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Spatial Economics Research Centre

Monday, 19 March 2012

The case for local pay

The weekend papers full of coverage on the move to regional pay. Some thoughts:

1. [Public servants in poorer regions to get lower pay](#) we are told by the Guardian. Misleading, at best, but captures the sentiment of many. In fact, what details we have suggest that this will be local, not regional and that pay will not be cut. Instead, once the pay freeze stops there will be higher wage increases in some areas than others. One way to do this would be to look at areas where it's difficult for the public sector to recruit high quality staff and allow wages to rise more there. Another would be to use finer grained data on (increases) in costs of living. Either of these would be better represented as 'public servants in high costs areas to get more pay'.

2. The most direct impact will be to raise the quality of public good provision in high cost areas. Colleagues at CEP, for example, suggest that low public sector wages in high cost areas lead to worse outcomes in the NHS. More preliminary evidence finds the same effect for schools and policing. Of course, addressing this through higher pay increases in high cost areas raises the possibility that these services would deteriorate in the poorer areas. Again, evidence from the NHS suggests this may not be a major concern because the effect is 'non-linear'. The bad effect of national wages in high cost areas are not offset by better outcomes in low cost areas (probably because higher quality staff in the high cost areas move to the private sector, rather than moving to the public sector elsewhere in the country).

3. What about the indirect costs on the local economies of disadvantaged areas? Here, we have very little evidence. In the short term, you could argue that the major issue in these areas is demand rather than supply. But these are not short term changes we are talking about - the differentials will tend emerge only in the long term (as small differences in pay increases work through). It's also reasonable to suggest that longer term higher public sector salaries do create a local distortion that works against the private sector. Here there is a clear tradeoff. Higher public sector wages provide a demand stimulus to local service sectors. This likely offsets the distortion on the supply side (which comes from the fact that they have to pay higher wages to compete with the public sector). On the other hand, manufacturing (and other tradable) industries which don't serve local markets lose out because they don't benefit from the demand stimulus, but do get hit by the supply side distortion. Preliminary evidence from my own research on public sector employment suggests that these effects can be economically important. In short, high public sector pay may 'distort' local economies (towards local services away from manufacturing) and make them more 'dependent' on the public sector than they would otherwise have been.

4. What about 'fairness'? Personally, I prefer to think in terms of equal reward for equal work - which means that wages *should* reflect the local cost of living (something this move tries to achieve). Others may have different views - although I am unclear in what sense *equal pay* is in any sense 'fair' in a specific context even if there may be other reasons for supporting it more generally (e.g. for male and female workers doing the same job at the same firm).

5. On the subject of fairness, it seems reasonable to think that the negative effects of national pay in high cost areas are disproportionately experienced by poorer families. Partly because they will be the ones earning this pay, partly because they can't opt out of poorly performing public sector services. Again, personally, I think this is a bad thing.

On balance, I think the case for local pay looks strong although, as the reaction of many makes clear, the politics are likely to be nasty.

Posted by [Prof Henry G. Overman](#) on [Monday, March 19, 2012](#)



4 comments:

Nick Gray said...

In point 2 you say, "probably because higher quality staff in the high cost areas move to the private sector, rather than moving to the public sector elsewhere in the country"

Are you saying that health outcomes are worse in high cost areas because medical staff who would otherwise work in the NHS choose instead to work in the private healthcare sector?

That's not super-convincing. Are there enough opportunities in private healthcare to accommodate that many "high quality" medics?

[19 March 2012 at 14:39](#)

Nick Gray said...

This comment has been removed by a blog administrator.

[19 March 2012 at 14:40](#)

Prof Henry G. Overman said...

 Nick,

The paper provides evidence to suggest that the effects likely come through the increased use of agency staff.

It seems quite reasonable that in high cost areas people who would have gone in to, say, nursing do something else - including private healthcare - leaving agency staff to take their place.

Regardless, the non-linearity is there - so if you don't buy that explanation I'd be interested to hear other possibilities. Why is the negative impact in high cost areas much stronger than the positive impact in low cost?

[19 March 2012 at 14:52](#)

Larry Sportello said...

1. Reward levels are different from 'labour costs' – rates of reward are not the same as costs of employing someone.
2. Basing your argument on one study? Do you do this in your day job?
3. You seem to have lost your ability to refer to any evidence and rely on assertion.
4. Again no evidence - the cost of living varies very little outside of London and the South East - which usually already have pay premiums in the public sector. The median weekly earnings across all sectors excluding these regions vary very little (the range is just £19 across 7 of the 11).
5. ??

[20 March 2012 at 17:17](#)

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