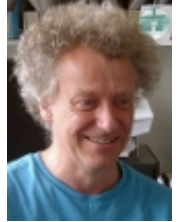


The National Living Wage: a policy experiment well worth trying

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With the dramatic increase in the minimum wage in the summer budget, many are wondering whether the policy might have negative implications for employment. [Alan Manning](#) writes that there might be substantial adverse effects, but the new policy is one well worth trying; evidence-based policymaking does require experimentation with policies whose effects are unknown.



The culmination of [George Osborne's budget](#) speech was the announcement of the introduction of the National Living Wage (NLW). Although borrowing terminology from the Living Wage Campaign, this was simply a higher minimum of £7.20 per hour from next April for those aged 25 and above and an ambition to raise it to 60 per cent of median earnings by 2020 with the Low Pay Commission being asked to plot that course.

To be sure this was intended in part as a counter-weight to the accusation that he is indifferent to the welfare of the poor and its presence at the end of the budget speech perhaps designed to distract attention away from the welfare cuts outlined elsewhere in the budget. And part of the appeal is that higher wages will improve the public finances as tax receipts rise and tax credits fall.

But, there is no denying the fact that this was a bold move – a rise of over almost 7.5 per cent in the minimum wage for older workers taking the minimum wage into uncharted areas.

Because of this it is hard to be sure of the consequences of this policy. The fear with the higher minimum wages is always that they cause sizeable job losses as labour becomes more expensive. The research conducted by the [Low Pay Commission](#) has found no evidence of this at the levels of minimum wages we have experienced so far but there must surely come a point at which this concern becomes relevant.

These fears can be over-played. The OBR estimates that the new NLW is 55 per cent of median earnings for the over 25s, very close to the ratio of the current NMW to overall median earnings and lower than the bite of the current minimum wage in the youth labour market. The OBR did estimate that it would cause modest job losses though the methodology used simply assumes that increases in minimum wages always reduce employment, an assumption that did not fare well when the NMW was introduced in 1999. I think the area where there is most concern is in social care, a sector where labour costs are a very high share of total costs and prices are largely determined by government.

There is also the concern that the government has seriously undermined the independence and integrity of the Low Pay Commission by first imposing the NLW next April and telling the LPC where it would like the future level to be. I would actually argue that this has strengthened the LPC.

Under its current remit it is very hard to see how it could have made as bold a move as the introduction of the NLW. It is an evidence-based body and it is hard to see how such a body can recommend a policy for which there is scant evidence as to its benefits (and costs). In recent years it has recommended only modest increases in minimum wages and it is difficult to discern the impact of these changes when other factors are always affecting the labour market.

Evidence-based policymaking does require experimentation with policies whose effects are unknown otherwise one simply preserves the status quo. It is as important to try new policies that one thinks have benefits as to have stringent ex-post analysis of those policies. I think the new policy is one well worth trying but I don't pretend to know that there will be no substantial adverse effects.

So I hope that the LPC will continue the excellent track record it has established to evaluate the NLW, recommending future increases only if the costs do not seem too large and recommending what needs to be done if it thinks the government's target of 60 per cent of median earnings is unwise, whether that is improved skills or lower taxes. I think this will give the LPC a new lease of life not signal the start of its demise.

Other countries have been pushing minimum wages higher in recent times. Germany introduced a national minimum wage in January at similar levels in relation to average earnings as the NLW. And some US cities are pushing to \$15 an hour, considerably higher. In future years we will know much better whether minimum wages at these levels are safe or not.

About the Author

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