PROSPERITY INSTITUTE

The Case for Freezing the National Living Wage

Matthew Bowles and Emmanuel Igwe



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Endorsements

"With almost 1 million young people not in education, employment or training this report is timely and its recommendations very sound. The Government should adopt them in full."

—Lord Sharpe of Epsom OBE, Shadow Minister for Business and Trade

"When the minimum wage was introduced in 1999, it was well below the average wage, so it brought in the fair work practices promised by New Labour without damaging the employment market. As it has increased as a proportion of the average wage, the unintended effects have become apparent: flattening wage structures and reducing the number of entry-level jobs. This proposal from the Prosperity Institute is a proportionate, time-limited step in today's difficult economic environment. The employment market will improve and new opportunities will be created."

—Lord Elliott of Mickle Fell, President of Jobs Foundation

"We told the Government that raising the minimum wage, particularly to the current very high level, higher than most in the OECD, would mean fewer job vacancies, particularly for young people. The Government didn't listen. Our prediction has rapidly come true, with job vacancies plummeting and youth unemployment shooting up. For the sake of our youth, particularly, we need to reverse this situation as soon as we can."

—Lord Moynihan of Chelsea

"This excellent paper forensically examines the consequences of a minimum wage. It explains why conservatives were wrong to be worried about its employment effects initially but now it is seriously deleterious. It is clearly time to freeze the minimum wage."

—The Rt Hon. Sir Jacob Rees-Mogg

"The ramifications of minimum wages are poorly understood by politicians, many economists and the general public, and deserve fuller discussion. In the UK our minimum wage structure has gone well beyond what was originally envisaged and now involves the government effectively setting pay for around a fifth of the workforce, directly or indirectly. This is having a negative effect on employment and the workings of the jobs market. This report makes a strong case for a pause in the growth of the National Living Wage, the 'bite' of which in some parts of the country, and in some sectors, is a real deterrent to expanding employment opportunities—especially for young people."

—Len Shackleton, Professor of Economics, University of Buckingham

About the authors

Matthew Bowles is Senior Policy Researcher at the Prosperity Institute. He focuses on preparing actionable policy briefs while engaging with stakeholders to shape informed discussions. Matthew also provides op-eds and public commentary for external outlets. He is the author of the paper *Broken Windows Britain: A Plan for Policing Low-Level Crime and Disorder*.

Prior to joining the Prosperity Institute, Matthew led corporate relations and engagement as Strategic Partnerships Manager at the Institute of Economic Affairs (IEA). He also served as the Policy Advisor to the former Director General at the IEA.

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While working as an economist in the Department for Levelling Up, Housing and Communities, he was involved in economic appraisal modelling for projects such as the Brownfield Land Renewal Fund, Estate Regeneration Fund and Accommodation for Ex-Offenders. He also worked in the capacity of a policy adviser within the department.

He completed his PhD in International Business and Economics at the University of Greenwich. Whilst studying for his doctorate, he taught various modules to students reading Economics at the University of Greenwich and Business Management at the University of Newcastle.

Glossary

GVA: Gross value added

ITL: International Territorial Level

LPC: Low Pay Commission

NICs: National Insurance contributions

NLW: National Living Wage

NMW: National Minimum Wage

NEET: Not in education, employment or training

OBR: Office for Budget Responsibility

OECD: Organisation for Economic Co-operation and Development

ONS: Office for National Statistics

SMEs: Small and medium enterprises

Foreword

It must have been at least ten years ago now, but I remember watching a BBC compilation of humorous moments from its late-night current affairs programme *Question Time*. Bloopers and gaffes, as Danny Baker would call them. Studio lights going out, people storming off, accidental innuendos. Anything can happen on live TV! Sticking out like a sore thumb amongst the light-hearted nostalgia was a clip of a Conservative politician—I think it was Michael Howard—explaining that he was against introducing a minimum wage because it would lead to unemployment. The BBC put up a smug caption at the end of the clip saying something along the lines of "unemployment has gone down since the minimum wage was introduced in 1999".

And so, it did, but Howard (if it was he) was only repeating what economists had told him. The theory is perfectly sound: if employers are forced to pay £15 an hour and your labour is worth less than £15 an hour, you will not be able to find work. Some leftists consider this to be an immoral argument. No one, they say, is worth less than [insert your arbitrary figure here]. But we are not talking about the worth of the person. We are talking about the value that a person can add to the business. Employing people at a loss is a one-way road to bankruptcy, and unemployment will surely be the result.

An understanding that some people's labour is worth more than others, and that forcing employers to pay above the market rate will freeze them out of the labour market, is implicit in the current system which has lower rates for people aged under 21. It should be self-evident that a minimum wage of £100 an hour would bring the economy to its knees. It is equally obvious that a minimum wage of £5 an hour would make no real difference to anybody. At some point in between, the minimum wage gets so high that it causes significant and visible unemployment. The only question is where. In this paper, Matthew Bowles and Emmanuel Igwe argue that the tipping point has been reached and that it is time for a cooling-off period.

Successive governments have been keen to improve the lot of the lowest paid, not by growing the economy but by forcing employers to pay them more. "Britain deserves a pay rise", said George Osborne when he raised the minimum wage and rebranded it as the National Living Wage in 2015. Such generosity with other people's money led to the minimum wage rising from 46 per cent of the median wage in 1999 to 56 per cent in 2015. It currently stands at 66 per cent, one of the highest 'bite ratios' in the world. The negative consequences are becoming difficult to ignore.

Since 2022, the unemployment rate has risen from 3.6 per cent to 4.9 per cent. Most of the increase occurred after 2023 when the economy was growing, albeit modestly. Unemployment is never monocausal, and there are other factors, such as the rise in the employer National Insurance rate, that likely contributed, but it coincided with the standard minimum wage rate rising from £9.50 to £12.71 per hour. The hospitality sector, and pubs in particular, often cite the minimum wage as a leading cause of business closures.

The youth unemployment statistics are even more alarming. Whatever else was going wrong with the British economy, we used to be able to console ourselves that we didn't suffer from Europe's seemingly endemic scourge of youth unemployment. That cope is no longer available to us. Youth unemployment in the UK has risen from 9.3 per cent in 2022 to 16.2 per cent today. It is predicted to rise to 17.6 per cent next year. The EU has seen no significant increase in recent years and has a youth unemployment rate of 15.1 per cent. Perhaps the difference is that the UK dropped the age threshold for the National Living Wage in 2021 (from 25 to 23) and then again in 2024 (to 21).

If the analysis of Bowles and Igwe is correct, the BBC gloated too soon. The initial warnings about the minimum wage turned out to be overblown, but only because the bite ratio was set at a reasonable level. Subsequent governments became complacent and pushed the dial too far, harming the very people the minimum wage was supposed to protect. The authors' recommendation of a five-year freeze may not be popular, but it is eminently sensible.

Christopher Snowdon
Institute of Economic Affairs

Executive summary

The cost of employing a full-time worker in Britain, as of April 2026, was £28,308.52 per annum. This number includes the full-time salary of an employee earning the National Living Wage (NLW), the new higher rate of employer National Insurance contributions, and the auto-enrolment pension contributions an employer makes to an employee's pension. **The minimum wage 'bite ratio'—that is, the ratio of the minimum wage to the median wage in a country, also called the Kaitz Index—has risen from 46 per cent in 1999 to approximately 66 per cent today.** This sits comfortably above the 60 per cent threshold which was the NLW's original target and is often treated as the suggested point where disemployment effects begin to emerge.

In Britain today, we are already seeing these effects. This has been borne out especially when looking at employment opportunities for young people. **The NLW has risen by 48 per cent since 2019 in cash terms (15.8 per cent in real terms), whilst output per hour has only risen by 2.4 per cent over the same period.** The Low Pay Commission estimates that wage spillovers from multiple increases to the minimum wage have now reached the 35th percentile of earners.

This has resulted in the slow erosion of the differential between junior and mid-level roles. As a result, **the financial incentive to seek promotion or assume more responsibility in the workplace has been weakened, with damaging effects on workplace productivity. Most unfortunate is the continuous increase in 16–24-year-olds who are not in employment, education, or training (NEETs).** The number of NEETs has increased from 715,000 in 2021 to 946,000 in 2025. This is a major cause for concern, signalling that the door to entry-level jobs has been steadily closed to young people seeking employment.

To buck this trend, this paper proposes a five-year freeze to the NLW at current rates. Assuming a nominal trend growth of 3.5 per cent in median wages, a freeze will restore the bite ratio to 56 per cent—a level at which Britain operated between 2008 and 2015. Crucially, this would not imply any cut in nominal wages as the wage floor remains at £12.71. However, it implies real terms cut in the NLW, with purchasing power eroding by 9 to 12 per cent given a projected inflation of 2 to 2.5 per cent. **This will push the relative value of the NLW to the median wage from 66 per cent to 56 per cent, due to the freeze.** We do not present these findings as costless to workers. The case to accept this proposal hinges on three factors: first, it will restore the bite ratio to a historically sustainable level; second, it would be phased in gradually; and third, the impact on low-income households will be partially cushioned by complementary reforms we recommend such as adjustments to the tax threshold, the fiscal costs of which are not estimated in this paper.

By using a two-way fixed effects panel model across the 12 ITL1 regions in Britain between 2010 and 2025, we estimate that **a one-percentage point increase in the minimum wage is associated with a 0.37 percentage point decline in the youth (16–24) employment rate.** This is conditional on a year and regional fixed effects, as well as labour market controls. Applying this central estimate to a ten-percentage point fall in bite ratio over a five-year freeze implies **an increase of approximately 270,000 young people in employment by 2031.** Due to analysis based on 12

regions, we have a wide confidence interval (approximately –58,000 to +597,000 jobs). Although this margin of error suggests that we cannot statistically rule out a net job loss, the central estimate and most of the confidence interval points towards a positive employment response.

The benefits also extend to macroeconomic effects, with a Gross Value Added (GVA) gain of £9.7bn per annum, a gross fiscal gain of £2.4bn per annum to the Exchequer and a present value human capital gain of £14.7bn by avoiding wage scarring; though these macroeconomic effects depend on the central estimate holding.

Main policy recommendations

1. **Freeze the National Living Wage at £12.71 for five years**: Any forthcoming uprated recommendations by the Low Pay Commission should be rejected. This will allow median earnings growth to restore a bite ratio of 56 per cent—the value in 2015. This would require no primary legislation to accomplish.
2. **Abolish the Low Pay Commission or recast its remit:** The setting of the minimum wage should be a decision for government. During the freeze, uprating recommendations by the Commission should be declined as a second-stage reform which will require primary legislation and the body should ultimately be abolished.
3. **Revert Employer National Insurance contribution rates to their pre-April 2025 level:** This would involve reducing the Employer NIC back to 13.8 per cent above the £9,100 secondary threshold while keeping the current Employment Allowance at £10,500 so that SMEs are not left worse off. This would reduce the cost of hiring a worker on minimum wage by £800 per annum.
4. **Reinstate the two-year qualifying period for unfair dismissal protection:** This would reduce the risk borne by firms seeking to hire new staff—especially SMEs that rely on recruiting lower-productivity workers. From January 2027, the Employment Rights Act 2025 will reduce this period to six months. To restore this would require primary legislation.

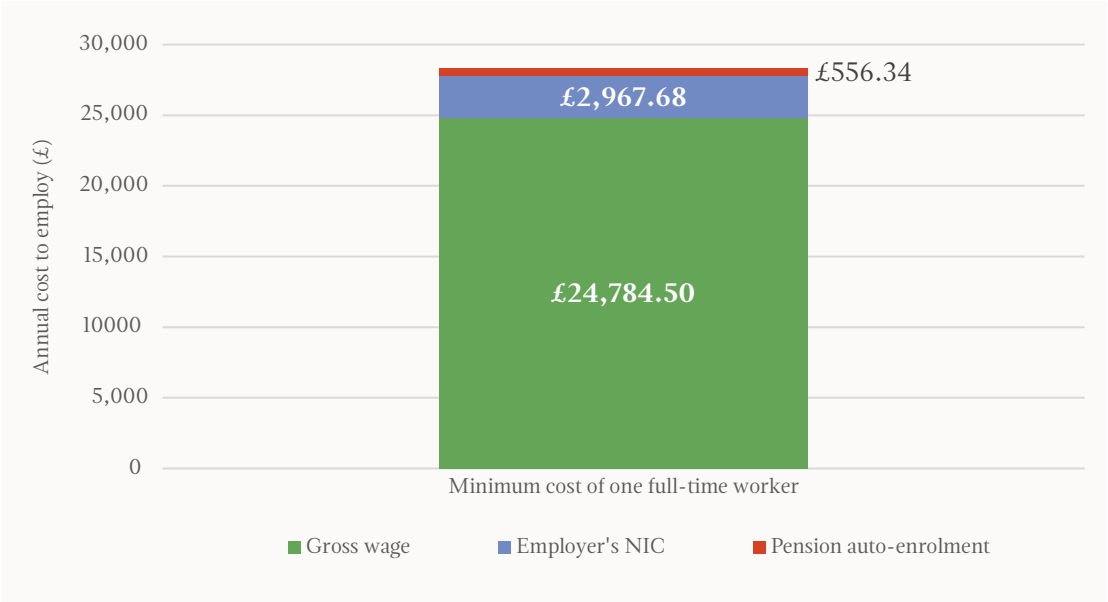
1. Introduction

Main points

- Britain's statutory wage floor makes the minimum cost of employing a full-time worker £28,308.52 a year, including employer National Insurance and pension contributions.
- The ever-rising National Living Wage has become detached from productivity, compressing wages and restricting entry-level opportunities, particularly for young people.
- Freezing the National Living Wage at £12.71 an hour for five years will likely have beneficial effects on youth employment and economic growth.

As of April 2026, the minimum cost of hiring a new full-time equivalent employee in Britain is £28,308.52 per annum. This value—not the gross salary of £24,784.50, nor the announced headline rate of £12.71 per hour—is the required amount the British Government expects an employer to pledge before a single hour of labour is performed. **This is the government-imposed floor of the labour market, which hinders businesses from employing labour that produces value beneath this state-set rate.**

Figure 1: *The minimum indivisible unit of labour, April 2026*



The total cost shown in Figure 1 includes three statutory obligations above the headline wage. There is the gross wage at the new NLW (i.e. £24,784.50 for 37.5 hours of labour). Added to this is a 15 per cent Employer National Insurance Contribution (NIC) for earnings above £5,000—adding £2,967.68. Finally, a three per cent mandatory auto-enrolment pension contribution adds £556.34 to the bill. Most critically, a sizeable proportion of the £28,308.52 is a tax wedge of employer taxes and mandatory contributions between the value received by an employee and the cost to the employer.

We argue in this working paper that there is a very strong case for major reforms to Britain's minimum wage laws. Crucially, we propose a five-year freeze to the NLW at its current (2026) rate of £12.71 per hour. This paper does not argue for an outright abolition of the minimum wage as the empirical data we have used does not permit extrapolation outside the minimum wage environment. The data that would be required to do this is not easily accessible publicly, so we are unable to determine a clear economic effect of a total abolition of the minimum wage.

We are not suggesting that low pay is desirable. Rather, we agree with a growing consensus that Britain's minimum wage laws have drifted from their economic intent over the past twenty-five years. **We see the results in compressed wage structures, suppressed employment at the margins, decoupling of pay from productivity, and most visibly by a generation of young people who are trapped by rising worklessness.**

In this paper, we set out the empirical record, the counterfactuals, and a framework to assess the effect of these reforms on youth employment and national economic growth.

2. From safety net to wage ratchet

Main points

- In 1999, New Labour's National Minimum Wage was introduced at a relatively modest 46 per cent of median hourly earnings, with the Low Pay Commission intended to guard against employment harm.
- The Conservative introduction and expansion of the National Living Wage pushed the wage floor towards, and then beyond, the original target of 60 per cent of median earnings.
- Labour's post-2024 reforms have broadened and politicised the Low Pay Commission's remit and point towards a still higher bite ratio, increasing risks to youth employment.

New Labour introduction of National Minimum Wage

Prior to April 1999, there was no statutory minimum wage on a national scale in Britain. In fact, pre-existing sectoral minimum wage rates applied mostly to low-paying industries were abolished under the Trade Union Reform and Employment Rights Act in 1993. At the time, the evidence that supported the abolition of such minimum wage rates made the case that their effects on employment were either negligible, or positive in some respect.[1] **By 1999, the New Labour Government had reversed these reforms by introducing a National Minimum Wage (NMW) of £3.60 per hour for a working adult. This value was approximately 46 per cent of median hourly earnings in cash terms and was comparable with 'modest' wage floors exemplified internationally.**

The following sixteen years saw the NMW growth rate increase somewhat faster than median earnings such that, by 2015, the bite ratio—the ratio of the minimum wage to the median wage—was approximately 56 per cent. This was above the United States and was comparable to France's bite ratio. To ensure a level of restraint was upheld on this upward momentum, the Low Pay Commission (LPC) was established in 1997 to provide recommended rates based on empirical assessment, which would not jeopardise employment.

Cameron-Osborne introduction of National Living Wage

This compact was broken in two stages. First, the Cameron Government introduced the National Living Wage (NLW) in April 2016. **The NLW was a higher statutory minimum rate that replaced the previous adult National Minimum Wage (NMW) rate and applied to workers aged 25 and over upon initial roll-out.** This was later extended to incorporate those aged 23 and over in 2021, and then those aged 21 and over in 2024. Now all workers aged 21 and over receive the higher NLW,

1 Juan Dolado, Francis Kramarz, Stephen Machin, Alan Manning, David Margolis, and Coen Teulings, "The economic impact of minimum wages in Europe", *Economic Policy* 11, no. 23 (1996); Stephen Machin and Alan Manning, "The effects of minimum wages on wage dispersion and employment: evidence from the U.K. Wages Councils", *Industrial and Labor Relations Review* 47, no.2 (1994).

whilst younger workers, apprentices and some trainees continue to be covered by separate NMW rates.

This paper will focus on the NLW rather than the youth and apprentice NMW rates, which cover a much smaller share of the workforce and serve somewhat different labour-market objectives.

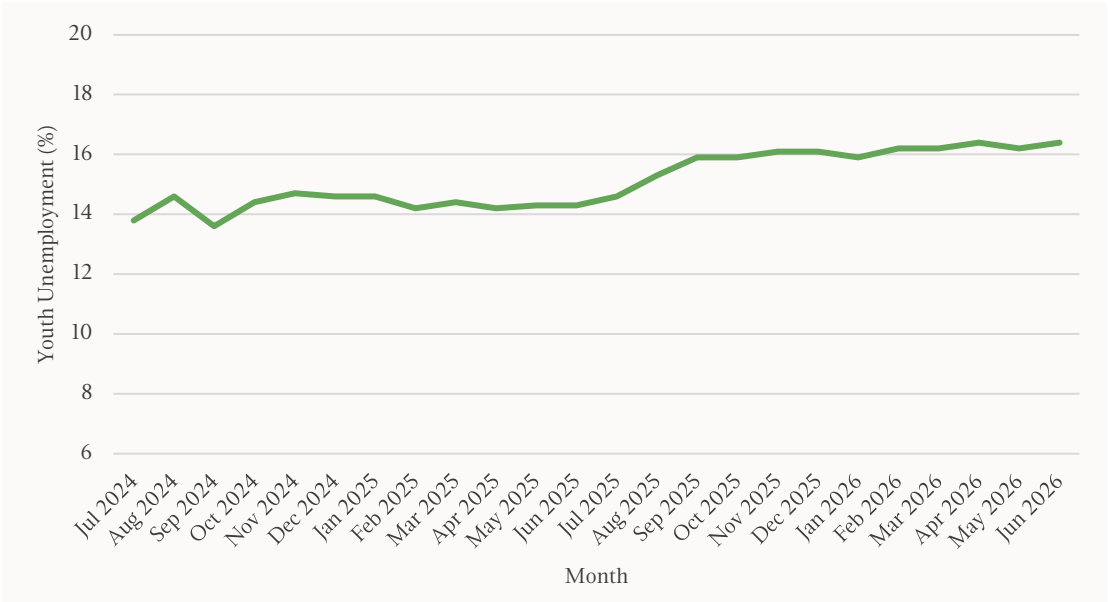
The rationale for the policy introduced by the Conservatives in the 2010s was to raise the earnings of the low-paid and attempt to transition Britain towards a high-wage economy. In the 2015 Summer Budget, then-Chancellor George Osborne announced that "Britain deserves a pay rise, and Britain is getting a pay rise".[2] He then followed by highlighting the Government's instruction to the Low Pay Commission (LPC) to target the NLW at "60 per cent of median earnings by 2020".

Post-2024 Labour reforms

Second and more recently, the Labour Government elected in 2024 has taken this further. It overhauled and expanded the remit of the LPC as a key component of their "Make Work Pay" strategy, aiming to transform the minimum wage into what they call a "genuine living wage".[3] **The LPC must now explicitly factor in the cost of living and expected inflation trends when making its recommendations, signalling higher rates.**

Further to this, a long-term ambition is for the LPC to phase out what the Government calls "discriminatory age bands", merging the separate lower rates for young adults into a single adult pay band over time.[4] There has been no specific timeline for this "narrowing [of] the gap" and the LPC has been given flexibility as to when the final alignment might take place.

Figure 2: *Youth unemployment since 2024 General Election, 16–24 (%)*



Source: ONS, Prosperity Institute analysis

2 George Osborne, "Chancellor George Osborne's Summer Budget 2015 Speech", HM Treasury, 8 July 2015. (link)

3 Labour Party, *Make Work Pay: Delivering A New Deal for Working People*, 2024, 3. (link)

4 Department for Business and Trade, "Government moves to end discriminatory age bands and unfair pay", press release, 5 August 2025. (link)

A policy paper looking at the Low Pay Commission's Remit 2025 stated:

> The government is committed to raising the living standards of working people and this is the key focus of the government's Growth Mission. That is why the government asks the LPC to ensure that the National Living Wage rate does not drop below two-thirds of UK median earnings for workers in the National Living Wage population, a recognised measure of low hourly pay.[5]

The current direction of travel shows a move towards an even higher bite ratio from its already high level. This will likely exacerbate the effects on youth unemployment that we have seen during this parliament. Figure 2 below shows the low, but gradual, increase to youth unemployment since the 2024 General Election between those aged 16 and 24.

5 Department for Business and Trade, *Low Pay Commission Remit 2025*, policy paper, 5 August 2025. (link)

3. The bite ratio

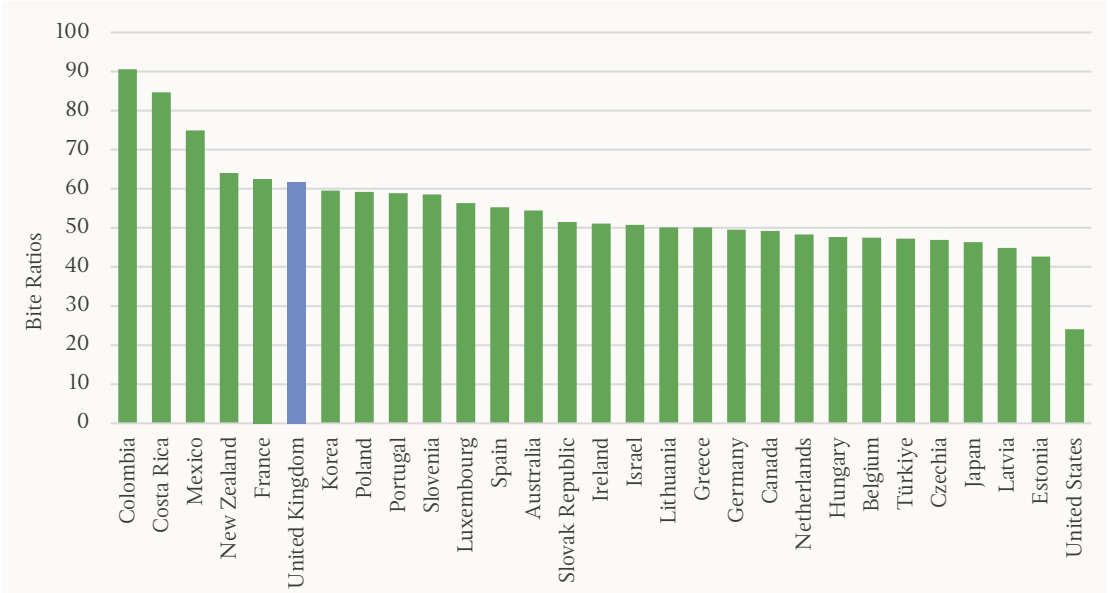
Main points

- Britain's minimum wage bite ratio has risen to approximately 66 per cent, placing it among the highest in the OECD and above the level commonly associated with employment risks.
- Minimum wage growth has substantially outpaced median wage and productivity growth, widening the gap between labour costs and workers' output.
- The resulting wage compression affects the entire bottom third of the earnings distribution, weakening incentives for promotion and increasing employers' total wage costs.

The 'bite ratio' (formally known as the 'Kaitz Index') of a minimum wage is the level of the minimum wage shown as a proportion of the median hourly wage. It compares the legal wage floor against what middle earners make in the economy.

As Figure 3 shows below, **Britain has a comparatively high minimum wage as a percentage of the median wage of full-time workers compared to OECD countries in 2025.** This is another example of how exceptionally rapid the growth of the minimum wage has been in Britain relative to typical wages.[6]

Figure 3: *Statutory minimum wage as % of medium wage (full-time workers), 2025*

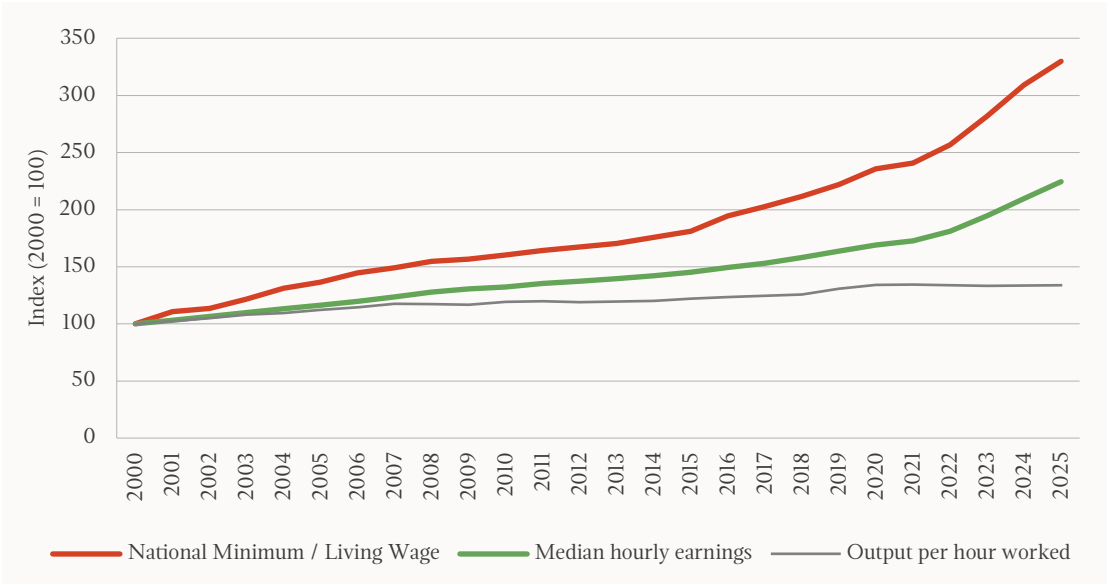


Source: OECD.

6 The OECD figures in Figure 3 differs from the domestic Kaitz measure used elsewhere as a result of the OECD calculating the minimum wage as a proportion of median hourly earnings for full-time workers only, using the average minimum-wage rate over the calendar year, whereas the domestic measure uses median hourly earnings for all workers. See OECD, "Employment protection and minimum wages", accessed 2 October 2026. (link)

In Figure 4 below, the minimum wage has more than tripled since 2000, rising by about 230 percent in cash terms by 2025. In the same period, median hourly earnings rose by approximately 125 percent. So, over the past 25 years, the minimum wage rose almost twice as fast as the typical pay in Britain. By contrast, output per hour grew by only 34 per cent and has barely grown since 2020. The gap between the minimum pay and the median pay has widened since 2021, with the minimum wage rising by more than 30 per cent in four years.

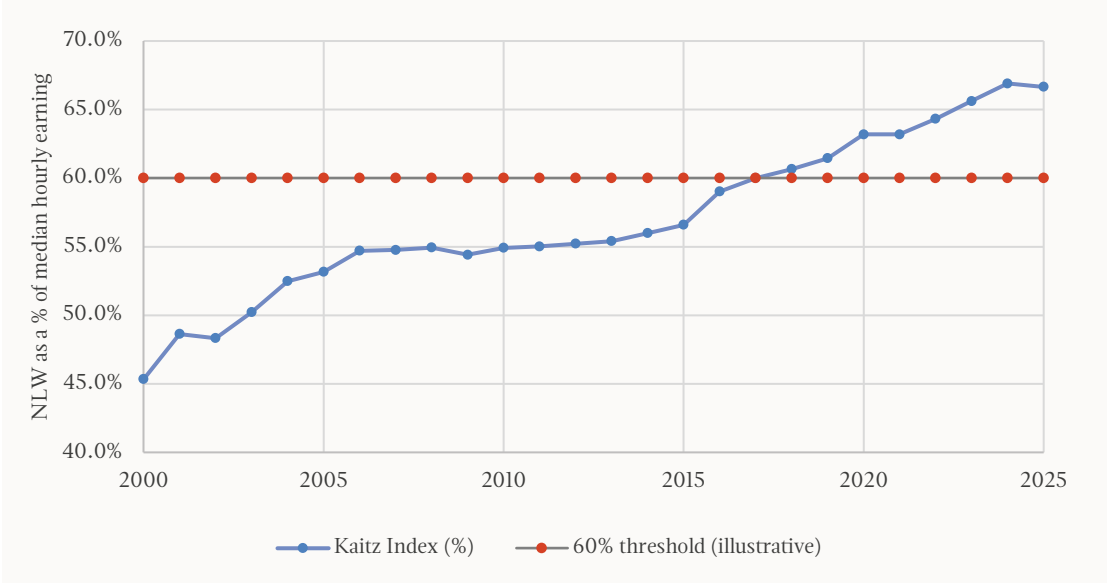
Figure 4: *Wage growth has decoupled from productivity, 2000–2025*



Source: ONS, Prosperity Institute analysis

To further illustrate this point, Figure 5 below shows the bite ratio over the full life of this policy. **Between 2000 and 2017, the ratio grew from 46 per cent to 60 per cent. By 2023, it sat at 65 per cent, and it is approximately 66 per cent today. This is concerning as 60 per cent is widely treated as a cautious upper bound, above which negative impacts on employment rises.**[7] Britain now sits comfortably above this level. If nothing is done to change the current remit of the LPC then Britain will stay within this zone indefinitely.

Figure 5: *The Kaitz Index has crossed the danger zone*



| 7 Alan Manning, "The elusive employment effect of the minimum wage", *Journal of Economic Perspectives* 35, no. 1 (2021).

Source: ONS, Prosperity Institute analysis

The productivity paradox

The central economic problem surrounding the NLW is the growing divergence of pay from the productivity of minimum wage workers. Conventional labour economic theory posits that, in equilibrium, the wage paid to a labourer tends towards the marginal revenue product of that labourer's output—that is, the additional revenue an employer gains from hiring extra staff or buying new equipment. **When the statutory wage floor exceeds the marginal product, employers can only resort to three available approaches: employ fewer staff, replace existing staff via automation or employ more productive staff based on available capital**.[8]

Britain's labour productivity has flatlined since the 2007/08 Financial Crisis. The latest ONS figures show that as of the third quarter of 2025, output per hour worked was just 2.4 per cent above its 2019 average. This amounts to a cumulative annual growth rate of less than 0.5 per cent per annum.[9] In that same period, the NLW has risen by 48 per cent in cash terms.

This has resulted in a sustained disparity between the price of labour and its productivity, leading to compressed profit margins, rising prices, or a reduction in the quantity of labour purchased (sometimes a combination of the three). In the case of a small, open economy that is exposed to international competition, the most exposed variable here is the quantity of labour purchased.

Proponents of the continued advancement of the NLW within the LPC's remit would point to Manning's concept of the "elusive employment effect" to back up their argument. Manning suggests that there were no measurable disemployment effects due to early minimum wage increases in the United States or Britain during the 1990s and early 2000s.[10] **This finding is sound but applies to a range of bite ratios that were on low to moderate levels and generally strong economic conditions at the time. The available data does not support applying this conclusion to Britain's current bite ratio.**

Similarly, other popular studies such as Cengiz et al refer only to minimum wages at 'modest' bite ratios (between 37 and 59 per cent of the median wage).[11] This tells us little about what happens when the bite ratio is above 65 per cent as is the case in Britain.

Wage compression

Wage compression occurs when pay at the lower end of the earnings distribution rises more rapidly than pay elsewhere in the distribution. When the statutory wage floor approaches an increasingly large proportion of median earnings, compression extends beyond the workers directly covered by the minimum wage. **This has detrimental effects on the labour market by disincentivising employees from seeking promotions and pay rises. This has been exacerbated by the fiscal**

8 George J. Stigler, "The economics of minimum wage legislation", American Economic Review 36, no. 3 (1946)

9 Office for National Statistics, "Productivity flash estimate and overview, UK: October to December 2025 and July to September 2025", 17 February 2026. (link)

10 Manning, "The elusive employment effect".

11 Doruk Cengiz, Arindrajit Dube, Attila Lindner, and Ben Zipperer, "The effect of minimum wages on low-wage jobs", *Quarterly Journal of Economics* 134, no. 3 (2019), 1405–54.

drag and higher marginal tax rates caused by lengthy freezes to income tax thresholds.

The LPC has acknowledged this phenomenon. In its 2025 report, the Commission noted that "relative pay differentials continued to compress" across both low-paid and non-low-paid industries. **Employers reported difficulties maintaining wage differentials between entry-level staff and other workers holding greater levels of responsibility, skill or experience.** The LPC observed that many firms believed they had little scope to compress wages further without creating workforce problems.[12]

This can create a higher true cost of any minimum wage increase, which extends beyond those workers receiving salaries at statutory floor level. Employers frequently maintain internal pay ladders that reward tenure and supervisory responsibilities, meaning that when the wage floor rises substantially, firms face increasing pressures to preserve differentials. **Consequently, wage increases cascade upwards through the earnings distribution via so-called "spillover effects", as employers are forced to raise everyone's wages to maintain differentials.**

Recent LPC analysis estimates that the effects of NLW uprating extend far beyond those formally covered by the legislation. **Whilst about six per cent of jobs pay the NLW, the Commission estimates that wage spillovers can extend as high as the 35th percentile of the hourly earnings distribution. This encompasses workers earning all the way up to £15.17 based on April 2025 earnings.**[13] This suggests that any change to the wage floor can have effects extending across the bottom third of earnings distribution, going much further than those directly subjected to the statutory minimum.

Compressed pay structures ultimately reduce the traditional incentives for workers to seek promotion or take on additional responsibilities. Businesses have reported recruitment difficulties for supervisory positions and increasing dissatisfaction among experienced staff whose earnings have risen little relative to new hires entering employment. Such compression to pay disproportionately benefits new entrants over experienced low-skilled workers. This is why a "high-wage economy" cannot be mandated from above by government policy and statutory wage floors. It must emerge through proper incentives in a functioning market.

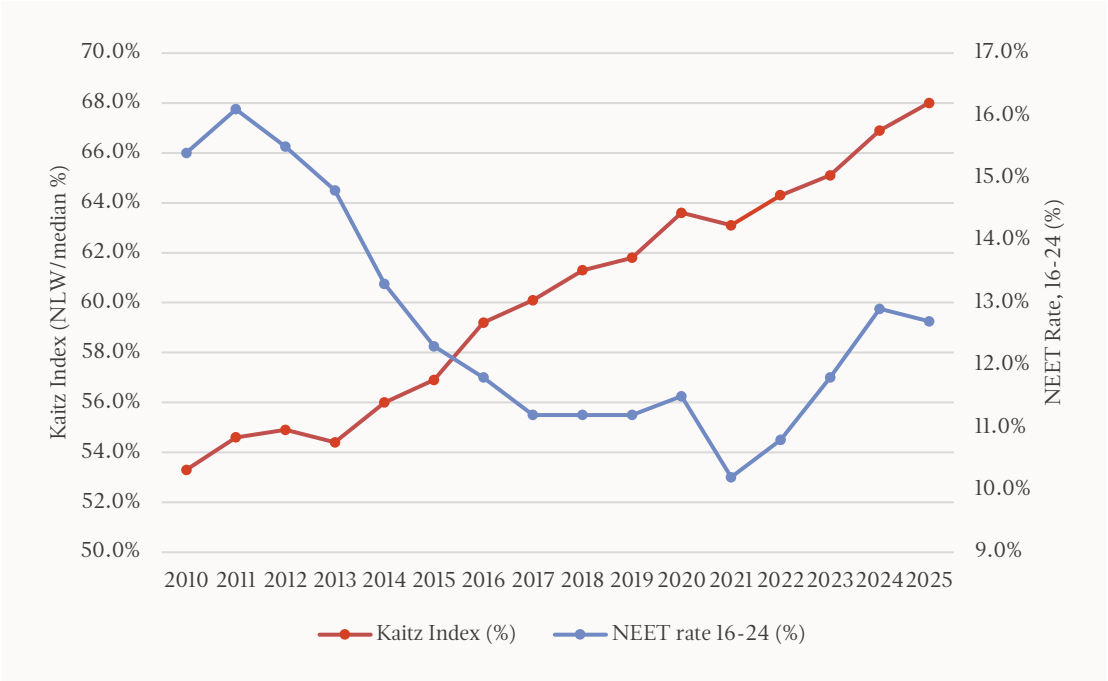
The bite ratio and youth worklessness

Figure 6 below observes the changes in the Kaitz Index as compared to changes in NEET rates among 16–24-year-olds between 2010 and 2025. For much of the 2010s, there was a divergence between the NEET rate and Kaitz Index due to the sustained post-2013 recovery from the financial crisis and rising post-16s participation in the labour market and the lower minimum wages for young people kept unemployment down while standard minimum wages increased.

12 Low Pay Commission, *National Minimum Wage: Low Pay Commission Report* 2025 (London: HM Government, 2025). (link).

13 Low Pay Commission, "Low Pay Commission Explainer: The Minimum Wage and Inflation", Low Pay Commission blog, 1 April 2026. (link)

Figure 6: *After divergence for a decade, the bite and NEET rates rose together from 2022*



Source: ONS, Prosperity Institute analysis

This trend changes from 2021 onwards after the implementation of two policies. First, the age threshold for the NLW was reduced to 23 in April 2021, and further down to 21 in 2024. Second, NLW uprating was the largest in history in 2023 and 2024, at 9.7 and 9.8 per cent respectively. **The effects of these two policies contributed to a bite ratio of 66 per cent and extended the NLW for more young workers. Even as the bite rate passed 60 in 2017, we still see NEETs falling until 2021, which suggests that the lower youth rates in place at the time shielded under 25s.** These protections have mostly been removed. While a rising bite ratio influences employment, in this period, post-pandemic scarring and a welfare regime that increasingly disincentivises people from work are also contributors to rising unemployment among the young.

4. The labour market argument for freezing the National Living Wage

Main points

- Had Britain never introduced a statutory minimum wage it could simply have functioned like countries such as Switzerland, relying on less centralised mechanisms to perform the same function.
- A temporary five-year freeze of the National Living Wage at £12.71 would reduce the bite ratio from approximately 66 to 56 per cent, restoring a healthy relationship between low and median earnings.
- Our regional panel model estimates that reducing the bite ratio from 66 to 56 per cent through a five-year freeze could increase youth employment by around 270,000.

Counterfactual: what if Britain had never introduced a National Minimum Wage?

A useful starting point in assessing the effects of the National Minimum Wage is to distinguish between the existence of statutory wage floors and the broader institutional architecture through which wages are determined.

The introduction of the National Minimum Wage Act 1998 marked a decisive shift away from the fragmented system of wage councils (independent bodies set up by law to set minimum pay and working conditions in low-pay industries). These councils were abolished in 1993 through the Trade Union Reform and Employment Rights Act 1993, having had most of their authority weakened. This allowed a period of partial deregulation prior to the introduction of a national floor.

Empirical work on this transition, particularly studies of the post-abolition experience of wage councils, is often used to explore what a "no minimum wage" equilibrium might look like in Britain. Dolado et al find little consistent evidence of large-scale disemployment effects following the removal of sectoral wage floors.[14] Whilst the institutional context is not identical to today's economy, the findings are frequently interpreted as suggesting that in relatively flexible labour markets, wage floors are not always binding constraints on employment.

International experience suggests that the absence of a statutory minimum wage is neither synonymous with labour market deregulation, nor indicative of uniformly weak wage protection. **Countries without formal wage floors typically rely on alternative wage-setting institutions that perform a similar function via different mechanisms.**

14 Dolado et al., "The economic impacts of minimum wages".

Switzerland is frequently cited as one of the clearest advanced-economy examples which demonstrates that a statutory minimum wage is not a prerequisite for maintaining relatively high-wage labour markets. At the central government level, there is no single nationwide minimum wage. **Instead, wage determination is decentralised across a combination of sectoral collective labour agreements (*Gesamtarbeitsverträge*), cantonal regulation, and other more standard employment contracts that are issued where necessary to prevent any undercutting.**

A substantial portion of Swiss workers are covered by agreements that set binding minimum wages and employment conditions across entire sectors, which are often extended to all firms operating within those industries. Where collective bargaining does not apply, cantonal governments have in several cases introduced minimum wages at the regional level, in areas such as Zurich, Jura, and Basel-Stadt. Typically, the minimum level ranges in the low-to-mid CHF 20s per hour depending on the canton.

The argument for freezing the NLW

Of course, Britain did introduce a minimum wage and we are now dealing with its legacy.

Having considered the counterfactual of no minimum wage in the first place, we now consider a workable alternative in an environment in which a statutory wage floor has become established: what if the NLW were frozen for five years?

Modelling the freeze counterfactual

A panel two-way fixed effects model has been developed to assess the relationship between youth employment and the Kaitz index (bite ratio).[15] This model controls for time effects and aggregate labour market conditions.

Although the central estimate points to disemployment effects, we cannot rule out the possibility that there could be a zero-effect at the level of precision achieved. This is because we do not achieve five per cent statistical significance given 12 clusters and a 95 per cent confidence interval for $\hat{\beta}$ that falls between -0.88 and +0.13. This is a commonly understood problem with panel studies with only one wage floor (i.e. NLW in this case) in a within-country panel where there is no opportunity for a pre- and post-natural experiment design structure as would be the case in a cross-country analysis.

Considering the policy counterfactual, the five-year freeze in the National Living Wage would see the bite ratio reduced from 66 per cent to its pre-2016 bite ratio of 56 per cent as median wages rise. The result of this will be a central estimate increase in youth employment by about 3.7 per cent (approximately 270,000 additional 16–24-year-olds will be employed). For this counterfactual, the 95 per cent confidence interval ranges from a minor net employment loss of -58,000 to a huge expansion in youth jobs by +597,000 jobs nationwide.

Labour market efficiency

A temporary freeze of the National Living Wage at its current rate of £12.71 for a period of five years would improve labour market efficiency. The objective of this policy would be to restore a healthier relationship between minimum wages and median earnings, while leaving the

15 The full specification is set out in the Appendix.

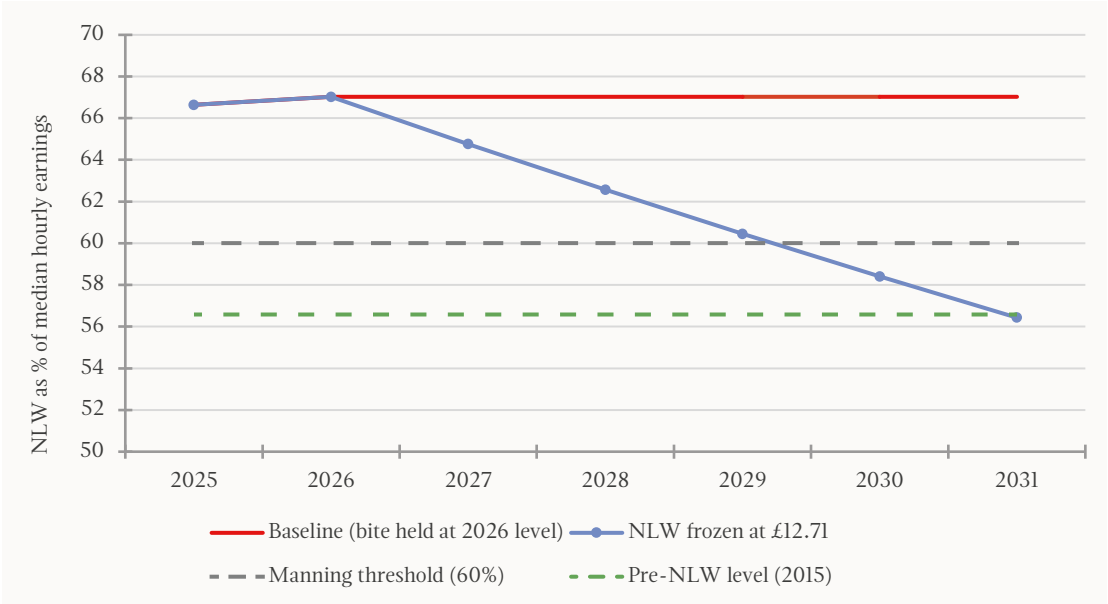
statutory wage floor in place.

Restored relationship between minimum wage and median earnings

The primary purpose would be to re-establish a degree of separation between median wages and the minimum wage. Over the past decade, successive governments have consciously pursued a policy of increasing the NLW faster than average earnings, resulting in one of the highest minimum wage bite ratios in the developed world.

The ONS estimates that median weekly wages for full-time employees have grown by about 3 per cent per annum in nominal terms over the past fifteen years.[16] Assuming nominal median growth of 3.5 per cent, holding the NLW constant between 2026 and 2031 whilst median wages rise would gradually reduce the Kaitz bite ratio from approximately 66 per cent to 56 per cent, returning Britain to the wage-floor bite it had in 2015, before the NLW was introduced. This would also be the same level that Britain operated between 2008 and 2015 without producing the dysfunction we see in Britain's labour market today. The projected path of the bite ratio under a five-year freeze is depicted in Figure 7 below.

Figure 7: *Projected national Kaitz bite under a five-year NLW freeze*



Source: Prosperity Institute analysis

Importantly, this adjustment would occur without requiring any reduction in existing pay rates. The wage floor would become less binding over time as earnings elsewhere in the labour market rise. Market wages would gradually catch up with the statutory floor rather than the statutory floor continuously being pushed upwards towards median earnings.

Increased employment

The employment implications could be substantial**. A reduction of ten percentage points in the minimum wage bite ratio is estimated to generate a 3.7 percentage point increase in youth**

16 Office for National Statistics, "Employee earnings in the UK: 2025", statistical bulletin, 23 October 2025. (link)

employment by 2031. This translates to approximately 270,000 additional new jobs to the labour force by the end of the freeze based on the central estimate, with gains concentrated amongst younger and lower-skilled workers who are most sensitive to changes to labour costs[17].

This counterfactual is based on three conditions.

Condition 1: Discount and abolish the LPC

First, it would require an amendment to the current LPC remit and a refusal to implement its latest recommendation on uprating pay, and any further future recommendations for annual uprating. The institutional machinery would remain intact, but its objective would shift from increasing the wage floor to maintaining it. Our recommendation to abolish the LPC is a second-stage recommendation (see Implementation).

Condition 2: Make the freeze temporary

Second, the policy would be explicitly temporary. At the conclusion of the five-year freeze period, a future government could choose to resume uprating, maintain the freeze further or pursue more fundamental reform. The proposal would therefore avoid permanently binding future policymakers to any course of action.

Condition 3: Allow market-clearing wages to emerge

Third, the resulting effect of this policy is that the price of labour is transferred to a wage discovery (market clearing option) from the current position which is based on a price-setting option. Freezing the NLW allows market-clearing wages to re-appear above the floor across regions and sectors.

Therefore, the freeze is politically tractable, leaving the policy structure intact while gradually reducing the bite ratio. Given that the analysis here is based on a reduction in bite ratio not an abolition of the NLW, **freezing the NLW is best assessed on its own terms: as a useful, controlled experiment that assuages the fears proponents of advancing wage floors may have.**

17 The addition of approximately 270,000 jobs reflects a reduction in the bite ratio by 10.4 percentage points over five years and a median wage growth of 3.5 per cent per year.

5. Productivity and economic output benefits

Main points

- By adding an estimated 270,000 workers to the workforce, a five-year NLW freeze would increase annual Gross Value Added by £9.7bn, despite a small decline in average output per worker.
- Bringing young people into employment would reduce long-term wage scarring, generating an estimated £14.7bn in present-value lifetime earnings.
- Higher employment could produce a gross fiscal gain of about £2.4bn a year to the Treasury through additional tax receipts and lower welfare spending.

Having considered the employment gains aforementioned, how would a freeze to the NLW affect economic growth and productivity? This section provides analysis on productivity effects and economic growth effects. The full methodology is presented in the Appendix.

The productivity puzzle

A major argument against advocating for a fall in the bite ratio as evidenced above is that labour market productivity may decline.

The rebuttal here comes from the 'marginal productivity theory of wages'—the theory that by freezing the minimum wage over time, firms can afford to hire workers that would otherwise have been priced out of employment opportunities due to a higher effective wage floor. **As a result, the average Gross Value Added (GVA) increases because there are more workers, though it may be expected that the average GVA per worker would lead to a slight decrease due to the diminishing marginal returns caused by new entrants entering the workforce beyond necessary productive capacity.**

We can provide a summary of the static effects on productivity using our central estimate of approximately 270,000 extra workers, assuming marginal entrants produce approximately 45 per cent of the British average GVA per worker as per ONS estimation (i.e. 45 per cent of £80,500 = £36,025—approximately £36,000). **Although the annual GVA increases by £9.7bn[18], the average GVA per worker would decline slightly by 0.44 per cent.**

The fall in average GVA per worker is not reflective of a welfare loss. A society does not simply become more economically productive by excluding its least productive members from contributory economic activity. **The crucial aspect of this finding is that total output increases,**

18 The 95 per cent confidence interval reveals a range from -£3.5bn to +£22.9bn.

even if average output reduces. In the current context of rising unemployment and economic inactivity, especially among the young, labour market reform should prioritise increasing economic participation by lowering the cost of hiring.

Long-run wage-scarring effect

The static measure of productivity misses out on long-run effects. At one end, a young person unemployed for more than six months is more likely to experience prolonged benefit dependency.[19] This scarring effect extends to a wage penalty of approximately 13–21 per cent two decades later.[20] We follow Bell and Blanchflower's seminal paper, which estimates scarring effects across European countries with similar findings to those of Gregg and Tominey.[21] Using a conservative scarring effect of 8 per cent over a 40-year career, the HM Treasury Green Book discount rate of 3.5 per cent[22], **we find that the present value of avoided wage scarring for each young person that enters the labour market—rather than lingering as a NEET—following the freeze to the NLW is approximately £54,700. When aggregated central estimates apply, the present value lifetime earnings for all approximately 270,000 young people added to the labour market is £14.7bn. Using the higher scarring effect of 15 per cent within Gregg and Tominey's range, yields a lifetime present value earning of £28bn**. This reflects career progression, skills acquisition over time, and the broad and consistent attachment to the labour market over one's working life.

Summary

The static measurement shows a short-run increase in total output by £9.7bn despite a modest decline in average GVA per worker. The human capital accumulation by avoided scarring generates present value lifetime earnings of £14.7bn over the long run.

These findings are complementary. The first derives the immediate output gain because of freezing the NLW. The second derives the long-run productivity dividend that is a result of avoiding the scarring effect that builds up as more young people are left outside of the labour market. **On our central estimate, by freezing the NLW, current output would be increased, the lifetime earnings of young people would be increased as wage scarring is reduced, and the trajectory of Britain's productivity in the long run would be positive.**

Fiscal implications

Thus far, we have considered the benefits freezing the NLW would have on employment, productivity, and economic output. The benefits would also extend to public finances.

Essentially, every additional worker reduces welfare spending for the Exchequer while generating tax revenue as an employed taxpayer. The fiscal gain from additional employment can be derived from first principles using DWP and HMRC rates.

19 Young Futures Foundation, *Youth Employment: 2025 Outlook* (Youth Futures Foundation, 2025). (link)

20 Paul Gregg and Emma Tominey, "The wage scar from male youth unemployment", *Labour Economics* 12, no.4 (2005).

21 David N.F. Bell and David G. Blanchflower, "Young people and the Great Recession", *Oxford Review of Economic Policy* 27, no.2 (2011). See also Gregg and Tominey, "The wage scar".

22 HM Treasury, *The Green Book: Central Government Guidance on Appraisal and Evaluation* (London: HM Treasury, 2026).

Estimations

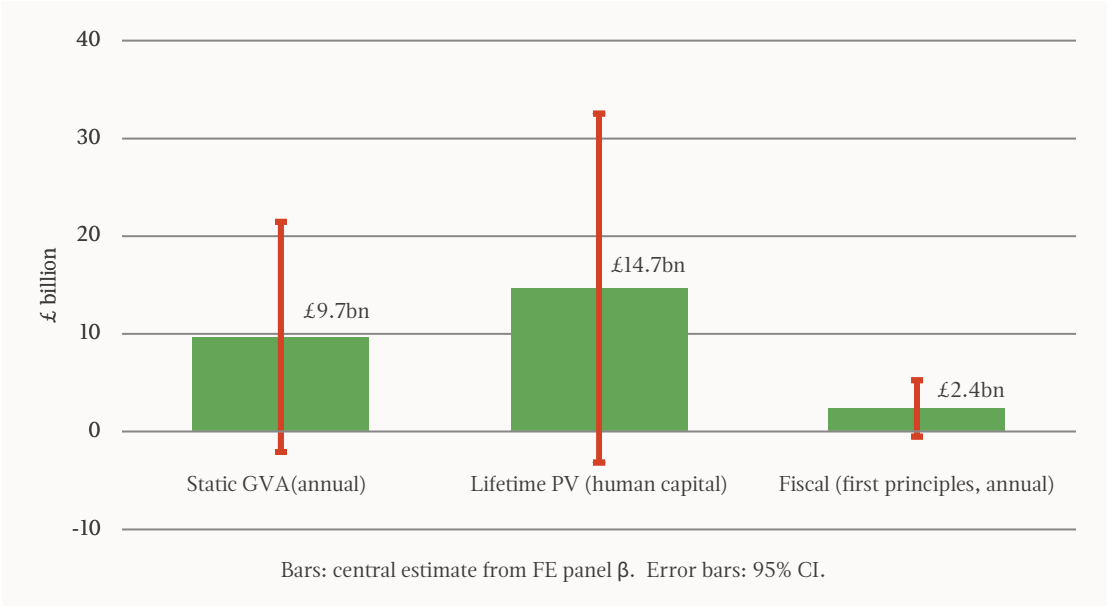
If we assume the Annual Survey of Hours and Earnings (ASHE) estimate for median earnings among 18–24-year-olds as approximately £20,000, Table 1 sets out the per-worker fiscal impacts:[23]

Table 1: *Estimated per-worker fiscal gain from an additional young worker in employment.*

Component	Per-worker (p.a.)
Income tax	£1,486
Employee NI	£594
Employer NI	£2,250
Savings on UC + Housing element (DWP average)	£4,500
Total (gross) fiscal gain	**£8,830**

The annual aggregate gross fiscal gain from all approximately 270,000 young people added to the labour market is approximately £2.4bn. The macroeconomic effects of the freeze are summarised in Figure 8 below

Figure 8: *Macroeconomic effects of a five-year NLW freeze.*



Source: Prosperity Institute analysis

Using the OBR 2024 "ready reckoner" to derive its OBR estimates for changes to employment levels to yield a fiscal gain of £7,500 for every new worker added to the labour market.[24] This is less than our estimated value of £8,830. Thus, the OBR-style estimate derives an aggregate fiscal gain of £2bn for all approximately 270,000 additional young people to Britain's workforce. The difference between our estimate and the OBR-style is 15 per cent—within the acceptable

23 The ASHE age cohorts run from 18–21 and 22–29. Therefore, to get a close approximation of earnings within the 18–24-year-old group, we use the average for 18–21-year-olds (£17,284) and 22-29-year-olds (£24,600). Source: Office for National Statistics, "Earnings and hours worked, age group. ASHE Table 6", dataset, 2025. (link)

24 Benke and Sousa, "The OBR ready reckoner".

tolerance for a robustness check.

By freezing the NLW, the Exchequer bears no direct cost from the policy. Firms, benefitting from foregone NLW uprating can either increase staff wages, employ new staff, or do both.

The figures above are gross values which capture the extra tax paid and benefits saved due to young people entering work based on our employment estimate and published tax and benefits rates. They do not account for the effect of slower pay growth for workers close to—or on—the NLW, which may reduce individual earnings and reduce income tax and NI contributions while raising Universal Credit entitlements for some households. To model this would require micro-level household microsimulations consisting of hours, pay spillovers, and benefit receipts which falls outside the scope of this analysis. From the business standpoint, a smaller wage bill redistributes capital back to the wider economy through corporate taxes and profits. Thus, the net fiscal effect of a wage freeze remains uncertain. The case for freezing NLW rests on its employment effects, rather than revenue impacts to the Exchequer.

6. Objections

Main points

- Evidence that modest minimum wage increases have limited employment effects does not apply to Britain's unusually high bite ratio.
- The NLW is not meant to be an anti-poverty tool and should be accompanied by reforms to Universal Credit and tax thresholds.
- Countries without a statutory wage floor, such as Switzerland, do not see firms racing to the bottom to underpay workers.
- Concerns about cheap migrant labour undercutting British workers point to the need for complementary labour-supply reforms.

There are four major objections to our position which are worth discussing.

Do minimum wage increases really impact employment?

First, the premise from the seminal work by Card and Krueger in 1994, which was further tested by Cengiz et al., suggests that modest increases in the minimum wage do not lead to noticeable job losses.[25]

This objection is correct, but it does not apply to Britain where the bite ratio is higher than the ratio recommended in empirical literature. In other words, Britain's minimum wage growth has been snowballing to a point where the adverse effects on youth employment are evident.

Will it worsen in-work poverty?

Another objection worth considering is that in-work poverty would worsen because the real value of the wage floor would fall due to the freeze. **This assumes that the minimum wage is designed to be an anti-poverty tool, when poverty is driven largely by household circumstances, not individual hourly pay rates.** [26]

Although the real effects of freezing the NLW could shift some financial support to the welfare system, these effects are offset by the broad positive effect of bringing more young people into employment.

It should be noted that we do not recommend a freeze in NLW in isolation, but **it should also be accompanied by reforming Universal Credit tapers to boost incentives to work and**

25 David Card and Alan B. Krueger, "Minimum wages and employment: a case study of the fast-food industry in New Jersey and Pennsylvania", *American Economic Review* 84 no.4 (1994); Cengiz et al., "The effect of minimum wages".

26 Giulia Giupponi, Robert Joyce, Attila Lindner, Tom Waters, Thomas Wernham, and Xiaowei Xu, "The employment and distributional impacts of national minimum wage changes", *Journal of Labor Economics* 42 no. S1 (2024).

adjustments to the tax-thresholds to increase broad take-home pay.

Will there not be a race to the bottom?

The most familiar objection is the notion that a weaker wage floor will lead to an infinite regression downwards of pay as firms will compete to pay as little as possible. Freezing the NLW does not remove the wage floor: NLW remains at £12.71 per hour throughout the period. **As stated earlier in this paper, places such as Switzerland, who do not have nationally set minimum wages do not have such behaviour from firms.**

Does a minimum wage not protect British workers from being undercut by cheap foreign labour?

A secondary function of the NLW is an insulation for British workers from wage undercutting by migrant labour. This recognises that the reservation wages of migrants who are supported by home-country alternatives, are considerably below those of young British workers. **Without considering labour supply effects, freezing the wage floor could encourage employers to substitute labour from resident workers towards migrant workers.**

On this view, some of the gains this paper projects would fail to materialise. **While there is merit to this objection, the argument placed here emphasises the need for a coherent sequencing as well as policy complementarity that goes beyond the primary focus of this report.** A wage floor as a blunt tool for migration control prices out young Brits without addressing the low-wage labour supply in Britain today. Its high elasticity exists because there is an ever-increasing pool of labour that already exists. Continued minimum wage increases would not change this elasticity, but it would continue to disincentivise companies from hiring young, inexperienced Brits. Therefore, the correct policy sequencing should align reforms to the wage floor with reduction in migrant labour supply. This is not treated in this paper but can be addressed in future research.

7. Why has reform to the NLW been unthinkable?

Main points

- Reform has been constrained by a cross-party political consensus that presents continued National Living Wage increases as support for working people while obscuring costs to businesses and young jobseekers.
- The Low Pay Commission has shifted from an evidence-led, depoliticised body to an instrument for pursuing government wage-floor targets, strengthening the case for its abolition.
- Although the minimum wage remains popular, reform can be framed as a youth-employment policy: a freeze would retain the existing nominal wage floor while restoring entry-level opportunities.

The findings shared thus far are among many in recent years that call for significant reform to the NLW and NMW more broadly. This raises the question of why no political party has the appetite for reform in this area.

We would argue that the constraint to reform is broadly political, rather than economic. This section lays out the main political constraints to reform and describes the necessary reforms that could make a freeze to the NLW politically sustainable.

The political consensus behind the National Living Wage

When George Osborne announced the NLW in 2015, it was a bold attempt to dominate an area in political discourse largely populated by the Labour Party. This rebrand of the NMW as a "Living Wage" that was targeted to be 60 per cent of median wages accomplished three objectives for the Cameron Government. First, it broadened the appeal of the Conservative party beyond being "the party of business" to also being the party of working people. Second, it co-opted a major strand of the Labour Party's redistributive arguments, neutralising its effect in the process. Third, it did not impose any fiscal cost to the Exchequer as the redistributive effects via wage regulations do not impact taxpayers but are absorbed between employers and employees.

While this was a major political win for the Conservative Party at the time, it was not apparent then what the mechanisms would be to reverse or halt the NLW rises once a 60 per cent bite ratio was achieved. Any attempt to halt the NLW would be perceived as a reversal to a stereotype of not being considerate towards the average worker.[27] Amassing many Red Wall seats in the 2019 General Election further impressed on the Conservative Party to signal consistent NLW uprating

27 We do not insinuate whether this stereotype is true or false.

as a marker of its alliance with the newly acquired and growing working class base.[28] By 2024, the party manifestoes of both the Conservatives, and the Labour Party were advocating for various forms of increase to the NLW. The Conservatives promised to maintain NLW at 66 per cent of median earnings while the Labour Party promised to broaden the remit of the LPC so that the NLW reflected the "actual cost of living"'.[29]

This broad consensus in British politics today has come at a significant cost to businesses in low-margin service sectors (e.g. retail and hospitality) and under-25s who continue to struggle to get hired. This cost remains invisible to the political process as they are either too dispersed to become a collective headache to political parties (as with many small businesses affected by rising NLW) or do not vote in concentrated geographies (as in the case of under-25s).

The Low Pay Commission

In its original design in 1997, the Low Pay Commission (LPC) was composed of academics, businesses, and trade unions. With a remit to its decision-making, successive political parties were able to offload the sensitivity involved in setting wage floors to a non-political body that consisted of experts. Therefore, to reject the LPC recommendation would require an exuberant government willing to bear the cost of such decision.

Over the years, the LPC has become a political tool to manage the tensions between workers' interests, employers' interests, and economic feasibility. It has further acted as a constraint on political tendencies to use wage floors as a tool for political point-scoring (e.g. spontaneous increases in minimum wage). Similarly, government could deflect any criticism of growing cost of living to LPC consensus. Depoliticising wage floor decision-making showed that the LPC worked as it was intended to when originally established.

This changed when the Cameron Government instructed the LPC to commit to an NLW target of 60 per cent of median wages by 2020. This introduced a political motive to a body designed to be apolitical, thus interfering with its evidence-led methodology by introducing a bias to estimations.

The current Labour Government has expanded the LPC's remit as it promised to in its manifesto to consider "the cost of living including inflation trends".[30] **As a result, the LPC can no longer be considered an apolitical body as its recommendations are not solely in consideration of labour market effects but also considers Government-expected targets.**

To implement a freeze to the NLW would require either the reinstatement of the LPC's depoliticised function or an abolition of the LPC. **Making the LPC apolitical is no longer feasible as it can no longer provide the political cover it once did due to being compromised by varying political interests. Therefore, a proposal to freeze the NLW would require that the Government own this decision and defend it on its merits. We therefore propose the abolition of the LPC as a second-stage reform requiring primary legislation, as it is no longer fit for its original purpose.** Governments have turned it into a political tool of their own, and it would be clearer and more honest for the public to know that these decisions are political ones, rather than allegedly

28 Conservative Party, *Get Brexit Done: Unleash Britain's Potential. The Conservative and Unionist Party Manifesto 2019*, 2019. (Link).

29 Conservative Party, *Clear Plan, Bold Action. Secure Future. The Conservative and Unionist Party Manifesto 2024*, 2024 (link); Labour Party, *Change: The Labour Party Manifesto*, 2024 (link).

30 Department for Business and Trade, *Low Pay Commission Remit 2024*, 2024. (link)

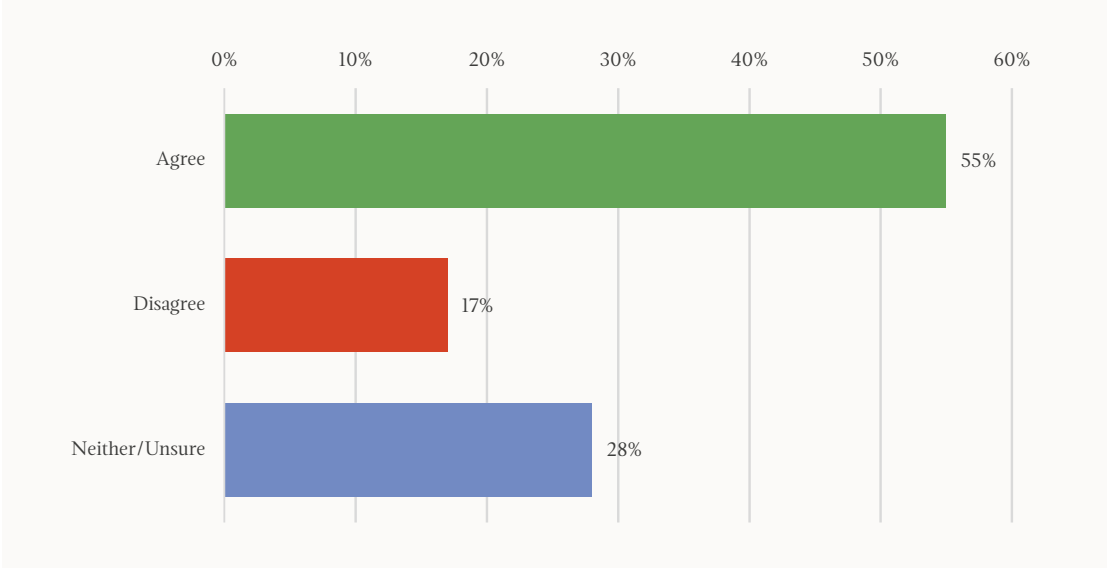
evidence-based and apolitical.

Public opinion

The NLW enjoys support from the British public. A YouGov poll in 2021 found that 89 per cent of the British public support the existence of a minimum wage, with only 5 per cent opposing it.[31] In April 2026, a poll of 40,000 voters conducted by the Trades Union Congress (TUC) found that 86 per cent of the voting public would support making the minimum wage the real living wage.[32] **It is little surprise that such a policy enjoys mass appeal. Policies that can be spun that money is being taken away from individuals is incredibly difficult to advertise and sell to the British public. Any reform to the NLW must consider this constraint and engage with it seriously.**

However, the public are aware of the downsides of significant increases. **Most recently, polling conducted by City AM/Freshwater Strategy found that 55 per cent of people surveyed agreed that increasing the minimum wage to above-inflation levels is not affordable.** This is important as recent increases have been above inflationary levels. We see the results in Figure 9 below.

Figure 9: *A majority of British voters believe that above-inflation increases to the minimum wage are not affordable currently*



Source: Freshwater Strategy.

To engage public support would involve explaining the mechanics of a freeze to the NLW: namely that freezing the NLW is not a nominal wage cut for existing workers. It leaves the current wage floor in place, but this would not increase in the future—at least, in the next five years.

Another point that should be made regards the fact that **the types of jobs most eroded by rising NLW are those entry-level jobs whose absence is disproportionately felt by young people caught up in the current unemployment crisis.** This reform should be considered as a youth employment policy, rather than a wage efficiency policy. As the findings show, freezing NLW would help avert the growing number of young people falling into the NEET cohort in the labour market.

31 YouGov, "The minimum wage: minority oppose the banding of wage by age", 29 July 2021. (link)

32 Trades Union Congress (TUC), "TUC: Public overwhelmingly support higher minimum wage – as rate rises today", 1 April 2026. (link)

8. Implementation

Main points

- A five-year freeze at £12.71 could be implemented without primary legislation by declining further uprating and amending the National Minimum Wage Regulations.
- Abolishing the Low Pay Commission would be a second-stage reform requiring primary legislation.
- Complementary reductions in employer National Insurance and restoration of the two-year qualifying period for unfair dismissal protection would further reduce hiring costs and risks.

A freeze of the National Living Wage would require little institutional or legislative change. It would necessitate the pause of any further uprating for a defined period to allow median earnings to continue growing.

The proposal outlined in this paper consists of a five-year freeze to the NLW at its current rate of £12.71. During this period the existing wage floor would remain legally binding. Employers would remain subject to all the same legal obligations that exist today. The sole change is that the statutory rate would no longer increase annually.

Freezing the NLW

The National Minimum Wage Act 1998 provides the legal basis for minimum wage rates, whilst any annual uprating is implemented via secondary legislation following recommendations from the Low Pay Commission. **A freeze, therefore, would not require primary legislation and a government could simply decline to increase the NLW and maintain the prevailing rate for the duration of the freeze period.**

As a second-stage reform, this paper recommends abolishing the Low Pay Commission through primary legislation as the Commission has a statutory basis.

For a freeze to be implemented, **a government would need to pass a Statutory Instrument (SI) amending the National Minimum Wage Regulations 2015.** The Secretary of State would lay an amending SI that either leaves the hourly rate unchanged or simply omits any scheduled uplift (if one was already in place).

Any such amending regulations would be subject to the affirmative resolution procedure, meaning that they would have to be explicitly debated and approved by both the House of Commons and the House of Lords before they can become law.

Abolition of LPC

As a second-stage reform, this paper recommends abolishing the Low Pay Commission through

primary legislation as the Commission has a statutory basis.

Accompanying reforms

Even if a freeze to the NLW may be achieved in isolation, its benefit would be most effective if it is part of a broader package of reforms to welfare incentives and the structure of labour costs. There are two complementary reforms that could convert this freeze to NLW into a broader labour market reform agenda.

Revert National Insurance Contributions to pre-2025 levels

First would be reverting employer National Insurance contributions (NICs) to its pre-April 2025 level. By reverting employer NIC back to its previous level of 13.8 per cent above the higher threshold of £9,100, the cost of hiring a new employee on the minimum wage scale would be reduced by approximately £800.[33] The current Employment Allowance of £10,500 would be retained for SMEs, so that they are not worse off.

Reverse day-one employment rights

Second, we recommend the reversal of the recently expanded day-one employment rights as stipulated in the Employment Rights Act 2025. This action would restore the two-year qualifying period for unfair dismissal protection, reverting the cut to six months in 2027. Granting parental leave entitlements, protection against unfair dismissal and eligibility for Statutory Sick Pay (SSP) from the first day of employment, severely increases the risks an employer faces when hiring new staff. This risk is acutely felt by smaller businesses hiring lower-productivity workers such as young people getting their first jobs in industries like hospitality or retail. **By reinstating the qualifying period to two years for these protections—which can only be changed by primary legislation—employers may be better at ease to hire new staff.**

The overall advantage of the above approach is that it preserves maximum flexibility. It does not commit to either permanent abolition or permanent expansion of the NLW. Instead, the temporary pause allows the government to observe the effects of a lower Kaitz bite ratio before deciding upon the next stage of reform.

33 Alongside an increase in Employer NIC to 15 per cent, the threshold for contributions was lowered to £5,000.

9. Conclusion

Main points

By arguing for freezing the National Living Wage, this paper is not making a case for cheap labour. In fact, **we are arguing for a more dynamic overall labour market which allows people to be paid more accurately for the work they do and the output they create; for an entry-level labour market that absorbs more young people than which it excludes; and a wage structure that rewards progression accurately.**

In the many years since it was established in law, the wage floor has become a barrier to entry rather than a protection for vulnerable employees against exploitation. As productivity continues to flatline and one in eight 16–24-year-olds are classified as NEETs, the cost of maintaining such damaging effects to the British economy is no longer abstract.

We have conducted an econometric analysis using a two-way fixed effects model to a balanced panel of UK International Territorial Level (ITL1) regions between 2010 and 2025. **Our central estimate is that for every one-percentage-point decrease in the bite ratio, youth employment rises by 0.37 per cent conditional on controls and fixed effects. When this is applied to the current population of 16–24-year-olds over a period of five years, there would be in the order of 270,000 additional workers in the labour market. The macroeconomic effects of this policy include an annual GVA gain of approximately £9.7bn, a gross fiscal gain for the Exchequer of £2.4bn and a present-value long-run human capital gain of £14.7bn; all of which are conditional events contingent on the central estimate.**

An outright reversal of the NLW to the bite ratio before its existence cannot stand alone. to the appropriate effects to be truly established, reforms to National Insurance (e.g. reverting the recent increase in employer NIC) and Universal Credit taper would be essential. Freezing the NLW would only require institutional restraint for it to be effective.[34] Fundamentally, our central estimates suggest that continued increase in the NLW risks exacerbating the growing trend of youth unemployment. A worthwhile course of action would look to reverse this trend.

34 This does not negate the importance of necessary reforms to the UC taper and NI.

Appendix

The youth employment-to-population rate is dependent on cyclical labour market conditions, the Kaitz index and some unobserved heterogeneity (error term):

$$E_{i,t}=\beta BITE_{i,t}+\boldsymbol{\gamma}'\mathbf{X}_{i,t}+\delta_i+\vartheta_{i,t}+\varepsilon_{i,t} \quad \text{(A.1)}$$

where

- $E_{i,t}$ represents the employment-to-population rate of adults from the 16–24 age group in region i at time t;
- $BITE_{i,t}$ is the regional Kaitz index (NLW divided by the median hourly wages);
- β which is the measure of the percentage-point change in the youth employment rate associated with a one-percentage point change in the bite ratio. This should not be treated as a conventional own-wage elasticity, but as a semi-elasticity expressed in percentage points;
- $\boldsymbol{X_{i,t}}$ is a vector of various controls (controls include unemployment rate, share of population in full-time education);
- δ_i observes the regional fixed effects (e.g. industrial composition);
- $\vartheta_{i,t}$ is the time fixed effect that absorbs shocks common to all region in a year (including uprating NLW);
- $\varepsilon_{i,t}$ is an error term.

A separate constant is not identified and thus omitted because the model includes both year and regional fixed effects.

Estimation

The panel data covers all 12 ITL1 regions in the United Kingdom over a 16-year period, spanning 2010 – 2025. This gives a total of 192 observations. Equation A.1 is a two-way fixed effect (within) regression with a clustered standard error of 0.230. Parameter estimates are derived following mainly Dube (2019), Manning (2021) and Cengiz et al. (2019).

A central estimate of $\hat{\beta}$=-0.372 , (p-value = 0.13; R^2 = 0.69; N = 192 and a clustered standard error of 0.230). Inference uses the t-distribution with 11 degrees of freedom (critical value of 2.201) given that the model has only 12 clusters. This gives a 95 per cent confidence interval for $\hat{\beta}$ of between -0.88 yo +0.13. This means that a zero effect cannot be ruled out as the estimate is not significant at the 5 per cent level.

We use an illustrative analysis for our sensitivity analysis in A.3 within a plausible range of -0.1 to -0.4.).

On the identification strategy

A major concern in our identification strategy (i.e. isolating causal effects) is that labour market conditions and the NLW are determined concurrently. This is because, the Low Pay Commission makes its recommendations based on interpretations of the state of the labour market across the country. Thus, it is difficult to establish explicitly whether wages affect economic conditions or vice versa. This is because wage variations across regions may correlate with unobserved regional characteristics. Therefore, estimates in this paper capture a conditional association across local labour markets, not a direct causal effect of the national policy itself. Mitigating for these confounding factors while isolating this conditional relationship, we do the following:

1. Although bite ratios are set regionally, NLW remains a national figure. Geographical differences in the bite ratio are driven by regional median wage differences. Adjusting for aggregate unemployment reveals that regional wage patterns are independent of temporary shocks to youth employment.
2. $\vartheta_{i,t}$ absorbs all national-level variations (plus LPC responses, i.e. changes to NLW). This means that β is not identified through policy changes directly, but only from differences in how the bite moves across regions.

On counterfactuals

Given an estimate for $\hat{\beta}$, to observe a counterfactual policy which would result in a reduction in the bite ratio from $BITE_0$ to $BITE_1$, we have:

$$E_{t\ counter}=E_{t\ observed}+\hat{\beta}(BITE_1)\text{-}BITE_0 \qquad A.2$$

This can be applied on a national scale, observing the total number 16–24 year-olds that will be employed as a result of this change in policy. This is expressed as:

$$\Delta N=\left(\frac{\hat{\beta}}{100}\right)\cdot(BITE_1\text{-}BITE_0)\cdot POP\{16\text{ to }24\} \qquad A.3$$

For $BITE_0 = 66$, $BITE_1 = 56$, (a return to the pre-NLW level), $\hat{\beta} = -0.2$, and $POP\{16\ to\ 24\} \approx 7.25$ million, equation (A.3) yields $\Delta N \approx +145{,}000$. Under the upper-bound elasticity $\hat{\beta} = -0.4$, $\Delta N \approx +269{,}700$. We hold the population number at its 2026 level, and the effect is reached by the end of the freeze in 2031.

Table A.1: Scenario estimates

Case	$\hat{\beta}$	Change in bite (pp)	Change in youth unemployment rate (pp)	ΔN
Central estimate	-0.372	-10.0	+3.72	+267,700
95% CI, lower bound	-0.878	-10.-	+8.78	+636,000
95% CI, lower bound	+0.134	-10.0	-1.34	-97,300
Scenario 1: lower	-0.2	-10.0	+2.00	+145,000
Scenario 2: upper	-0.4	-10.0	+4.00	+290,000
Central estimate, full freeze path (g = 3.5%)	-0.372	-10.4	+3.88	+281,300

Macroeconomic effects

Here, we set out the calculations of the macroeconomic effects reported in the productivity and output section of the document.

GVA effects

Let:

- N denotes the total number of Britain's employed workforce (approximately 33.5 million people),
- W denotes the average annual GVA contribution of existing workers (£80,500);
- ΔN denotes the additional employment as a result of freezing the NLW (approx. 270,000)
- W_m represents the average annual GVA contribution of the added-on entrants to the labour market (rounded to £36,000 or 45 per cent of W)

The pre-policy estimate of the aggregate GVA can be understood as *Y=N*W*. Post-policy, we are interested in the change effect $(i.e. Y' = \Delta N * W_m)$ with the absolute change in annual GVA expressed as:

$$\Delta Y=\Delta N^* W_m \qquad (A.4.)$$

$$\Delta(\text{GVA per worker}) = \frac{Y+Y'}{(N+\Delta N)} \qquad (A.4)$$

Therefore, the proportional change in GVA per worker is:

$$\frac{W'}{W} - 1 = \frac{\Delta N(W_m - W)}{(N + \Delta N)W} \qquad (A.5)$$

The annual GVA gain to be expected from freezing the NLW is estimated therefore to be **£9.7bn** with the change in GVA per worker falling by **-0.44** per cent due to diminishing marginal returns from extra labour.

Long-run wage scarring effect

Consider:

- D as the average annual earnings a British worker may obtain over the course of his career (ONS ASHE estimate this as £32,000)
- p as the proportional wage scarring effect as 8 per cent.
- T as the total length of a typical worker's career years (40 years)
- r as the HM Treasury recommended discount rate of 3.5 per cent (HM Treasury. 2026).

Without any wage scarring effect, we can apply the standard annuity formula to express the present value of career earnings as:

$$PV_0 = D^* \left[\frac{1-(1+r)^{-T}}{r}\right] \qquad (A.5)$$

Adding wage scarring effects depresses lifetime earnings by (1-p):

$$PV_1 = D^*(1-p) \left[\frac{1-(1+r)^{-T}}{r}\right] \qquad (A.5.1)$$

The gain the new entrant to the labour market would achieve by avoiding further wage scarring is the difference between PV_0 and PV_1:

$$\text{PV gain per worker} = D^*p^* \left[\frac{1-(1+r)^{-T}}{r}\right] \qquad (A.5.2)$$

We derive a per-worker present value gain of **£54,700**, which widens to **£14.7 billion** in present value when aggregated across approximately 270,000 additional workers to the labour market.

Fiscal effects

The relevant welfare and tax parameters are derived from public sources and applied to a representative worker. Let:

- k as the annual gross earnings of a young entrant at £20,000
- q_{PA} as the personal income tax allowance of £12,570
- τ_{PA} as the Employer NI threshold of £5,000
- r_{IT} as the personal income tax rate of 20 per cent
- r_{NIEE} as Employee NI rate of 8 per cent
- r_{NIER} as Employer NI rate of 15 per cent
- $\overline{UC}$ as the DWP (2025) estimated annual savings in Universal Credit per extra young adult in work (£4,500)

We can derive the per-worker effects as follows:

$$\gamma_{IT} = r_{IT}^* \max(0, k-q_{PA}) \qquad (A.6a)$$

$$\gamma_{NIEE} = r_{NIEE}^* \max(0, k-q_{PA}) \qquad (A.6b)$$

$$\gamma_{NIER}=r_{NIER}* \max(0,k-q_{PA}) \quad \text{(A.6c)}$$

$$\text{Net fiscal gain per worker}=G=\gamma_{IT}+\gamma_{NIEE}+\gamma_{NIER}+\overline{UC} \quad \text{(A.6)}$$

Aggregating across the additional employment as a result of freezing the NLW (ΔN) would give a value of

$$F = (\Delta N*G) \qquad (A.7)$$

Table A.2: Pre-worker fiscal gain

Component	Calculation	Per-worker (p.a)
Income tax	20% × (£20,000 - £12,570)	£1,486
Employee NI	8% × (£20,000 - £12,570)	£594
Employer NI	15% × (£20,000 - £5,000)	£2,250
Universal Credit saving ($\overline{UC}$)	DWP estimate	£4,500
Total fiscal gain (G)		£8,830

Applying the parameters in A.6a – A.6 yields G = £8,830 per worker per year. For approximately 270,000 workers, the annual fiscal gain becomes approximately £2.4 billion.

Table A.3: Summary of Central Estimates

Measure	Central Estimate (approx.)
Additional youth employment	270,000
Annual GVA gain	£9.7 bn
Change in GVA per worker	-0.44%
PV of avoided wage scarring	£14.7 bn
Annual gross fiscal gain	£2.7bn

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