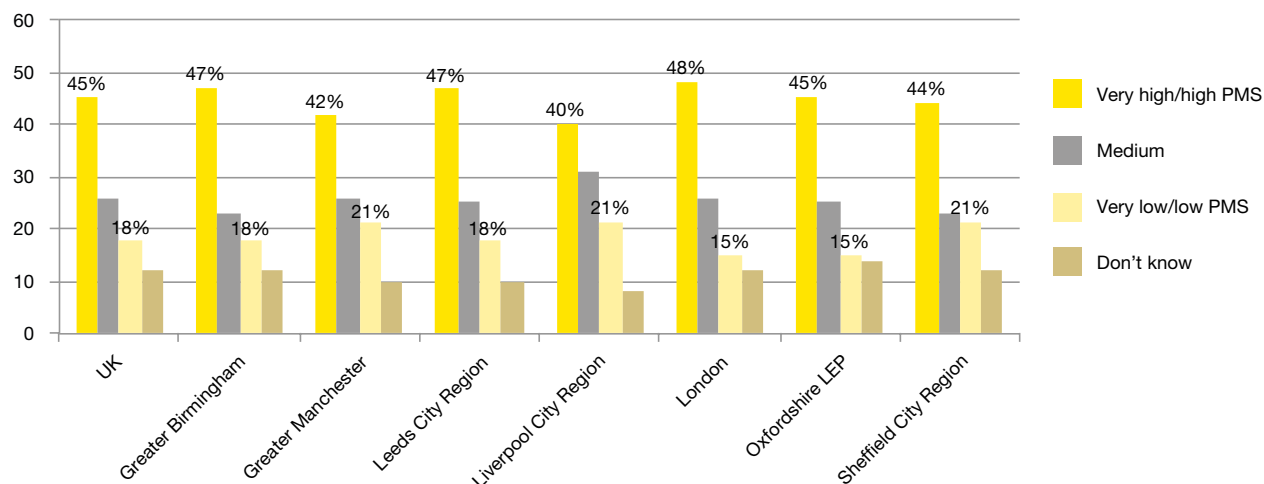


Source: Employer Skills Survey 2013

**7.20** Bringing these different measures together, it is possible to devise a PMS specification index and to measure the different LEPs accordingly – as UKCES does in the ESS. Overall, this finds that 42% of firms in Greater Manchester have a high spec PMS. This is a lower proportion than is typical for the UK as a whole (45%), but is not the lowest (Liverpool has the lowest proportion of firms targeting this high value market segment of 40%). At the other end of the spectrum, the proportion of firms with a low spec PMS was 21% – a figure which is high compared with other LEPs and with the UK as a whole (18%). Other LEPs which also had more than a fifth of their business base targeting the lowest value segment of their respective markets were Sheffield and Liverpool.

**7.21** Overall the results point to Greater Manchester being a city where the competitive strategies of its firms are generally pitched towards low cost, undifferentiated, basic products and services rather than at the higher value adding segments of the economy that can command higher prices (in as far as these concepts can be measured). If the connection described earlier in the report between approach to PMS and the demand for and use of skills is accurate, the results serve as an indication that the business base of the Greater Manchester city region is likely to have relatively weak demand for higher level skills relative to other city regions. An important element within this – given the research outlined above – is the degree to which Greater Manchester firms serve national and international markets. International competition functions as an important driver of the need for higher level skills.

**Figure 31: PMS summary: the overall positioning of firms in selected LEP areas**



Source: Employer Skills Survey 2013

## Employer Perspectives

**7.22** As part of the low pay project, we undertook a series of interviews among employers regarding the root causes of low pay, their attitudes towards business models, how they deploy skills and how people in low wage work could develop. The employers were drawn from many different sectors, but included hospitality, manufacturing, temporary employment agencies, telecoms, logistics, distribution and wholesale, as well as representative bodies such as the Greater Manchester Chamber of Commerce. The managers also came typically from very senior ranks of their respective organisations - from managing director or chief executive level. The interviews were undertaken on condition of anonymity.

## Understanding of the root causes of low pay

**7.23** Employers generally struggled to answer the question of what they understood to be the fundamental cause of low pay - at least initially. A few expressed the view that the question was alien from the primary focus of their jobs. A minority said they simply did not know. However, a variety of responses were offered once they had had a chance to reflect. Although skills issues emerged as a possible cause of low pay, this view was a novelty and no one highlighted skills acquisition as a means of progression out of low pay. In general, the view was that in many lines of low paid work the opportunities for progression were relatively few and far between. Among the answers were:

- The growth of core and periphery business models, leading employers to adopt workforce segmentation strategies;
- The decline of manufacturing and the corresponding growth of service sectors with labour intensive approaches to service delivery;
- Poor attitude and inadequate job readiness, especially among the young;
- The decline of unions;
- 'Winner take all' labour markets, which have had the effect of making those who are not seen as 'talent' 'more interchangeable';
- The growth of flexible labour market strategies, which have incentivised greater degrees of casualisation among workforces (zero hour contracts were referred to by four employers under this point).

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**7.24** Comments on this point included:

“A key cause, as I see it is the core and periphery model where you have a group of skilled labour that you are very dependent on and that you need to hang on to, and a group of people who are less core and this alters over time and between sector, but basically, employers are drawing pretty tightly the lines around the group who are truly core – more and more are therefore casual and periphery workers and they are fairly interchangeable. You would think twice about investing in this group.”

“The use of zero hours contracts has become absolutely obscene. No one can live a normal life when you are working like that.”

“Low pay has followed on from the breaking of the trade unions and management designed to drive efficiency and ‘being lean’.”

“Ultimately, the real bottom line here is profitability and that determines everything else - including how we go about recruiting and developing the skilled labour that we need.”

## Relationship between productivity and skill

**7.25** Regarding productivity approaches, the responses to this question revealed the central preoccupations as being with reducing waste, increasing efficiency, the critical importance of technology and ensuring the flow of skills into a business. Skills utilisation and HR management issues interacted with these other drivers. One particular interviewee, a chief executive, also emphasized that HR management practices needed to be as well aligned as possible with wider business objectives. While skills were a business performance issue to some degree, the relevance of skills depended on, and derived from, other strategic considerations (such as positioning in a market and the technology that operates in a workplace).

**7.26** Several employers highlighted ‘lean’ techniques for removing waste, both as an important technique in manufacturing and in services (in the healthcare sector in particular).

**7.27** No employer regarded skills per se as a vehicle for altering the strategy. Skills in general tended to be seen as an important, but ultimately a lower order consideration with answers concentrating essentially on a perceived ‘skills supply crisis’: opportunities existed among these employers, but the difficulty was in finding suitable candidates to meet them.

**7.28** A further dominant strand of thinking was around technology. Especially in manufacturing, but also in healthcare and digital, productivity advances were conceived as being dependent on technology, and with technology determining the need for skills and the possibility for up-skilling among individuals. In general, the employers felt that the rapid advances in technology militated in favour of a growing need for high level skills.

**7.29** A minority of the employers did acknowledge that the availability of ‘cheap and flexible’ labour was a possible influence on strategic choices. One employer who felt strongly about this said that the current availability of people willing to work at low rates of pay offered something of a ‘distraction’ from driving up productivity, but he went on to note that this situation was typically resolved (in his business at least) through the introduction of technology.

**7.30** Others urged the point that it is important to see business not in a local, but in a global context. Other nations were always likely to be “cheaper and more flexible” and were dramatically altering their productivity relative to the UK.

**7.31** Competitiveness ultimately could not depend on ‘cheap labour’ type strategies, several employers felt.

**7.32** Finally, a vocal minority of the businesspeople approached skill issues as part of a wider package of people management practices. In turn getting value from these practices also depended on how well aligned incentive arrangements were with the economic goals of the organization. Provided they were well-aligned with business purpose, the overall package of people management practices could make a significant difference to the quality of work and the quality of the service on offer.

**7.33** The comments below reflect some of these responses.

“In our business we need to be stripping 5% of costs every single year in order to remain competitive against international competitors, but also against ourselves around the world. That is about a laser like focus on waste and ensuring it is completely accepted by all members of staff as part of our DNA. In our business, lean is a critical element in achieving productivity goals.”

“Labour is decreasing with automation. Productivity changes fundamentally because of the technology.”

“Cheap and flexible labour can mean that business takes its eye off the productivity ball. Cheap labour is often up-skilled by the technology, though.”

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## Moral Duties and Practical Considerations in Skills Formation

**7.34** Around the whole question of low wage and/or low skill work, employers who ventured comments often tended to speak in moral terms rather than practical or financially minded ones. This mood appeared to be especially strong in relation to skill development which many interviewees felt was something that businesses could actively do more to contribute towards.

“Business also has moral responsibilities and it is right to be expecting them to up-skill the next generation out of moral duty. I’m not saying there is any one way that is right to go about doing it, but business does have a duty to invest in and develop people.”

“It really is about attitude and work-readiness. If that is wrong and people don’t have the basic aspiration to want to do well, it is not just going to work in terms of up-skilling them.”

## Developing Skills in Relation to Business Need

**7.35** Without exception, interviewees felt that skill should be seen as depending on business need rather than existing as an isolated value in its own right.

**7.36** Some restrained criticism of the provider base was also in evidence. Skill formation provision was perceived to be done without working with businesses.

“There is clearly a skills supply problem, there is a supply issue. Business needs are paramount and they do not always seem to be right at the top of the agenda in the way that they should be.”

**7.37** The interviewee who made this remark was also asked how, then, to balance the development of skills that are useful for individual businesses and transferable skills that can be used outside individual firms. She replied:

“That’s the key balance of skills – to get the skills businesses can actually use, but also to make sure that people have skills – like a form of insurance – to move into work again outside of that individual business if things don’t work out...I won’t pretend I have all the answers.”

## Conclusion

**7.38** The evidence reviewed in this section points to something of an alternative narrative on skills: increasing the qualifications levels of the workforce to drive productivity in the absence of a thorough understanding of the constraints of businesses in different sectors may be far too reductive. Instead, skills and economic development more widely needs to understand better the product market strategy and competitive strategy of employers. Firms seeking to compete in higher value markets are likely to demand higher skills and to seek to tap the discretionary effort of the labour force through practices that engage employees. Differentiated products and services are likely to demand the equivalent of jumping an NVQ level, for example. This approach to skills development points to interventions such as working through employer associations to develop the evidence base and communicate evidence (for example about the benefits of high performance work organisation); developing the skills of senior managers so they can see the advantages of competing with enhanced skill levels; and easing the financial constraints that inhibit risk taking and investment. Research has found however that skills strategies are too often ‘path dependent’, resting on past choices. Strategic evolution can be seen to be too difficult. Therefore, whether these approaches can sufficiently change the attitude to skills is questionable. To quote one commentary, a truly realistic assessment of the UK’s low-wage, low skill problem “would suggest that to make any serious advances would require policy interventions designed to foreclose cost-based routes to competitive success, exert pressure on firms to move up-market, tackle short-termism and strengthen the position of organised labour both within the workplace and national policy setting”.<sup>126</sup>

**7.39** The evidence in Greater Manchester suggests that local firms’ PMS strategies tend toward the lower-cost, lower-spec end of the spectrum. On the indicators of PMS reviewed here, Greater Manchester firms generally rank beneath national norms when it comes to the adoption of high spec PMS approaches. The city region’s firms are by no means pursuing the lowest cost options compared to other city regions, but they appear to compete on relatively low cost, low spec, undifferentiated goods and services. In turn, this is likely to mean their demand for higher level skills and competences within their workforce may be relatively modest. These findings may be influenced by the levels to which Greater Manchester firms sell into national and international markets. Where firms serve local or regional markets, their skills needs are likely to be lower.

**7.40** Meanwhile, employers do not profess to have any easy answers as to the causes of low pay or how to address it. Yet some express strong – even strident – views about the rights and wrongs of low wage work, tending, in as far as there is a general attitude towards it, to see it as the logical consequence of ‘flexibilisation’ in the labour market.

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<sup>126</sup> Lloyd, C and Payne, J Goodbye to all that? A critical re-evaluation of the role of high performance work organisation within the UK skills debate. *Work, Employment and Society*, vol. 20, 2006, p13

## 8 Tax Credits: Supporting the Working Poor

**8.1** Tax credits are a form of support for low income households that, in their current form, were introduced in April 2003. On current plans, they will be subsumed into Universal Credit by 2017. As well as forming a very significant part of the benefits bill (some £30 billion nationally), there have been repeated claims that the tax credit system also acts as a state subsidy for low wage work – a contention echoed by the Chancellor of the Exchequer. In the July 2015 budget, he said: “It can’t be right that we go on asking taxpayers to subsidise, through the tax credit system, the businesses who pay the lowest wages. That subsidised low pay contributes to our productivity problem. The government is against unfair subsidies wherever we find them.” In that budget, the Chancellor announced £12 billion of welfare cuts, of which £6 billion came from tax credits, as he aimed to return spending to 2007/8 levels by cuts to entitlements. However, by November 2015, this policy had been reversed. Immediate plans to cut tax credits were shelved. Yet longer term, how tax credits will be treated under Universal Credit could still imply significant cuts.

**8.2** In this chapter we draw on and summarise some of the principal findings of an accompanying report, *The Economic and Fiscal Impact of Low Pay in Greater Manchester*, which examines tax credits in detail, basing its analysis on the 2012/13 financial year. Readers seeking detailed statistics on tax credit spending and the characteristics of tax credit recipients should consult that report.

### Tax Credits in the Greater Manchester context

**8.3** The UK tax credit system includes two main types of tax credit: working tax credit (WTC) and child tax credit (CTC). CTC is available to all families with qualifying dependent children<sup>127</sup>, whether they are in work or out-of-work. WTC is only available to those in work who satisfy a minimum work requirement that depends on their circumstances<sup>128</sup>. WTC and CTC are calculated based

on the ‘elements’ for which a family is eligible, which are then withdrawn once income reaches set thresholds. In practice, the tax credit system is very heavily oriented towards families with children. For example, a lone parent with two children can earn up to £30,300 before losing CTC eligibility. At an annual labour income of £20,000, a lone parent with two children would still be eligible for roughly £4,200 in child tax credit. For the childless, withdrawal rates kick in at lower household incomes of about £17,000. How these items break down in Greater Manchester is shown in the table below.

**Table 17: Number and type of tax credit claimants in Greater Manchester in 2012/13**

Type	Number of families <sup>129</sup>
Working Tax Credit	27,900
Child Tax Credit	36,700
WTC and CTC	97,100
Out of work recipients	74,300

Source: HMRC

**8.4** Greater Manchester has 219,000 residents who receive tax credits. The city region spends significantly more on tax credits than the average for the UK – indeed tax credit spending is among the highest of comparable UK regions (only the West Midlands spends more). Per working age adult in 2012/13, Greater Manchester spends £715.33 compared with a UK average of £573.73 – some 25% higher than the national average. The number of tax credit claimants is 19% higher than the national average but broadly in line with claimant rates in other large northern metropolitan areas such as West Yorkshire and Merseyside. The average claimed in 2012/13 was about £6,509, 5% higher than the national average.

<sup>127</sup> Qualifying dependent children are either aged under 16, or aged 16-19 but in qualifying education or training.

<sup>128</sup> For households with children, lone parents must work at least 16 hours a week and couples with children must work a total of at least 24 hours a week with one person working at least 16 hours. WTC is available to childless individuals and couples who are: aged over 25 and work at least 30 hours a week; aged over 60 and work at least 16 hours a week; or are disabled and work at least 16 hours a week. More details about eligibility and tapers are contained in the accompanying report.

<sup>129</sup> <https://www.gov.uk/government/statistics/personal-tax-credits-finalised-award-statistics-geographical-statistics-2013-to-2014>

**Figure 32: Tax credit spending per working age adult, 2012-13**

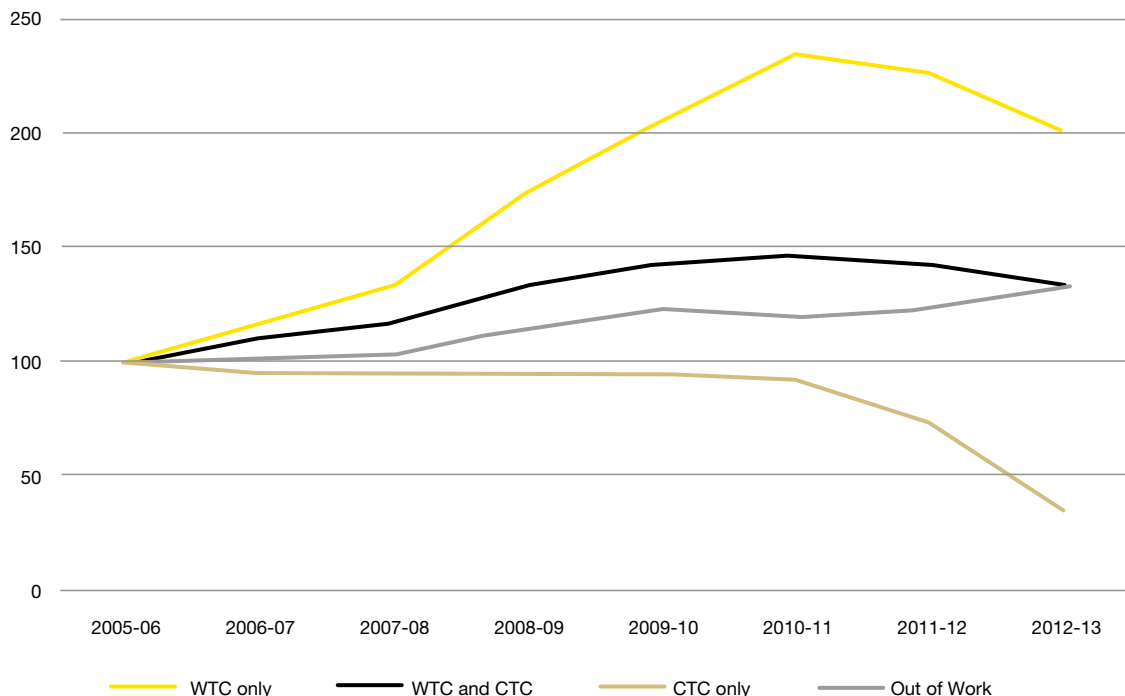


Source: HMRC

**8.5** Some 70% of tax credit spending goes to those in work. Among major metropolitan areas only West Yorkshire spends a greater share on those in work.

**8.6** Spending on tax credits rose in real terms between 2005/06 and 2009/10. After the coalition government took power, tax credit spending stabilised, and began to decline gradually beginning in 2011/12. Total nominal spending on tax credits in Greater Manchester rose from £974m to £1.556m between 2005/06 and 2012/13, an increase of 59%. But once accounting for inflation, this translates into a real terms increase of 29%, roughly in line with the 26% increase in the UK as a whole. Spending on tax credits broadly followed a similar pattern in several other metropolitan counties, rising by between 25% and 32% in real terms over the same time period.

**Figure 33: Trends in different types of tax credit spending, Greater Manchester, 2012/13**



Source: HMRC

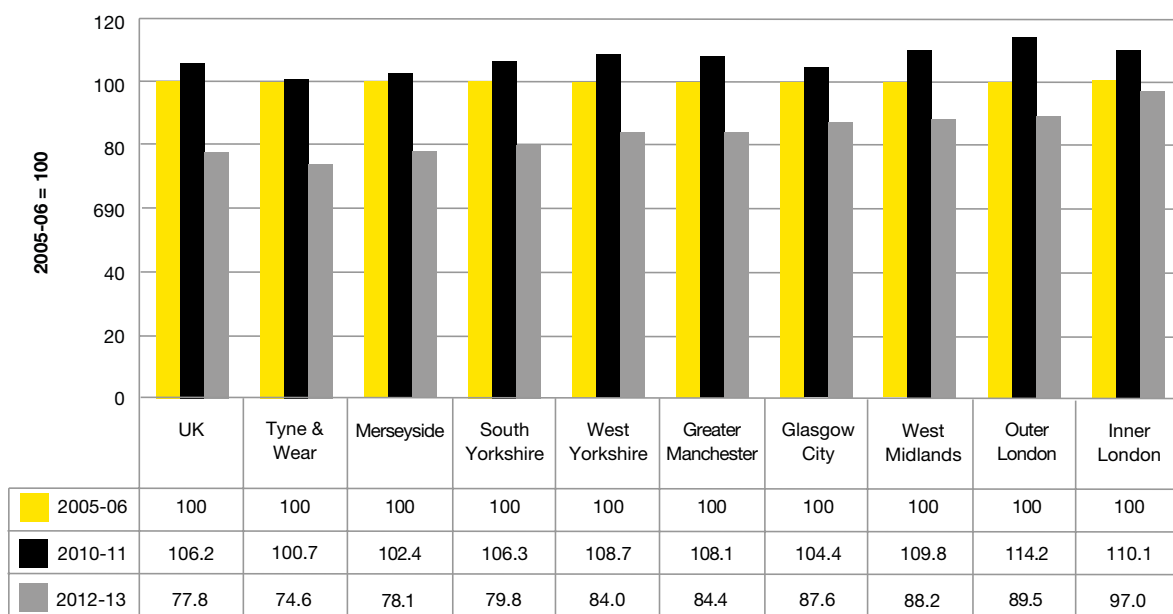
**8.7** There was, however, some diversity in the trends of spending on different types of tax credits. WTC paid to childless families rose most quickly, doubling in real terms in Manchester between 2005/06 and 2012/13 and increasing by 85% in the UK as a whole. The lion's share of the decline in spending, however, came about due to tightened eligibility criteria and faster withdrawal of CTC as income increases, changes that began to take effect in 2011/12.<sup>130</sup> As a result of the changes to CTC eligibility and tapering, most families with two children with incomes between £31k and £58k lost their eligibility for CTC, while most families with one child saw their income thresholds decline further to about £24k.

**8.8** The total number of tax credit recipients (including both in and out-of-work tax credits) in Greater Manchester declined by 16% between 2005/06 and 2012/13, rather more slowly than the UK-wide decrease of 22%. The total number of tax credit recipients rose during the recent financial crisis, peaking in 2010/11, before beginning to fall in the wake of tightened eligibility criteria for CTC beginning in 2011/12.

<sup>130</sup> Until 2010-11, the 'family element' of CTC, worth £545 annually, was not tapered until a threshold family income of £50k, and at a low rate of 6.7%. In 2011-12, the tapering threshold for the 'family element' was reduced to £40k and the taper rate was increased to 41%. In 2012-13, the threshold was reduced further to £16,190, in line with the threshold for the child element, and the taper was maintained at 41%.



**Figure 34: Trends in total number of tax credit recipients, geographic breakdown, 2005-6=100**



Source: HMRC

**8.9** The average tax credit spending per recipient family in Greater Manchester increased by 53% between 2005/06 and 2012/13, slightly below the UK-wide increase of 61%. This is likely to be driven by the concentration of spending on families with lower incomes: the numbers of higher income CTC claimants dropped, while the numbers of lower income families claiming the larger CTC and WTC benefits increased.

## Characteristics of Tax Credit Recipients

**8.10** Greater Manchester has a higher incidence of tax credit receipt than the UK as a whole. In total some 10.25% of people in Greater Manchester receive tax credits, compared with 8.43% in the UK. Tax credit receipt is particularly high among one parent families, where a third receive tax credits. Tax credit receipt is highest among people in their late thirties: about 22% of people in this age group receive tax credits.

**8.11** As one would expect, tax credit receipt is concentrated in intermediate and routine occupations. A further notable characteristic is that Greater Manchester has a higher number of self-employed in receipt of tax credits. Some 14% of the self-employed receive tax credits compared with 11.3% in the UK. In total, some 10.35% of those in employment (self-employed and employees) receive tax credits.

**8.12** By industry, sample sizes are insufficient to allow for Greater Manchester comparisons. Nationally, however, it is possible to see concentrations in wholesale and retail; accommodation and food services; administrative and support services; health and social work; education, and other service sector activities. The very limited information available for GM also suggests clustering in education and health and social work.

**Table 18: Tax Credit Receipt, UK level**

Sector, main job/% tax credit recipients	UK/%
Agriculture, forestry and fishing	9.85
Mining and quarrying	2.62
Manufacturing	6.58
Electricity, gas, air cond supply	4.18
Water supply, sewerage, waste	7.33
Construction	6.6
Wholesale, retail, repair of vehicles	12.23
Transport and storage	9.61
Accommodation and food services	14.35
Information and communication	3.42
Financial and insurance activities	4.8
Real estate activities	7.58
Prof, scientific, technical activity	4.64
Admin and support services	12.38
Public admin and defence	5.85
Education	10.9
Health and social work	12.49
Arts, entertainment and recreation	8.84
Other service activities	12.38
Households as employers	16.03
Extraterritorial organisations	0.96
All employed or self-employed	9.29

**8.13** In terms of occupations, tax credit recipients are bunched into a few occupational groups (administrative and secretarial, caring/leisure and other service occupations, sales and customer service, process/plant/machine operatives, and elementary occupations). Greater Manchester has the biggest shares of workers in these groups on tax credits, apart from sales and customer service (highest in the Mets) and process/plant/machine operatives (highest in London).

**8.14** Tax credits are considerably more prevalent among part time workers, for obvious reasons. Among part time workers, Greater Manchester has a larger share on tax credits than the national average.

**Table 19: Tax credit recipients in work: full-time / part-time workers, 2013**

Full time or part time work / % Tax credit recipient	UK		Greater Manchester		Mets		London	
	Full time	Part time	Full time	Part time	Full time	Part time	Full time	Part time
No	93.73	82.39	92.06	78.88	92.27	78.76	95.03	81.82
Yes	6.27	17.61	7.94	21.12	7.73	21.24	4.97	18.18
Total	100	100	100	100	100	100	100	100

Source: APS. Those on Work Programme or Apprenticeships not shown.

**8.15** Not everyone on the National Minimum Wage receives tax credits and not every recipient of tax credits is on the NMW. Across the UK, around 21% of those who earn the minimum wage or less, also get tax credits. In Greater Manchester this is higher, at 23.07%.

## Tax Credit Dynamics

**8.16** Conforming to the pattern of tax credits being oriented towards those with children, the childless have very low rates of in-work tax credit receipt and also transition out of tax credits at the highest rates. In the space of a year, almost half of tax credit recipients exit the system – a rate which is more than twice the exit rate for the whole sample of 23%. In fact, every quarter a fifth of childless WTC claimants leave the system. This compares with just 2.9% among lone parents and about 11% overall.

**8.17** One factor supporting the high exit rates might be the low incomes at which the childless cease to be eligible for in-work tax credits, which make it easy for full-time employees to earn incomes high enough to graduate from WTC. A standard full-time working week at just above the NMW is likely to mean tax credits are no longer available.

**8.18** Lone parents who stay on tax credits tend to work part-time at relatively low wages. Lone parents who stay on tax credits – the vast majority – work on average just over five hours daily, consistent with a pattern of working during school hours. This might indicate that providing incentives for or assistance in increasing working hours beyond school hours might be of use in increasing exit rates of lone parents. Once again we have insufficient data to reliably estimate the average wages required for lone parents to exit tax credits.

**8.19** There is insufficient data to calculate the exact incomes people need to leave the tax credit system altogether. Yet what evidence does exist suggests the incomes people need to leave the tax credit system are often relatively low. This might indicate that the exit from tax credits is associated with the (re-)entry to the labour market of a second earner, or with an increase in the second earner's pay or hours.

**8.20** The vast majority of people who leave tax credits do so because they enter employment (85%), but a small minority exit to economic inactivity (10.4%, the remainder exiting to unemployment. Exit was rarely predicated on increasing the number of hours of work, however, though sometimes increases in pay were apparent. The longer report speculates that this might be linked to the predominance of family heads from couples with children among the sample of exiters. A reduction in hours of the head along with stable earnings might be consistent with tax credit exit if it is associated with the (re-)entry into the labour market of a second earner in the family.

**8.21** Lone parents who stay on tax credits tend to work part-time at relatively low wages. Lone parents who stay on tax credits – the vast majority – work on average just over five hours daily, consistent with a pattern of working during school hours. This might indicate that providing incentives for or assistance in increasing working hours beyond school hours might be of use in increasing exit rates of lone parents. Once again we have insufficient data to reliably estimate the average wages required for lone parents to exit tax credits. The analysis finds that there is little practicable difference in terms of pay.

## Do employers gain from the tax credit system?

**8.22** A very important point is the degree of 'employer capture' of tax credits. However, modelling reveals that most (about three quarters) of the gains go to the employee. The method used to reveal this finding contrasted the wages of 24 year olds with those of 25 year olds (25 being the age for tax credit eligibility). It found that 25 year olds suffered a statistically significant fall in their income relative to 24 year olds. Some employer capture is inevitable given the fact that the benefit (or at least WTC) is explicitly targeted at people in work. And of course, it is possible to draw the conclusion that a quarter of the £1.5bn doled out to employers to subsidise low wage work is a very substantial sum flowing into the pockets of businesses. However, given the nature of tax credits, it is perhaps slightly more arguable that the credits are relatively well targeted.

**8.23** The report finds that the greatest fiscal advantages would not necessarily flow from lifting low wage workers up to the level of the living wage, but from encouraging more lone parents to enter the labour market and increasing the participation of second earners. For example, in terms of fiscal gain per head, increasing wages to the level of the living wage would yield advantages of approximately £1,445 per head. But if more lone parents could be helped to increase their labour market participation, fiscal gains in the order of £4,515 per head may be realisable.

**8.24** Tax credits ‘work’ in the sense that they incentivise people with relatively low potential wages to enter the labour market, while still allowing the state to provide a basic safety net to those out of work. The research, in line with the literature, shows that while some of the incidence of tax credits benefits the employer, the proportion is not large. And there is no obvious or simple way of recouping that money for the taxpayer without a reduction in work incentives, and hence employment, for low-paid workers. Increasing wages and hours alongside improved productivity will reduce the tax credit bill as well as benefiting workers and employers, but that is much easier said than done. It goes without saying that any programme designed to reduce reliance on tax credits would have to be on a very large scale: there are more than 200,000 tax credit recipients in Greater Manchester, the vast majority of whom will (if in work) have no contact at all with any government programme related to the labour market.

## Tax Credit Reform

**8.25** Incentivising (whether by carrots, sticks or both) employers to increase pay would have some impact on tax credit spending, although it is important to note that most recipients are not on the minimum wage. The surprisingly large share of tax credit recipients in Greater Manchester who work in the education and health sectors suggest that there may be scope for work with these employers (who are likely to be large public sector employers) in particular as a first step; this might then provide a base for engagement with large private sector employers (eg. in the retail sector). We should not, however, assume that pay increases are likely to ‘pay for themselves’ in terms of reduced tax credit spending (and/or increased tax revenue). Therefore, such an approach is likely to work better if introduced alongside other initiatives to improve productivity (research by NIESR for the Low Pay Commission suggest that higher wages for the low paid can indeed help incentivise improved productivity).<sup>131</sup>

**8.26** The immediate prospect of major reductions to tax credits appears to have receded since July 2015. Shortly after they were announced, the Institute for Fiscal Studies calculated that out of £12bn in overall cuts, tax credit change accounted for £6bn, freezes in benefit rates for £4bn and £1.4bn from reductions in funding to housing associations and local authorities<sup>132</sup>. From the perspective of Greater Manchester this can be seen as a highly significant reprieve given the evidence of high tax credit dependence among the residents of the city region. Calculations by New Economy suggested that the tax credit measures were likely to have removed £327.2 million from the local economy<sup>133</sup> and been felt most acutely by people in work, but on a low income. Longer term, however, the future of tax credits under Universal Credit is highly uncertain.

## Conclusions

**8.27** Tax credits may be a relatively recent welfare innovation, but they have become a vital part of the policy arsenal in addressing low pay. Representing just under 30% of all welfare spending they are a very substantial item of public expenditure. Research has found that the greatest scope for locally based reform lies in encouraging lone parents and second earners (the tax credit system’s key beneficiaries) to play a more active role in the labour market, for example by additional support with childcare. The scope for savings from pay increases from such mechanisms as the living wage is rather lower in terms of fiscal gains.

<sup>131</sup> Riley, R. and Rosazza-Bondibene, C. (2015). The impact of the National Minimum Wage on UK Businesses, Report to the Low Pay Commission, London: National Institute of Economic and Social Research and Centre For Macroeconomics.

<sup>132</sup> Institute for Fiscal Studies, Budget July 2015 Analysis, [http://www.ifs.org.uk/tools\\_and\\_resources/budget/505](http://www.ifs.org.uk/tools_and_resources/budget/505)

<sup>133</sup> New Economy calculations available on request

# 9 The National Living Wage Versus the ‘Real’ Living Wage and Personal Tax Allowance Changes

**9.1** This chapter examines the likely impact of the ‘national living wage’ for over 25 year olds in Greater Manchester and associated changes to the personal tax allowance system. The chapter then touches on the future of the ‘real’ living wage in the light of the proposed changes.

## New National Living Wage for over 25 year olds

**9.2** In the July 2015 budget the government announced the introduction of a ‘national living wage’ of £7.20 from April 2016 – effectively a new age-related premium on the NMW. It also set a target for this rate to reach £9 an hour by 2020. The low pay debate has become rather linguistically muddled in the wake of this move. The new rate is below the ‘real’ living wage, as determined by the Greater London Authority for London (£9.40 in 2016; £9.15 in 2015) and by the Centre for Research in Social Policy, based at Loughborough University (£8.25 since November 2015 2016; £7.85 between November 2014 and November 2015) for the rest of the UK. The new national living wage is 50p more than the NMW at the time of writing (£6.70). This is a bigger single rise than has ever occurred since the introduction of the NMW in 1999. However, in percentage terms it is dwarfed by the increase of 2001 (10.8%).

**9.3** The table opposite presents anticipated rises in the national living wage through to 2020.

**Table 21: National Minimum Wage/National Living Wage movements, 1999-2020**

	Year	NMW Adult rate	Difference	% Change
Actual	1999	£3.60	n/a	n/a
	2000	£3.70	£0.10	2.8%
	2001	£4.10	£0.40	10.8%
	2002	£4.20	£0.10	2.4%
	2003	£4.50	£0.30	7.1%
	2004	£4.85	£0.35	7.8%
	2005	£5.03	£0.18	3.7%
	2006	£5.35	£0.32	6.4%
	2007	£5.52	£0.17	3.2%
	2008	£5.73	£0.21	3.8%
	2009	£5.80	£0.07	1.2%
	2010	£5.93	£0.13	2.2%
	2011	£6.08	£0.15	2.5%
	2012	£6.19	£0.11	1.8%
	2013	£6.31	£0.12	1.9%
Projection	2014	£6.50	£0.19	3.0%
	2015	£6.70	£0.20	3.1%
	2016	£7.20	£0.50	7.5%
	2017	£7.65	£0.45	6.3%
	2018	£8.10	£0.45	5.9%
	2019	£8.55	£0.45	5.6%
	2020	£9.00	£0.45	5.3%

Source: Authors’ calculations from ASHE 2015

## How will the National Living Wage affect Greater Manchester?

**9.4** How many people are likely to benefit from the new £7.20 rate in Greater Manchester? Using the ASHE data on the jobs of Greater Manchester residents, estimates indicate that 13% of the jobs of residents (approximately 130,000 jobs) in Greater Manchester are likely to see a direct wage rise<sup>134</sup> as a result of the NLW. The borough with highest proportion of gainers is Rochdale with 16% of jobs which are likely to see a pay rise (about 11,600 jobs).

**9.5** According to the Low Pay Commission, 1.8 million workers will see a pay rise as a direct result of the NLW. Yet once pay differentials are also factored in (for example, workers on pay rates slightly above the legal pay floor seeking to maintain their relative pay position), calculations by the Resolution Foundation estimate that about one in six workers nationally will see a wage rise as a result of the NLW<sup>135</sup> with about one in three gaining in Britain's 'low pay hotspots'. Part-time workers are much more likely to see wage gains than full timers. The table below shows the estimates for Greater Manchester.

**9.6 Table 22: Estimates of Proportions and Numbers Benefiting from £7.20 NLW (25 and above year olds), April 2016**

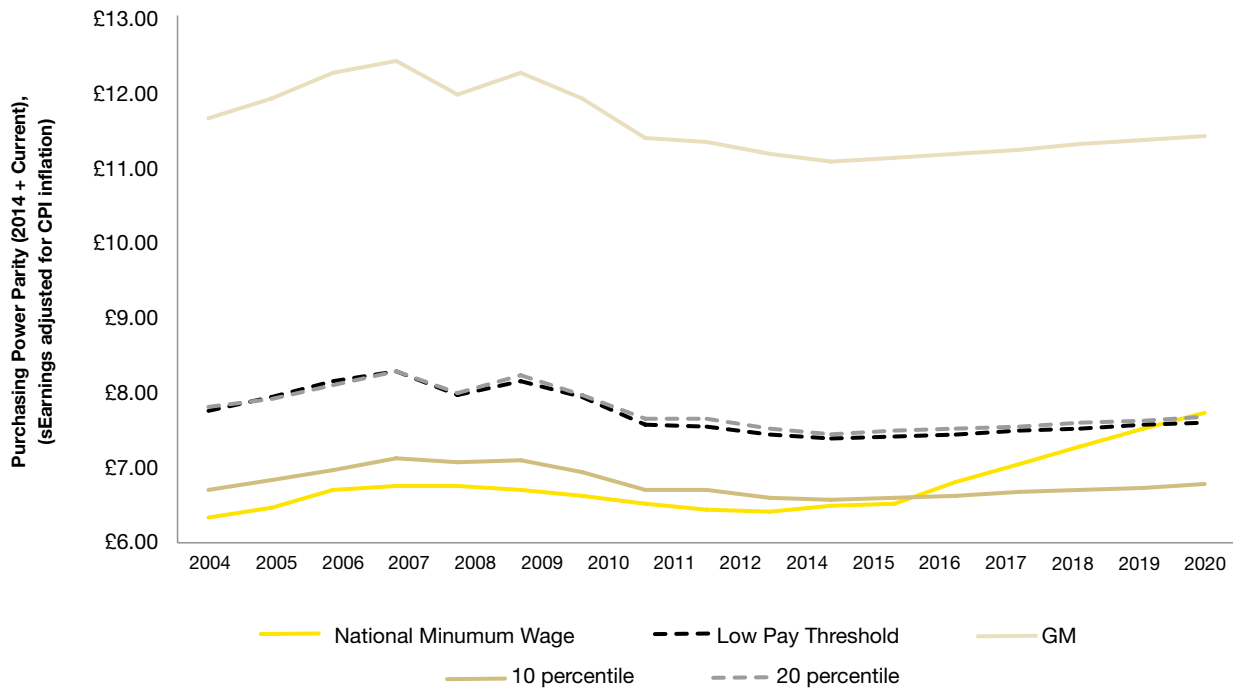
	Jobs held by people over 25 years paying below NLW	% of jobs held by over 25 year olds paying below NLW
Bolton	13,650	15%
Bury	7,720	10%
Manchester	25,520	15%
Oldham	10,330	14%
Rochdale	11,610	16%
Salford	11,670	13%
Stockport	12,810	11%
Tameside	11,350	14%
Trafford	10,500	11%
Wigan	15,630	12%
Greater Manchester MC	129,960	13%

**9.7** The change in the rate means that the legal pay floor is likely to cover a significantly larger proportion of the workforce than previously. In 2014, the NMW in Greater Manchester affected between about 7% and 10%. The new rate moves the proportion higher. However, it is important to remember that we do not know what will happen to inflation, jobs prospects or the wider economy in the next five years which renders the calculation of impact speculative in the years to 2020. In the chart below we assume inflation will rise between 2015 and 2020 at 0.5% annually. If this assumption holds, the NMW/NLW will rise at a much faster rate than earnings and prices in general: 18.1% compared with 2.5% over the five years in question. It will mean that the NLW is likely to rise to 60% of the median (from 53.9% in 2015). This moves the new NMW into unknown territory: the 'bite' (the pay floor as a percentage of the median) has never been so high.

<sup>134</sup> Publicly available ASHE data is imperfect for these calculations, so estimates have been derived by combining ASHE data on wages with LFS data on the ages of employees. It is also worth bearing in mind that workers who are on rates above the legal pay floor are also likely to see wage gains as employers seek to maintain pay differentials. ASHE jobs numbers need treating with caution and differ from other data sources, for example the Business Register and Employment Survey. For further national level estimates of the impact, see Low Pay Commission: The National Minimum Wage, 2016, BIS, 2016

<sup>135</sup> See Resolution Foundation, Press Release, Wednesday 30 March 2016

**Figure 35: Wage Projections 2015 2020, accounting for CPI Inflation**



Source: Authors' calculations from ASHE

**9.8** Much will depend on the reactions of employers. The funding of the additional wage has to come from somewhere. Obvious candidates include cutting jobs, reducing hours, reducing profits or increasing prices (or funding), lifting productivity or some combination of all of the above. Inevitably, given the concentrations of low pay in certain sectors, industries such as retail, hospitality, care and cleaning will be disproportionately affected. According to a report from the CIPD and Resolution Foundation, published in February 2016, more than half of employers will be affected by the national living wage<sup>136</sup>. Although the single most popular response was to raise productivity (30%) there was acknowledgement that this can be easier to say than to do. Some 22% planned to absorb the costs in lower profits. Others planned to cut jobs (15%), raise prices (15%) or cut hours (9%).

**9.9** Dire warnings about the impact of the NMW have been disproved before. Nevertheless, perspectives have been mixed. For Whitbread, the owner of Costa Coffee and Premier Inns, 34,000 staff are paid less than the living wage and it anticipates a cost increase of between £15 and £20 million. It has warned prices will have to rise<sup>137</sup>. According to Care England, a body which represents the care industry, "without adequate funding to pay for the National Living Wage, the care sector is at serious risk of catastrophic collapse."<sup>138</sup> The Local Government Association anticipates that the NLW will cost councils an additional £1bn a year by 2020 in an era of funding reductions<sup>139</sup>. Elsewhere, cuts to 'enhanced' pay rates – for example for working Sundays, evenings and Bank Holidays – are expected.

<sup>136</sup> Weighing Up the Wage Floor: Employer Responses to the National Living Wage, Policy report, CIPD/Resolution Foundation, February 2016

<sup>137</sup> See Daily Telegraph, 'Costa Owner Whitbread Warns Living Wage Will Hit Prices', 8 Sept 2015; <http://www.telegraph.co.uk/finance/newsbysector/retailandconsumer/leisure/11850173/Costa-owner-Whitbread-warns-living-wage-could-hit-prices.html>

<sup>138</sup> BBC News, National Living Wage will 'damage care homes', 20 August 2015; <http://www.bbc.co.uk/news/health-33986252>

<sup>139</sup> See Local Government Association Press Release, 13 July 2015, [http://www.local.gov.uk/media-releases/-/journal\\_content/56/10180/7386419/NEWS](http://www.local.gov.uk/media-releases/-/journal_content/56/10180/7386419/NEWS)



**9.10** According to the Office for Budgetary Responsibility (OBR), 60,000 job losses are likely<sup>140</sup> from the NLW changes, but this will be dwarfed by the growth of new jobs, with 1.1 million being added by 2021. Employment (excluding self-employment) in Greater Manchester is 4.08% of the UK total. Therefore, assuming the OBR's forecast of the impact is shared proportionately across the UK (unlikely in practice) Greater Manchester can expect 44,880 new jobs to 2021 and will lose 2,448 as a result of the NMW. However, this calculation does not allow for two important factors: a higher incidence of low wage work in Greater Manchester and a higher rate of employment growth compared with the UK<sup>141</sup>.

## Personal Allowance

**9.11** The government's aim is that that the higher NLW reform is expected to work in tandem with the lifting of the personal allowance to £11,500 from April 2017 from its current level of £11,000 (as of April 2016). According to publicly available ASHE data, approximately 18% of employees earned less than this figure in 2016. It plans to lift workers undertaking 30 hours a week at the NLW out of income tax altogether (although low paid workers will still be liable for national insurance (NI) contributions).

**9.12** The table below presents income tax and NI calculations for low paid workers on the NLW (£7.20 an hour). A total of 18 hours a week is the average for part-time workers while 37.5 hours is the average for full-time workers, but 30 hours is the technical definition of a full-time job and is the one that the government benchmarks tax impact against. In 2016, it appears that NLW workers will continue to be liable for a small amount of tax until April 2017.

**9.13** Two points are worth making. First, the indicative calculation suggests that there may be (continued) disincentives to increasing hours. If minimum wage workers increase their hours from 30 a week up to a more typical working week of 35 or more hours they would face fairly steep marginal tax increases. For example, if a worker on £7.20 an hour in 2016/17 sought to lift their hours from 30 to 35 a week they would pay an additional £1,273 in income tax per year. Second, for most low paid workers NI is a bigger item of expenditure than income tax, yet NI is not included in tax calculations.

**Table 23: Indicative Calculations of Earnings of NLW Worker (25+, £7.20 an hour)  
Using £11,000 Personal Allowance, 2016/17**

Hours	NMW	Income per Week	Income per Year	Taxable	Tax Owed	NI (annual)	Net Income	Net as % of Gross
18	£7.20	£129.60	£6,739.20	£0.00	£0.00	£0.00	£6,739.20	100%
30	£7.20	£216.00	£11,232.00	£232.00	£46.40	£380.64	£10,804.96	96%
35	£7.20	£252.00	£13,104.00	£2,104.00	£420.80	£605.28	£12,077.92	92%
37.5	£7.20	£270.00	£14,040.00	£3,040.00	£608.00	£717.60	£12,714.40	91%
40	£7.20	£288.00	£14,976.00	£3,976.00	£795.20	£829.92	£13,350.88	89%

Source: Authors' calculations

<sup>140</sup> See, p 34 of the Budget document here,

[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/443232/50325\\_Summer\\_Budget\\_15\\_Web\\_Accessible.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/443232/50325_Summer_Budget_15_Web_Accessible.pdf)

<sup>141</sup> New minimum wages for younger workers were confirmed in the budget of March 2016. 21-24 year olds will receive a new rate of £6.95 from October 2016. This is an increase of 25p an hour (3.7%), compared with the jump of 50p (7.5%) an hour that the NLW introduces for 25+ year olds. 18-20 year olds also receive an increase of 25p (4.7%) to £5.55 an hour from £5.30 today. 16-17 year olds receive a smaller rise of 3.4% to £4.00 an hour. Apprentices are also to receive lower pay rises – to £3.40 an hour from the current £3.30 (3%).



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## The future of the real living wage

- 9.14** So in the light of these changes, what does the future look like for the 'real' living wage? And what additional gains would flow to Greater Manchester if more employers took up the concept?
- 9.15** The living wage has transformed the low pay debate in a very short space of time. It has only existed outside London since 2011. Since then, it has become well-established as a campaigning vehicle to the extent that the Conservative Party manifesto endorsed it for the May 2015 election, while drawing attention to its voluntary nature<sup>142</sup>. Arguably, the concept of a NLW also pays homage to it, although, as noted previously, in monetary terms, the NLW is not a 'real' living wage.
- 9.16** Many local authorities in Greater Manchester currently pay the living wage for outside London, but Salford is the only borough that is accredited by the Living Wage Foundation. A survey by Unison found that 41% of local authorities in the North West paid the living wage, compared with 27.5% in England and Wales as a whole<sup>143</sup>. The London Borough of Brent is believed to be the first to incentivise local businesses to pay it with the offer of a one-off reduction in business rates of up to £5,000.
- 9.17** An important aspect of living wage campaigns is that the argument in favour is not merely advanced in moral terms, but also in terms of a 'business case'. Guy Stallard, Head of Facilities at KPMG, has argued "a living wage makes sense for business because to have an efficient and effective operation, firms require staff who are motivated, rewarded and incentivised to go that extra mile in servicing customer needs."<sup>144</sup> However, it is notable that many of the businesses which have championed the living wage to date pride themselves on having ethical brands, do not operate in low wage sectors, and tend to have small numbers of low paid staff<sup>145</sup> who are typically contracted out. These kinds of arguments also link to related concepts, such as employee engagement and high performance working, which converge on the premise that better paid, better treated and better managed employees deliver improved customer experiences, productivity and financial results.
- 9.18** A critical question is how to assess the gains and losses

from a more widespread adoption of a living wage. Potential gainers and losers include individual low paid workers (financial benefits from pay increase versus risk of job losses); the Treasury (reduced tax credit bill, potentially larger income tax and NI take); employers (increased wage bill; workforce uncertainty; potential better motivated workforce) and – most difficult to assess – the benefits to the wider economy. Depending on the specification of the fiscal multiplier used for calculations, a living wage could also have a wider economic stimulus effect, boosting demand and growth, reducing earnings inequality and increasing the share of wages in national income<sup>146</sup>.

- 9.19** According to a Resolution Foundation/IPPR report, the greatest beneficiary is likely to be the Treasury. It estimates a gross saving of £3.6bn<sup>147</sup> and says six million jobs could benefit. Its model also suggests that 160,000 jobs would be lost and estimates the gross earnings of the workforce could rise by £6.5bn, an average of £850 per household. Elsewhere, the Living Wage Foundation estimates £4.2bn could be saved by the Treasury<sup>148</sup>.
- 9.20** Previous New Economy research into a possible Manchester Living Wage found that a living wage "is likely to have a positive impact on wages for some of the lowest paid, with negligible negative economic impacts"<sup>149</sup>. The report argued that as well as raising incomes, local authorities also needed to reduce living costs through expanding house building and transport schemes that benefited the lowest earners and opened more opportunities for work further afield. The report found: "The impact of Manchester adopting a living wage policy to address low pay is, in isolation, not likely to be sufficient or targeted enough to deal with the acute challenges faced by many at the bottom end of the earnings scale. It is also likely to fall short of raising annual incomes sufficiently, and fails to tackle on-going rises in costs facing the lowest paid."

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<sup>142</sup> Conservative Party manifesto, p21

<sup>143</sup> See <http://www.lgcplus.com/news/third-of-authorities-adopt-living-wage/5067052.article>

<sup>144</sup> See, Sweeney, E, Making Work Better, An Agenda for Government, Independent Inquiry Into the World of Work, Smith Institute, 2014, p51

<sup>145</sup> An exception to this was the announcement by the Coop that it intended to pay the living wage. See <http://www.co-operativecreditunion.coop/blog/news/2015/supporting-the-living-wage-campaign/>

<sup>146</sup> This argument has been made by Reed, H., op cit, 2013

<sup>147</sup> Lawton, K., Pennycock, M., Beyond the Bottom Line: The Challenges and Opportunities of a Living Wage, Resolution Foundation/IPPR, January 2013

<sup>148</sup> Living Wage Commission (2014) Working for poverty: the scale of the problem of low pay and working poverty in the UK.

<sup>149</sup> Holden, J., Raikes, L., Pay Up? Living Costs and the Living Wage in Manchester, New Economy Working Paper, 009, New Economy, July 2012

**9.21** Evidence about the local economic impact of the living wage is scarce. But according to a report from the Centre for Local Economic Strategies (CLES)<sup>150</sup>, commissioned by Manchester City Council and carried out among the council's own contractors, 26.4% of suppliers currently pay the Living Wage and some 21% of social care providers pay it (the respondent base was heavily skewed towards social care). All suppliers in construction, housing, environmental services, professional services and taxi services paid the living wage. A total of 45.5% had been paying the living wage for about two years. Among the benefits cited were loyalty, retention, better staff, a happier workforce and reduced dependence on in-work benefits. But disadvantages included competitive disadvantage and that the living wage was not matched by contract value uplifts. Among suppliers which paid the living wage 50% said they encouraged their own suppliers to pay it. Among suppliers not paying the living wage, 43.8% said they planned to do so – across all sectors. The main barriers identified were: cost, decreasing LA contract values and fee rates.

**9.22** The report found that among local authorities, there is general uncertainty about the cost of implementing it: estimates ranged from £1m to £100,000 a year. Some 60% of local authorities which have the living wage are encouraging their suppliers to adopt it, while less than half have inserted clauses into tender criteria (one popular model for this is embedding a living wage clause into a local employment charter which suppliers must sign up to (eg. Birmingham City Council). However, according to CLES: "It is important to note that authorities reflected that stipulated clauses were not as effective as encouragement of the supply chain."<sup>151</sup>

**9.23** According to full year data from ASHE 2014, 241,000 jobs in Greater Manchester did not pay the living wage in 2014. This was comprised of approximately 15% of full time workers and 46% of part time. The table below offers an indicative calculation of the likely gain to the Greater Manchester economy on the (admittedly unlikely) assumption that all employees were paid at least at the level of the real living wage. Were this to be the case, the aggregate wage gain would total some £453.7million.

**Table 24: Estimate additional costs of all employees receiving the living wage as a minimum**

	GM jobs paying below the LW (ASHE)	Average hours worked per week (ASHE)	Earning gap estimate - hourly earnings	Weekly additional earnings per employee	Weekly additional earnings across GM	Annual additional earnings
Full-time employees	110,000	37.8	£1.35	£51.03	£5,613,300	£291,891,600
Part-time employees	131,000	17.6	£1.35	£23.76	£3,112,560	£161,853,120
<b>Total</b>	<b>241,000</b>					<b>£453,744,720</b>

Source: Authors' calculations from ASHE, 2014

## Conclusions

**9.24** One argument likely to be encountered is that the new national living wage reduces the case for the 'real' living wage, especially if the two rates converge at broadly comparable levels. The advent of the national living wage may prompt change in the rate-setting process for the real living wage – not least because the real living wage takes credits and benefits into account: less generous tax credit payments imply a higher wage rate will be needed. The living wage may rise at a faster rate in future to compensate<sup>152</sup>. Further themes to watch in future will be the effect on young people and on living wage campaigns in the capital. The national living wage does not apply to younger workers below the age of 25 (arguably providing an incentive to hire younger workers) and does not recognise the higher cost of living in London relative to the rest of the UK. Despite such considerations, the national living wage does not appear to have damaged the ability of living wage campaigners to 'recruit' new employers into paying the voluntary, higher, real living wage. Retailers such as Aldi, Lidl and Ikea, for example, all confirmed they plan to pay the higher rate since the announcement of the NLW was made.

<sup>150</sup> See Using Procurement Process to Encourage Living Wage Principles, Centre for Local Economic Strategies for Manchester City Council, August 2014

<sup>151</sup> Ibid

<sup>152</sup> Living wage rises were limited to increases of no more than 2% above average earnings

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# 10 Conclusions

**10.1** Greater Manchester is typical of many other city regions in the UK in the extent of low pay. It follows that the policy responses that are most likely to be of most practical benefit to low wage workers rest with the national government and its agencies. Yet action on a city regional level is a dimension of the low pay debate that tends to be downplayed. City regional policy can and should aim to accelerate and reinforce action to address the national culture of low paid work. The most obvious policy that directly affects wages is likely to be the living wage. As we argue below, there is clearly a role for the living wage in helping to address the challenge. Yet the complex array of issues tackled in this report, including skills, productivity, insecurity, working time and the strategic choices of businesses (and especially how these issues interact with one another) mean that there is no one single response that on its own could be regarded as sufficient. Instead, a range of policy interventions that push in different directions simultaneously are necessary to help respond to city regional low pay. A dynamic city region such as Greater Manchester has a valuable voice and perspective on low pay. It ought to help play a role in the national conversation on working poverty.

**10.2** This chapter reviews some of the principal themes and messages emerging from the report.

## Themes of the research

**10.3 Low pay as a job quality problem:** This report has focused on pay, but wages ought not to be seen in isolation from wider ‘bad work’ concerns: insecurity, low levels of autonomy, low skills and poor use of skills, working time flexibility, poor management practices, lack of opportunities and so on. From the perspective of the low paid themselves – at least those interviewed in the course of this research – wages tend not to be identified as the primary irritation of their work (insecurity, contracts and organisational management figure more prominently). Although particular policies target wages or taxes (for example, the NMW and living wage), the best designed policy responses invoke a package of measures that seek to support improvements in the quality of work.

**10.4 The care sector is a special case:** The care sector has emerged as being of particular concern. The care sector is a ‘medium skill, low pay’ industry that appears to ‘underpay’ relative to the skill level of the workforce. It has grown in terms of numbers of workers (4,200 new jobs between 2009 and 2014, of which the majority were low paid). Budget cuts, procurement decisions and cost minimisation strategies have had deleterious effects on job quality (including pay) in the sector, which has in turn been linked to poor patient outcomes<sup>153</sup>. Finally, it is a sector that under devolution, the city region has significant influence over. The dilemma for public sector commissioning bodies here, though, is that although there may be arguments in favour of imposing tougher social value clauses in procurement contracts (such as, for example, insisting that care contracts pay a living wage), it may be difficult in the current environment to add additional costs to care budgets. Furthermore, research has found that better procurement budgets alone do not mean that staff lower down the supply chain see the benefits<sup>154</sup>. Practically, it may be more beneficial to engage with supply chains to encourage better work rather than tie the hands of procurement specialists in contracting decisions<sup>155</sup>.

**10.5 Low pay is not just about skills:** Skills are related to pay levels, albeit in more subtle ways than are sometimes imagined. Although the possibility of individuals advancing themselves through education and skills is a time-honoured route out of poverty, nuance needs to be brought to bear on the relationship between skill acquisition and wages. Low levels of employer interest in using skill, and business models that reduce or obviate the expense of developing skills, render the relationship extremely complex. As well as skill, motivation and initiative are also important and these are not the same conceptually as ‘skills’. Many low paid workers believe the possibility of progression is simply an alien concept in their place of work. Therefore, intervention may be best targeted in three directions simultaneously: first, at business support that aims to lift the ambition of firms and move them towards higher value, more productive business models; second, that careers support and the skills system seeks to develop motivation as well as skills; and third, at ensuring the skills system does not just develop skills that serve to entrench the status

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<sup>153</sup> Philpott, J., *Rewarding Work for Low Paid Workers*, Joseph Rowntree Foundation, April 2014

<sup>154</sup> Robery, J., Grimshaw, D., Hebson, G., *Exploring the Limits to Local Authority Social Care Commissioning: Competing Pressures, Variable Practices and Unresponsive Providers*, Public Administration, Vol.91, No 2, (419-437), John Wiley and Sons, 2012; for every additional £1 spent on enhanced care support, workers see only 18p of the gain

<sup>155</sup> *Using Procurement Process to Encourage Living Wage Principles*, Centre for Local Economic Strategies for Manchester City Council, August 2014

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quo, but facilitates labour market progression through skill acquisition (for example, by ensuring that funding systems reward providers who can demonstrate progression among learners). There are good economic and also social reasons for policymakers aiming to raise skill levels. But the existence of 'medium skill, low pay' sectors, alongside the experience of recent years in which sharp rises in qualification levels have occurred simultaneously with a worsening low pay issue, need to encourage realism and nuance in what can be achieved through upskilling.

**10.6 Low pay has wider explanatory factors than productivity performance alone:** Low paying sectors clearly overlap to a significant degree with low productivity sectors. However, as argued in chapter four, it is an oversimplification to contend that the fundamental response to low pay lies only in raising productivity. There are three central reasons. First, there are other influences on pay besides productivity. These include bargaining power and cultural valuations of what certain types of work are 'worth' (for example, this argument has been used to help explain low pay in certain female dominated sectors, including care, textiles and personal services); in the case of care, low pay is explained by national and local funding arrangements as much as by marginal productivity. Employer's ability to use labour flexibility in ways that work to advance their interests shapes the entire nature of work in low wage sectors, including decisions around wage levels. These are different order considerations from the traditional accounts of marginal revenue product. Yet they are important in coming to a fuller understanding of low wage work. Second, as noted, most low pay/low productivity sectors in Greater Manchester have actually shown that they are capable of productivity gains (at least superior gains compared with other sectors) in the years since the recession. In other words, Greater Manchester's low pay sectors have recently proved themselves relatively productive – especially the retail sector. This performance, however, has yet to obviously feed into wages. The bigger productivity gaps lie in more knowledge intensive sectors such as financial services, property and the professions and it is these sectors that need to be targeted more aggressively to lift productivity and drive growth rather than the low wage sectors. And third, a more abstract point: productivity is an increasingly mysterious concept in a service dominated economy (and also an economy where low pay is most concentrated in services). Devised for an economy of tangible outputs, what productivity means for the jobs of nurses, teachers, beauticians, carers, agency casuals, cleaners and customer service workers is far from being obvious and uncontested – and often appears to imply worsening service quality. Perhaps as a result, it is not a concept that employers in these sectors tend to use very much; it lacks purchase on commercial realities in service sector businesses. For these reasons, this report argues it is wiser to position productivity is an important influence on work in the low wage sectors, but not necessarily the only fundamental driver worth discussion.

**10.7 Wider adoption of the living wage will not necessarily produce the largest fiscal savings:** From a public service reform perspective the largest savings are likely to flow from measures which aim to encourage lone parents and second income earners to increase their working hours rather than the wider adoption of the 'real' living wage. This is due to the tax credit system being in effect a form of subsidised childcare: it is notably more generous to families with children, while workers without children may often find themselves ineligible, even on relatively low incomes.

**10.8 Low pay needs to be understood in terms of sectors:** Low pay is highly sectorally concentrated. The low paying sectors account for 36% of all employment in Greater Manchester, but explain 66% of low pay. In hospitality, retail, cleaning and care, the vast majority of jobs pay less than the low pay threshold. These sectors will be in the vanguard of policy reform in the years ahead and will have the most difficulty in adapting to the national living wage.

**10.9 The recession has exacerbated low pay:** Workers on the very lowest rates of pay (10th percentile of the distribution) may not have seen their real incomes fall to the same extent as those higher up the income distribution, probably because the pay floor offered some modest 'protection' for the lowest paid workers. But at still low pay rates – albeit above the very lowest levels (20th percentile) – the impact has been disproportionate: workers at the 20th percentile saw a 10% fall in real pay between 2007 and 2014 – exactly the same as workers at the 80th percentile. This fall would have entailed very substantial drops in living standards among the working poor.

**10.10 How employers compete may also help explain low pay:** The evidence regarding business models is much less well developed than that around wages, skills or productivity. It is also necessarily more qualitative in nature. Nevertheless, as we showed in chapter 8, low wage, low skill work may be in part a reflection of strategic choice: if a business can be competitive by selling low cost goods and services, and does not require highly skilled (and well paid) staff, what is the incentive for businesses to develop workers and improve pay? Secondary analysis of UKCES data suggests 21% of Greater Employers in the city region pursue 'low cost, low value, low skill' business models. This compares with 18% for the UK as a whole. This low road approach implies lower demand for skills than would be the case if customised, differentiated, innovative (and in turn higher cost) products and services were being marketed by more employers. Some 45% of businesses in the UK have 'high or very high PMS strategies', according to data from the Employer Skills Survey<sup>156</sup>. In Greater Manchester the figure is 42%, although this is higher than other cities such as Sheffield and Liverpool. The tentative evidence around business models is a further influence on pay. Paying relatively low wages may be a viable business strategy in some sectors of the economy.

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Evidence surrounding business models suggests that part of the response to low pay could be to encourage businesses – for example through business support services, grant giving and workforce development – to rethink competitive strategies and focus on innovation, exports and workforce development.

## Considerations for Policymakers

- 10.11** In recent years reducing unemployment has been a priority locally and nationally. Whilst this focus needs to continue, Greater Manchester should also develop mechanisms and policy levers to aid in-work progression, encourage businesses to move up the value chain, reduce state support for people in work, and to address low pay.
- 10.12** This research was not aimed primarily at developing policy recommendations. Yet areas for future consideration by policymakers for further research and policy development could include:

## Skills and Employment

- 10.13** The research identifies that skills are related to pay levels, albeit in more subtle ways than are sometimes imagined. However, research also suggests there are significant numbers of employers who have low levels of interest in using skills and whose competitive strategy obviates the expense of developing skills. This finding may limit the potential productivity gains that could be achieved through improving upon current skills performance.
- 10.14** Devolution will be important given increased local influence over skills budgets. These powers can facilitate greater labour market progression and ensure public money is not being spent disproportionately on the labour supply of low wage sectors.
- 10.15** Future funding models and payment systems being considered as part of the devolution debate could seek explicitly to encourage progression for low-paid individuals. Skills system reform could include greater incentives for learning providers to target high quality jobs in sectors with progression opportunities. More widely, policymakers need to maximise the effectiveness of available funds (such as the European Social Fund and its potential post-Brexit replacements) that support skills interventions that will be of potential benefit to the low paid.

## Business Support

- 10.16** The research identifies that the ambition of increasing productivity rests partly on the strategic choices of firms around how they compete. The strategy of individual businesses is obviously something that is not directly subject to public policy. However, competitive strategy may be an agenda that can be shaped by policymakers – albeit to a relatively modest degree.
- 10.17** Where the public sector and its agencies offer business support, consultancy and grant-giving services, it may be possible to direct these activities towards helping firms to develop their business models to shift to higher value and away from a reliance on low cost, low skill strategies. Business support services can thus be used to help address bad job design, improve leadership and management skills, and develop ‘high performance’ working practices. An example of such a programme is the Investors in People (IIP) framework.
- 10.18** Devolution brings an opportunity to develop a set of principles that will inform business support, and to explore the potential benefits of a differentiated business support service offer that reflects the value of the jobs generated through the support and/or the productivity gained. For example, a higher level of support could be given to sectors and businesses which: offer the best opportunities for high quality jobs or productivity gains; are looking to transition to a new business model; are focused on innovation and export; and are good employers that are wholly committed to developing their workforces.
- 10.19** Workforce development that brings together skills and business support at the outset is vital to ensure businesses can access, utilise and invest in the skills they need to grow. Greater Manchester as a city region could encourage more employers to develop their workforces.

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<sup>156</sup> UKCES, 2013, available at <https://www.gov.uk/government/collections/ukces-employer-skills-survey-2013>

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## The Living Wage

- 10.20** The living wage is a further promising potential avenue for addressing low pay – but, as noted above, needs to be positioned as part of a policy package rather than as a single-issue intervention.
- 10.21** Possible ways to support the living wage are for local authorities, and the Greater Manchester Combined Authority, to act as public sector leaders and commit to paying the living wage to directly employed staff, and to consider that the living wage is referred to in all contract tendering documentation as part of social value tendering processes.
- 10.22** Furthermore, the public sector can also work alongside local businesses interested in addressing low pay to encourage further uptake of the living wage and to act as local living wage champions.

## Job Security

- 10.23** The research identifies that employees have a wide range of concerns around job insecurity, low levels of autonomy, low skills and poor use of skills. The burdens for low wage workers caused by extended outsourcing and contracting out in both private and public sectors (for example, the two tier workforce, organisational turmoil and opaque accountability chains) emerged extremely strongly from interviews.
- 10.24** In order to raise living standards and achieve economic sustainability the Combined Authority and Greater Manchester local authorities could look to minimise the use of zero hours contracts (ZHCs) within their workforces and to use social value tendering as a mechanism for deterring the use of inappropriate or excessive ZHCs among contractors.

## Childcare

- 10.25** £1.556 bn is spent on in-work tax credits each year. The research indicates that the greatest potential for reducing dependence on tax credits in Greater Manchester is in increasing the working time of second earners (and to a lesser extent lone parents). One key contributory factor to enable this is affordable and flexible childcare. Nationally 60% of families utilise some form of formal childcare.
- 10.26** Government has announced that all families with children aged three and four will receive 30 hours free childcare per week, beginning for some areas from 2016 – up from the current entitlement of 15 hours. Some childcare providers have said that the funding offered is not sufficient to make it worthwhile, meaning that there may be a shortage of places. Greater Manchester could prepare to maximise benefits in addressing low pay and productivity through this intervention and to support the childcare sector in order to make this work.
- 10.27** Greater Manchester and Greater Manchester local authorities could, in dialogue with central government, seek to explore the potential of piloting flexibilities through devolution so as to ensure the intervention is reaching low income workers, and that provision is developing in the appropriate forms. This could include the design of a Greater Manchester childcare programme that is flexible and cost effective and makes best use of the city region's assets.

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<sup>157</sup> The Economic and Fiscal Impact of Low Pay in Greater Manchester, NIESR, 2016, forthcoming

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