

[Raising the true minimum wage](#) [1]

Written by [Anton Howes](#) [2] | Monday 14 March 2011



The Social Market Foundation recently released a [report](#) [3] claiming that one of the best ways to boost the economy would be to raise the minimum wage. This received widespread ridicule, particularly from the Adam Smith Institute. However, the minimum wage is already being raised, even though it's nominally staying at £5.93 per hour for most workers.

The reason is simple: tax cuts. The 'true' minimum wage (as distinguished from 'real' wages when inflation is taken into account) is not £5.93. Assuming a 40 hour week for 52 weeks a year, it was more like £4.98 per hour in 2010-11 once income tax and employees' national insurance contributions were paid. In 2011-12 it will already be rising to £5.09 per hour due to the increase in the income tax allowance from £6,475 to £7,475. The coalition plans to raise this even further to £10,000 by the end of this parliament, allowing the lowest paid workers to keep £5.33 of their hourly wage.

The main charges against raising the minimum wage are that small businesses are hit hard, the lowest paid employees may be made redundant as wages cannot be negotiated any lower, and the unemployed are priced out of low-paid jobs. However, by raising the tax allowance, none of these effects manifest themselves at all, whilst the lowest paid enjoy higher 'true' salaries. In fact, from a welfare perspective, this rise is helping to make work pay. Unfortunately, it appears that unusually high inflation may erode these gains, but it's better than nothing.

Despite the cost to the treasury, it appears that this kind of policy really does help the low-paid without affecting businesses or the unemployed. Using the same assumptions, allowing those on minimum wage to keep all of their £5.93 earnings would require raising the allowance to around £12,344 whilst increasing the national insurance lower earnings limit (or primary threshold) to about £237 per week. If we really wanted to make work pay, we would try to increase the 'true' value of wages, with the eventual aim of taking minimum wage earners out of income taxes altogether.

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