States of Jersey
Economics Unit
2015

Economic impact of a living wage for Jersey

1 Executive Summary

Any estimate of the impact of introducing the living wage in Jersey is limited by the difficulty in predicting how many employers will sign up, or how many employees will be affected. Experience from the UK suggests that accreditation of employers has resulted in wage increases for a small number of staff.

Firms may benefit from implementing the living wage, through productivity improvements, reputational benefits, improving competitiveness or lower staff turnover – but it is not clear why firms would not choose to implement the higher wages anyway.

With a voluntary living wage, there is unlikely to be any impact on inflation or aggregate employment. There may be some impact on competitiveness or employment if firms feel forced into implementing higher wages, e.g. through moral pressure.

There may be some reduction in benefits or increase in personal income tax but the impact will also depend on the level of take-up and number of employees affected. The impact of States expenditure will be very much dependent on what level the living wage might be in comparison to existing States hourly rates.

2 Introduction

P.37/2013 requested an assessment of *"the overall economic impact and business costs by sector"* of introducing a living wage in Jersey. The Economics Unit have carried out an economic impact assessment (EIA) to assess this and have also been asked to include an assessment of the following two elements of P.37/2013:

(d) the effect on States revenues

(f) methods for, and timing of, the introduction of the living wage

This assessment has been based on a number of assumptions:

a. Any living wage introduced in Jersey will be voluntary;
b. Any living wage would only be introduced if it were higher than the minimum wage;
c. Employers will only pay their staff the living wage if they believe it is affordable;
d. Employers will only pay their staff the living wage if they believe they can remain competitive.

The first assumption above has important implications for the approach taken by this assessment. With a voluntary living wage, there is no way to know in advance what the level of take-up might be from employers on the Island. The impact will largely depend on the number of firms implementing the living wage and the characteristics of those firms. For example, some of the firms signing up may have few staff earning less than the initial living wage and therefore the impact in these firms will be limited.

In the UK, approximately 800 employers are officially accredited with the Living Wage Foundation – less than 0.1 per cent of the 1.2 million employers in the UK (BIS 2013: "Business Population Estimates 2013"). However, research by the British Chambers of Commerce suggests that as much as 60 per cent of their membership pay at least a living wage to all directly employed staff (BCC 2014: "Majority of businesses pay, or aspire to pay, living wage"). It is not possible to assess how many of these employers will have been influenced by the existence of a precisely defined living wage in the UK – and how many would be paying the same amounts anyway.

The Living Wage Commission's final report ("Work that pays, the final report of the Living Wage Commission") suggested that each accredited employer brought an average of 64 staff up to the UK's living wage. At the time of the report, it was estimated that accredited employers had brought 45,500 employees up to the living wage, a relatively small impact given that it is estimated that approximately five million employees in the UK remain below the living wage. However, there may be further employers who have brought staff up to the living wage, without becoming accredited with the Living Wage Foundation.

An evaluation carried out in 2014 for Trust for London ("Living Wage Special Initiative Evaluation") estimates that only 11,000-12,000 workers in London have received a wage increase – a small proportion of total employment in London and only 2% of low-paid workers.

Even in comparator jurisdictions that already have a living wage, therefore, it is difficult to know what the impact of introducing a voluntary living wage has been. The level of take-up in Jersey will not necessarily follow that in comparators such as the UK, as the business environment is considerably different.

Accepting that it is impossible to predict the number of employers who would introduce the living wage, or the number of employees who would be impacted, it is possible at a high level to consider which firms might implement it. Those firms who do implement the living wage are likely to only do so if they see it as affordable. Further, employers will only implement it either if they think it will have some positive impact on their business – in terms of increased productivity or reputational impacts – or for ethical reasons, or a combination of the two.

The Statistics Unit collected data on low-paid (£6.85 or less) staff in Jersey, as part of their 2013 average earnings survey. This found that, of 5,200 employees paid less than £6.85, the majority (90 per cent) were in the *hotels, bars and restaurants*; *other business activities* and *agriculture* sectors.

The employers implementing the living wage may be in different sectors from those who employ significant numbers on a low hourly rate. The UK experience suggests that most accredited employers are in the *charity*, *finance*, *health*, *education*, *housing*, *law*, *government* or *media* sectors. This contrasts with the lowest paid sectors in the UK, which are *hospitality*, *agriculture*, *administrative & support service activities*, and *wholesale & retail*. Research in the UK (Markit 2014: “Living Wage Research for KPMG”) suggests that the occupations with the highest numbers of employees paid below living wage are *sales and retail assistants*, *kitchen and catering assistants*, and *care workers and home carers*. There are estimated 1.45m employees in these three occupations earning below the UK’s living wage – more than a quarter of the total in all sectors. There are likely to be few staff in these occupations in any sector which has significant numbers of accredited companies. Considerable media coverage has been given to the fact that no major UK retailer has yet been accredited – suggesting that companies accredited to date will have little impact on the category with the highest number of below living wage earners – sales and retail assistants.

To summarise this section, any estimate of the impact of introducing the living wage in Jersey is limited by the difficulty in predicting how many employers will sign up, or how many employees will be affected. Section 3 looks at the economic impacts on this basis, assuming that employers will only implement it they view it as affordable and can make a case on either business or ethical grounds. Section 4 looks at the impact on States finances. Section 5 considers issues around the timing of implementation by employers in Jersey.

3 Economic Impact

As stated in section 1, the impact on the economy as a whole will be dependent on how many employers implement the living wage and on how many members of staff are given higher wages as a result. As it is not possible to estimate the level of take-up, it is not possible to estimate the aggregate impact on the economy. However, it is possible to look at what might generally be expected, albeit this will vary between employers. Therefore, this section focusses on four specific areas of impact:

- Impact on firms who choose to implement the living wage;
- Impact on firms who choose not to implement the living wage;
- Impact on employment;
- Impact on inflation.

3.1 Impact on firms who choose to implement the living wage

The final report of the UK's Living Wage Commission (Living Wage Commission 2014: "Work that pays, the final report of the Living Wage Commission") stated that:

"Several studies have been carried out into the business case for the Living Wage, with a general conclusion that there are clear benefits on productivity, staff turnover, absenteeism, stability, motivation and commitment, and business reputation."

While these benefits may not be available to all employers, a rational employer will implement the living wage only if they consider it affordable and only if they believe there is a sufficient case for it on either business or ethical grounds. Not all firms are likely to see the business benefits as outweighing the additional cost, but it is possible to look at how some of the claimed benefits might occur for employers. This section looks at the potential for productivity impacts, impacts on recruitment / staff turnover, reputational impacts and impacts on competitiveness.

3.1.1 Productivity impacts

The argument that higher wages result in productivity gains is related to the concept of *efficiency wages*, i.e. the theory that employers will set wages above the market-clearing level in order to benefit from productivity gains or lower staff turnover. Higher wages not only boost morale but increase the cost to the individual if they were to lose their job (and are forced to take a job at the lower market-cleaning wage rate). However, it is not entirely clear why companies would not be paying such higher wages anyway, if they believed the productivity gains would outweigh the additional cost.

Further, implementing the living wage will increase the cost of labour and may cause employers to seek to find efficiencies, e.g. more efficient use of resources, adoption of information technology or modernising equipment. This will increase productivity, allowing the employer to pay higher wages without impacting on profits. However, employers may have a limited ability to identify efficiencies which they would not have otherwise implemented. Setting a living wage for Jersey may, however, prompt employers to think about how they could implement it for their staff, without negatively impacting on the business.

3.1.2 Impact on recruitment / staff turnover

Increasing the wage rate of a job will generally tend to increase the interest in the vacancy, and this will be the case for employers who have increased the wage rate of a particular post after introducing the living wage. This will therefore lead to potentially higher-skilled or more experienced applicants applying for a post, or to a shorter or less expensive search process to find qualified staff.

There may also be some recruitment benefit by being accredited as a living wage employer, even for posts which would have been paid above living wage anyway. Paying the living wage could form part of a package of measures that a business might take to be seen as an ethical employer and this will increase interest in working for the company, giving the company an advantage in recruitment.

The theory of *efficiency wages* also applies to staff turnover. This suggests that employers will pay higher wages in order to reduce staff turnover and thereby avoid some of the costs associated with recruitment.

3.1.3 Reputational impacts

Section 3.1.2 indicated that being a living wage employer can have reputational benefits in terms of staff recruitment, but this will also be the case for a company's reputation in the eyes of customers. Firms may use it as a marketing tool to attract business, as they can use the accreditation to demonstrate a certain company ethos which will be attractive to some potential customers. This might fit with other similar initiatives which indicate a fair or ethical approach to business, such as fair trade or support for local charities.

For export-focused companies, there may be limited opportunities to promote this reputation to international customers. However, there will be some circumstances where clients will be discerning over which companies they deal with and the living wage accreditation could be a positive selling point in these circumstances.

3.1.4 Impact on competitiveness

Many businesses in Jersey operate in a competitive global market – not just sectors which export goods (e.g. agriculture) and services (e.g. finance) but also the tourism sector which competes with destinations internationally and businesses who compete with imports in the local market. For such firms, any increase in costs will impact on the firm's competitiveness against both local competitors and on the international marketplace. Firms in other jurisdictions without a living wage may have wage costs set at market-clearing rates and may therefore become more competitive compared to a Jersey firm who implements the living wage. However, this may be offset by the productivity improvements and reputational impacts gained by firms implementing the living wage.

With a voluntary living wage, a rational employer would not choose to sign up if they think it would make them uncompetitive, either locally or internationally. However, this would be a different matter if firms were somehow forced into increasing wages. This would be the case for a compulsory living wage but might also be if firms felt coerced into signing up due to moral pressure within Jersey which was not felt by competitors elsewhere.

3.2 Impact on firms who choose not to implement the living wage

The economic impact will not be limited only to firms who do implement the living wage; there will also be an impact on firms who do not. As indicated in section 3.1.2, employers who have signed up to the living wage may have an advantage in recruitment. Therefore it may be more difficult for other firms to recruit, if wages are lower relative to those competing for the same labour. This may result in more expensive recruitment efforts, or firms recruiting employees with lower skills or less experience than would otherwise have been the case.

It is possible that firms who do not implement the living wage may gain some advantage over their competitors who do implement the living wage. This will happen if the labour costs of their competitors increase and this has to be passed on in higher costs to the customer. Though companies are unlikely to implement the living wage if it would make them uncompetitive. Alternatively, if locally-based competitors are able to benefit from productivity improvements as a result of implementing the living wage, this would see competitive pressures increase for firms who are not able to do so. This could compound existing pressures as firms who are unable to afford the living wage will generally have been less productive to begin with.

There will also be reputational risks for companies who do not implement the living wage, particularly if the public and/or media have a negative perception of these companies. Sectors such as hospitality and agriculture have the highest proportions of staff on low hourly rates and therefore would have the most significant cost implications of implementing the living wage. If many employers in these sectors felt unable to increase wages due to competitive pressures, it may have a negative impact on the reputation of these sectors as a whole. For export-focussed sectors, it is not clear that their reputation would necessarily be affected outside Jersey, but their local reputation may exacerbate difficulties these sectors already report in recruiting locally.

3.3 Impact on employment

A compulsory living wage would be likely to result in some job losses in low paying sectors, as firms reduce their total employment in order to control labour costs. While some studies suggest that the induced impacts of additional spending would result in net job creation, others have found a net negative impact. A compulsory living wage may see job losses at the level of the individual firm but may not mean job losses at an economy-wide level, depending on how the economy adjusts.

The first-round impacts are much less clear for a voluntary living wage. On the face of it, some employers may choose to pay higher wages to a smaller number of staff, if they can maintain their level of output – but it is difficult to see how this opportunity would not exist before introduction of a living wage. Where this does happen, it would result in the company's productivity improving as the number of staff reduces. With a voluntary living wage, other firms will still be paying the market-clearing rate so there will not be any impact on aggregate employment.

However, as indicated previously, employers may feel forced to implement the living wage, even if it is not compulsory. If this was widespread, it could have similar impacts to a compulsory living wage.

3.4 Impact on inflation

There are two ways in which implementation of the living wage could influence inflation – through the impact on costs, as employers pass on wage increases through higher prices; or through the impact on demand as increased income will result in more demand for spending (assuming the additional income is not all saved) and potentially push up prices.

The cost impact is unlikely to be significant. As has been stated before, with a voluntary living wage, employers will not generally increase wages if it required them to increase costs as this would make them uncompetitive. New or existing competitors would therefore be able to undercut the prices and therefore there would be no impact on inflation.

The demand impact will partially depend on the numbers of employees who have their wages increased. Lower paid staff, on average, tend to spend a greater proportion of any additional income so this will tend to feed through to additional demand. There may be a ripple effect within companies who implement the living wage, whereby employers increase the hourly rate of staff on higher pay scales, in order to maintain differentials. However, even with this impact, it is unlikely that it would have a significant impact on aggregate demand in Jersey. The effect would be even more insignificant for prices which are set based on global aggregate demand.

4 Effect on States finances

The impact on States finances will be mainly through:

- States wage bill;
- Increase in cost in supply chain;
- Impact on benefits and supplementation;
- Increased income tax receipts.

4.1 States wage bill

All States employees are paid at least £9.35/hour, with the exception of those on therapeutic or trainee rates. Therefore if the living wage were below this level, the only significant impact would be if the States were to pay contracted staff. No data were available on the salaries of contracted staff.

4.2 Cost of purchases

It is not possible to know what impact a living wage would have on the supply chain for the States. As indicated in section 3.1.4, firms would not be expected to increase wages where this would have an increase in their costs – so the impact may not be significant.

4.3 Benefits / supplementation

This is covered in section 9 of the detailed background report.

4.4 Income tax receipts

This is covered in section 9 of the detailed background report.

5 Methods of and timing of the introduction of the living wage

To the extent that this relates to introduction of the living wage by employers, this will vary by firm and is not an issue for government. Some firms will wish to wait to see the responses of their competitors, while others may immediately follow their UK parent company and seek accreditation.

Public pressure can have an impact – there have been media campaigns and consumer movements in the UK which have had mixed results. For example, student protests have led to implementation by universities but a long media campaign has failed to persuade any large retailer to sign up.