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Minimum wage rises may prompt firms to switch to zero-hours jobs

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The UK's labour market performance continues to confound. The employment rate is at its highest level since figures began in 1971. Unemployment is at its lowest rate since early in 1975. Yet a supposed bogeyman still stalks the workforce statistics: the near million folk who identify as being on zero-hours contracts (ZHCs) for their main job.

Since the steep increase in this prevalence from 2013, the Labour party has made hay of the 901,000 people currently contracted without guaranteed hours of work. It is evidence, they say, of a jobs market characterised by low wages, few benefits, little security and scant hope of building human capital. Despite these workers representing just 2.8pc of overall employment, ZHCs have become the totemic issue in the debate about labour market regulation. In their 2017 manifesto, Labour promised to ban them entirely.

The virulence of this criticism is wrong-headed. ZHCs can clearly be mutually beneficial for employers and employees. But Jeremy Corbyn and co never stop to ask why companies may have expanded their use in recent years. Are bosses simply greedier than half a decade ago? That seems unlikely. The wider acknowledgement and awareness from workers of what ZHCs are may have contributed to their burgeoning number in official statistics. But new evidence suggests they may also be a consequence of a policy the Labour party is rather fond of: raising minimum wage rates.

In industries dominated by low-paid workers and where labour costs are a high proportion of total costs (such as retail and health and social care), ZHCs allow companies to buffer hits from rising statutory pay by reducing the number of staff on guaranteed hours. In effect, the burden of risk and insecurity is outsourced to employees, worsening their employment conditions, but better allowing firms to manage higher costs.

A recent paper by economists from the LSE's Centre for Economic Performance suggests the introduction of the National Living Wage in April 2016 had such an impact. The paper examined closely the effects on the social care sector, which at 15pc had the highest proportion of ZHC workers of any single industry. The sector's dependence on council funding also meant the opportunity to pass on cost increases through to higher consumer prices was very limited for these businesses.

Firms reacted to the minimum wage rise for over-25s by replacing some fixed hours jobs with ZHCs. The overall proportion of those employed in the social care sector on ZHCs increased by one percentage point – raising it 24pc above the pre-National Living Wage level.

According to their calculations, a domiciliary worker doing care in individuals' homes and earning the minimum wage saw, on average, a 7.5pc increase in their wage rate, but a 4.3pc increase in the probability of being on a ZHC.

Yet this effect was not limited to social care. Their analysis combining all low-paid sectors gave a similar conclusion. Minimum wage rises appear to come with big trade-offs on worker job security, even when firms don't react by directly cutting employment or hiring levels. This suggests the number of ZHC workers would be much lower today had the minimum wage not been increased significantly since 2010.

All this is not to say, of course, that ZHCs are inherently a bad thing or wouldn't exist if the minimum wage was much lower. Contracts with options for hours at short notice, that employers are not obliged to offer nor employees accept, bring flexibility, making them preferable to fixed-hour contracts for many.

On the employer side, this is obvious. In sectors such as tourism or hospitality, demand fluctuates massively depending on the weather or the number of time-sensitive bookings. But it is also true for many employees. A few years ago, McDonald's ran a trial offering all their ZHC staff new fixed-hours contracts. Just 20pc took up the offer. Surveys regularly show that ZHC workers overwhelmingly seem satisfied with the hours they are given, and are more satisfied with their work-life balance than full-time workers.

This is not surprising considering their demographic breakdown. A massive 36pc of ZHC workers are aged 24 or under, and nearly 19pc are in full-time education. Others include working mothers and fathers who want flexible, part-time jobs to allow them to care for their children, or pensioners who want incomes only at certain times of the year.

The economists' data suggests 42pc of ZHC workers hold multiple jobs, and about a third already have a job with a secure contract. ZHC positions, then, act as a form of "top up" for some, or as insurance against the possibility of lack of hours from other positions.

However, it is incorrect to extrapolate to say that all employees are happy with these terms. The Office for National Statistics figures show around a quarter of those on ZHCs want more hours. The economists estimate this figure could be as high as 40pc, with two thirds of this group saying that more hours at their company were simply unavailable. This is clear evidence that a significant minority of workers on ZHCs would prefer more security, if firms could afford to offer it.

While ZHCs are far less of a general "problem" than most commentators assume then, for some workers they are indeed deeply problematic. Rather than damning companies and bosses for their use though, Corbyn and co should consider the effect of the policies they favour.

Jack up the cost of full-time workers by raising minimum wage rates, and companies with razor-thin profit margins and little pricing power are pressed to manage their cost base in other ways. If not zero-hours contracts, it would likely be more painful adjustments, such as fewer job opportunities for these workers.

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