Resolution Foundation

# Crystal balls vs rear-view mirrors

## The UK labour market after coronavirus

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Sudden and significant hits to the UK labour market in recent weeks have shown that this will be a jobs recession. The focus has rightly been on how to respond to the huge numbers of people losing work, but policy makers and pundits are also beginning to ask what this crisis could mean for the longer-term future of our labour market.

While most discussions take a speculative approach about changes that might follow this crisis, we argue that policy makers would be best to consider the areas in which current developments run alongside actual or latent patterns that were visible pre-crisis. Instead of speculating about a wholesale conversion to distance working, this approach prompts policy makers to focus on the decline of our high streets; a major change in our industrial mix as lower-skilled migration dries up; the need to better value the work done by lower earners; and the reality that younger workers are bearing the brunt of this crisis, just as they did during the financial crisis. On the other hand, we note that the rise in self-employment may well go into reverse in the years ahead in the face of higher perceived risk and actual taxation.

Though the pace of change to our labour market has been much faster in recent weeks than anyone expected, looking in the rear-view mirror is as important as staring into a crystal ball when it comes to understanding where the world of work might be heading beyond the crisis.

Crystal balls are being brought out around the country to consider the UK's post-coronavirus crisis future. The predictions that follow often focus on the labour market, understandably given the scale and speed of the impact of the crisis upon it. We are experiencing major changes to how some people (generally higher earners) work and others' (disproportionately lower earners) ability to continue doing so.

But too often predictions about our future labour market are based on what people have always thought would, or should, happen anyway. They come in both optimistic and pessimistic variants. Those in the latter camp predict a permanent retreat from record employment, while some in the former argue that this mass experience of working from home will bring to an end the era of the office and usher in a new era of dispersed workplaces. 'Imagine there's no commuting, it's easy if you try', is the mantra.

Imagining our future is of course an important task amid huge changes. Crises do change countries and their economic policies. This one will change the economic context for those policies, create a new political environment to contest them in (think burden-sharing and contribution recognition), and reinforce lessons we should already have learnt (such as the weakness of our social security safety net).

This note focuses on the first of those, the economic context. Here it is worth reflecting on what the best predictions are likely to be based on, where two elements in particular stand out. The first is a detailed understanding of the nature of the shock that post-virus Britain will be emerging from. But second, we must recognise that crisis effects are most likely to lead to lasting change, rather than interregnums or detours, when they reinforce actual and latent patterns of change that were shaping the country before the crisis hit.

So for policy makers, putting crystal balls away and focusing on where crisis and context might come together is the best way to understand the path our labour market may be on. This note offers some pointers as to where that path may lead.

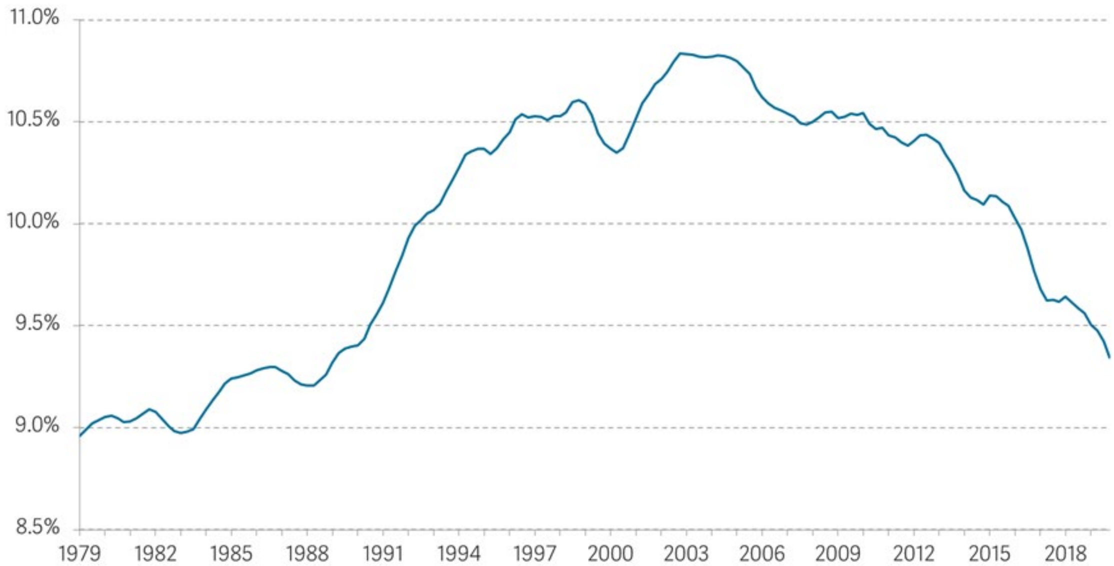
**Our high streets – from managed to unmanaged decline**

One of the most visible signs of the economic crisis has been the rapid shutdown of most of the (non-food) retail sector. While most closures should be temporary, the impact may be permanent as the managed decline of broad swathes of our high streets becomes a lot less manageable. We can already see that some previously struggling high street chains have closed their doors for good (Brighthouse), or are consider heading into administration (Debenhams). The pace of change even for firms that remain in business may also accelerate – some retailers are seeing the closure of bricks and mortar stores as a chance to accelerate the move online.

This marks a reinforcement of a two-decade trend of the sector's relative decline, shown in Figure 1. Yes, in the past decade this has been about the move to online shopping, but it's not just Amazon that is to blame. We all are, given our preferences to spend more of each marginal pound on experiences rather than things.

If the crisis precipitates a step-change in retail's decline, this will end up high on policy makers' post-crisis worry lists. This is partly due to the sector's importance for lower-paid employment, but also because the visibility of high-street decline is by far the most totemic signal of the relative decline of many places. Our high streets need time to successfully make the adjustment from retail-focused destinations to centres for work and leisure, but because of this crisis, time may be in short supply.

Figure 1 **Retail employment has been declining since the early 2000s**
Retail as a share of employee jobs: UK




Notes: Four-quarter rolling average.
Source: RF analysis of ONS, Workforce Jobs.

### The coronavirus hardstop to migration is a taste of where we are heading

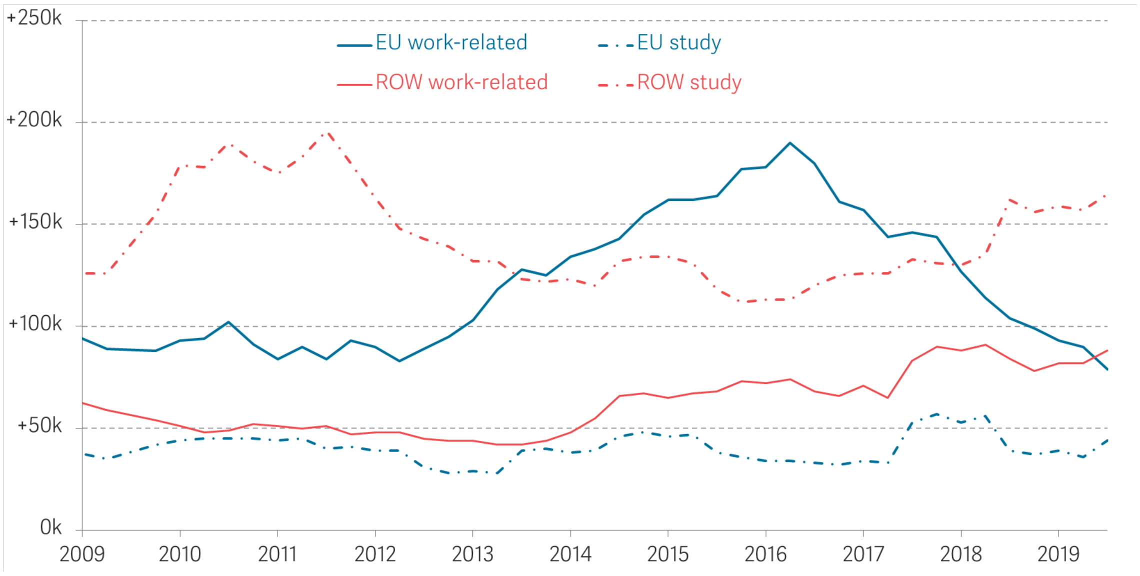
International travel, for leisure or work, has been brought to a standstill by this crisis. On the labour market side, we can already see the effects of this standstill in the challenges faced by the agricultural sector, which is unusually dependent on migration *flows* for seasonal workers. A lot of fruit will go unpicked this year. But a huge economic change for parts of our agricultural sector today looks set to become a longer-term shift in the extent to which lower-paid migration is a major feature of the British economy.

The scale of the current migration shutdown will of course ease, but there are very strong reasons for thinking we will not return to the levels we were used to during the 2010s. First, travel restrictions may well take much longer to be eased than many currently expect – countries wrestling with how to restart their economies while controlling the virus may well choose to keep more stringent arrival restrictions. Second, even if more restrictive border controls aren't in place, potential migrant workers' uncertainty about their re-emergence will discourage arrivals. Third, our labour market will have a lot more slack in it post crisis, and high unemployment, rather than the record employment we've become used to, makes Britain less attractive to potential workers overseas.

And crucially, fourth, change was already underway. As Figure 2 shows, declining work-related migration was already a major feature of pre-crisis Britain, driven by a fall of more than half in net EU migration to the UK since 2016. While migration from the rest of the world has picked up to partly offset the impact on overall migration numbers, that has included big rises in those coming to study – so the change for the labour market remains very large indeed.

Figure 2 **Work-related migration peaked before the EU referendum**

Annual net migration to the UK, by reason and EU/non-EU




Source: RF analysis of ONS, Long-Term International Migration.

Reinforcing these trends, the Government has committed to a new migration regime, which promises to further drive down migration for lower-paid work. Coronavirus will combine with post-referendum economic and political trends to mean that, for parts of our labour market reliant on lower-paid migrant labour, change has arrived and is here to stay.

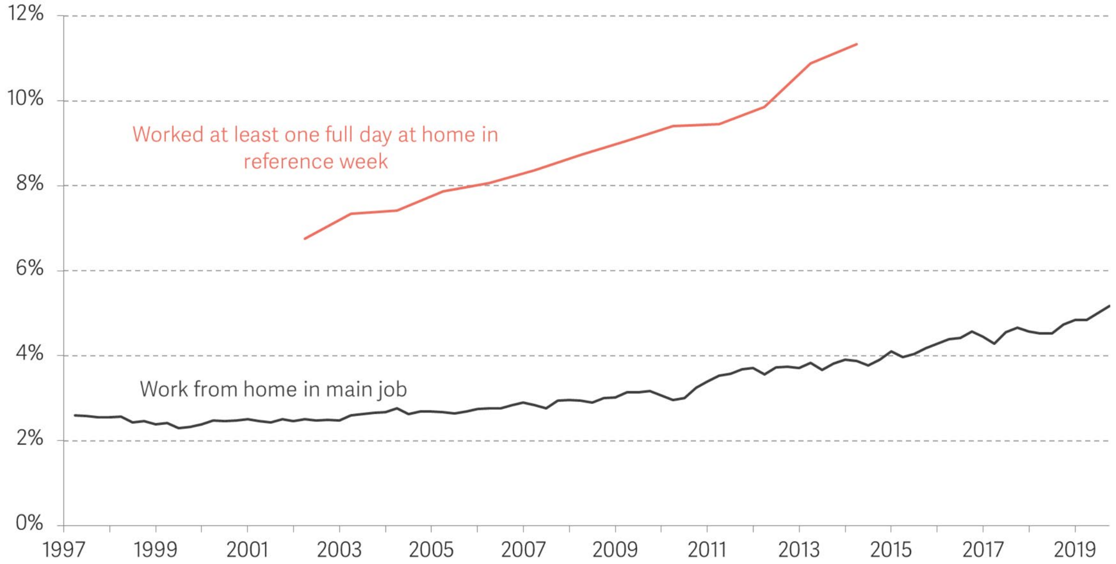
**The workplace is here to stay, but part-time home working by professionals may well increase**

For some luckier workers, the biggest personal change resulting from the coronavirus crisis is that they now have to work entirely from home. This will have been a big change – even among the highest-paid employees, who are most likely to be able to work from home, only around half said they were able to do so pre-crisis. But this change has also precipitated a swift learning curve where many find that modern IT makes working from home significantly easier than they expected. This has led some futurology discussions to predict that this crisis may sound the death knell for the traditional workplace, where most companies have most of their staff onsite.

There will surely be changes in individuals' behaviour, although the evidence suggests we should be cautious about those proclaiming a totally new era of organisations running on mass home-working. Huge leaps forward in what IT makes possible over the last few decades have been accompanied by only a gradual increase in those entirely working from home . Despite the rate doubling over the past twenty years, only one-in-twenty workers were working from home when this crisis hit, as Figure 3 shows.

Figure 3 **Only one-in-twenty employees worked from home pre-crisis**

Proportion of workers who work from home in their main job: UK




Source: RF analysis of ONS, Labour Force Survey.

This low level shouldn't be a huge surprise. Economists spend a great deal of time pointing to the role of agglomeration effects in driving the productivity of both firms and places. Ideas spread when large numbers of people interact, and people do a lot more interacting when physically present. Meanwhile, biologists and sociologists have rather older arguments for why we may prefer at least some office working – we're social animals. And leaving aside the preferences of businesses and people, it's worth remembering that not everyone is a higher-earning professional. While many professionals can relatively easily move to doing more home working (see the faster growth in the red line in Figure 3), that is manifestly untrue for lower earners, only one-in-ten of whom say they could do so. When we reopen our economy, waiters and cleaners aren't going to be doing their jobs from their spare room or kitchen table.

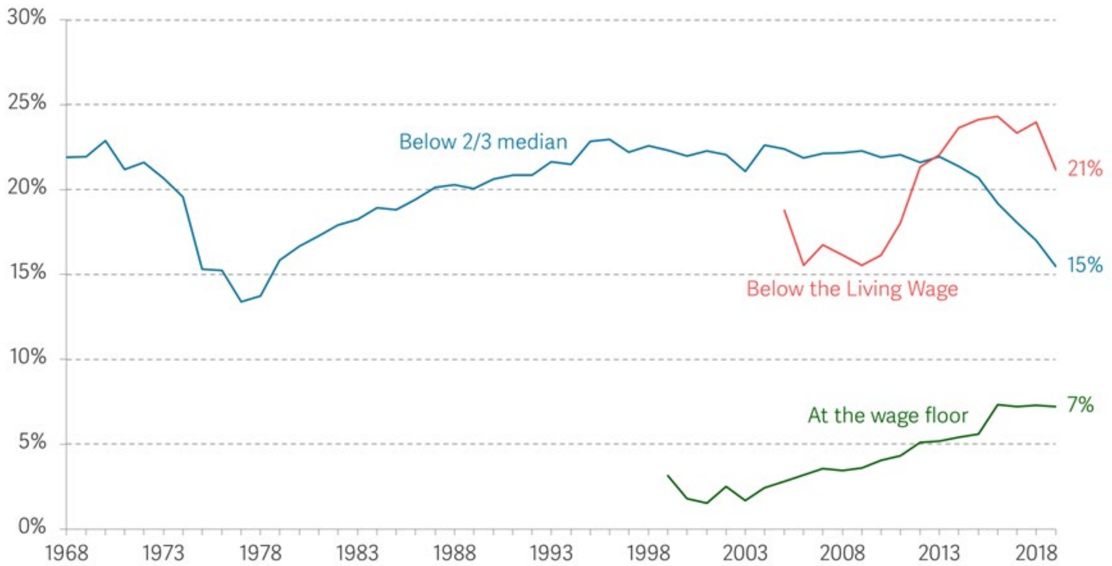
So the future we should prepare ourselves for isn't the death of the workplace, but further increases in the number of higher earners in service sectors who spend some of their working week at home.

**Low pay will decline**

The very reason many lower earners can't work from home is why they are both most affected by the shutdown of certain sectors (restaurants), and most exposed to the health risks of delivering essential services in others (food retail and care).

The widespread recognition of these facts will reinforce the political consensus on increasing our minimum wage. The National Living Wage (NLW) introduction in 2016 has driven the first sustained fall in low pay for four decades, as Figure 4 shows. The Government is committed to taking this further by 'abolishing low pay' (equivalent to raising the NLW to two-thirds of typical earnings) by 2024.

Figure 4 **Low pay was in decline, supported by increases in the wage floor**
Proportion of all employees below selected low pay thresholds: GB




Source: RF analysis of DWP, Family Expenditure Survey; ONS, New Earnings Survey Panel Data (NESPD); ONS, Annual Survey of Hours and Earnings.[1]

This welcome commitment will be made more challenging by the very difficult economic situation we face, which is why the Low Pay Commission has said it will carry out a review to see if the government should be reconsidering the pace of increases. But we should expect them to continue, partly because of the crisis reinforcing the pre-crisis consensus on this issue and partly because the policy is to set the minimum wage relative to typical earnings. This means that in so far as an adjustment is required, it should largely take place via lower-than-previously-expected typical earnings.

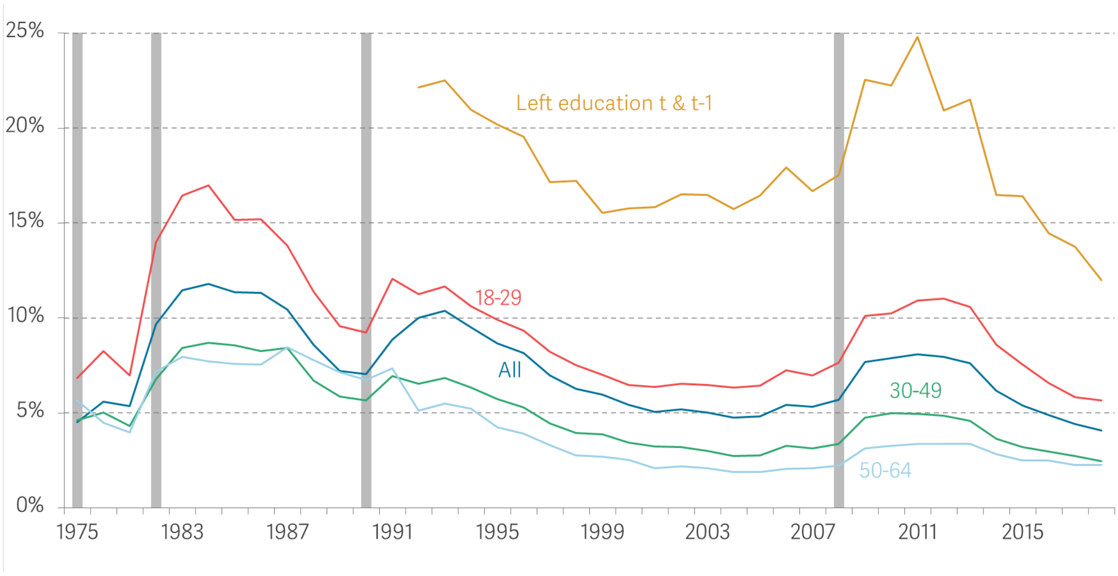
The coronavirus crisis has shed a light on low pay and called into question how we value our most essential workers. A rising minimum wage and falling low pay will be central features of our post-crisis world. But genuinely valuing low paid work will require us to go much further, via regulation of minimum standards, enforcement of the rules we have already set, and in some cases a recognition that valuing people will require us to pay more (in higher taxes, or prices, or government funding for services like social care) than we do today.

**The young will bear the burden of this recession**

The unprecedented economic changes of the past month are a result of policy decisions to mitigate a public health crisis. We are rightly saving lives at significant economic cost. More specifically, we are rightly saving disproportionately older lives at the price of reducing disproportionately younger people's living standards.

We already know that younger workers have been most likely to lose their jobs in this crisis. More broadly, the initial impact of recessions tends to be hardest felt by those leaving education and entering the labour market in their midst. As Figure 5 shows, recent education leavers experience by far the biggest increases in unemployment. The financial crisis pay squeeze also hit younger workers the hardest, with those in their 30s today who entered work during that crisis still bearing deep scars on their earnings.

Figure 5 **Younger and newer workers lose out after an economic shock**
Unemployment rate, by age and left education within the past two years: UK




Notes: 'All' unemployment rate is for age group 16+.
Source: RF analysis of ONS, Labour Force Survey.

This time round, policy is accidentally reinforcing these trends. The Government is rightly socialising much of the costs of this crisis, by underwriting wages and compensating the self-employed. But these approaches create insider/outsider dynamics in which the young come off worst – compensating people for the earnings they already had rather than the potential earnings they would otherwise have received. We do not compensate the young for the jobs they would otherwise have got or the pay growth that is the norm in early careers.

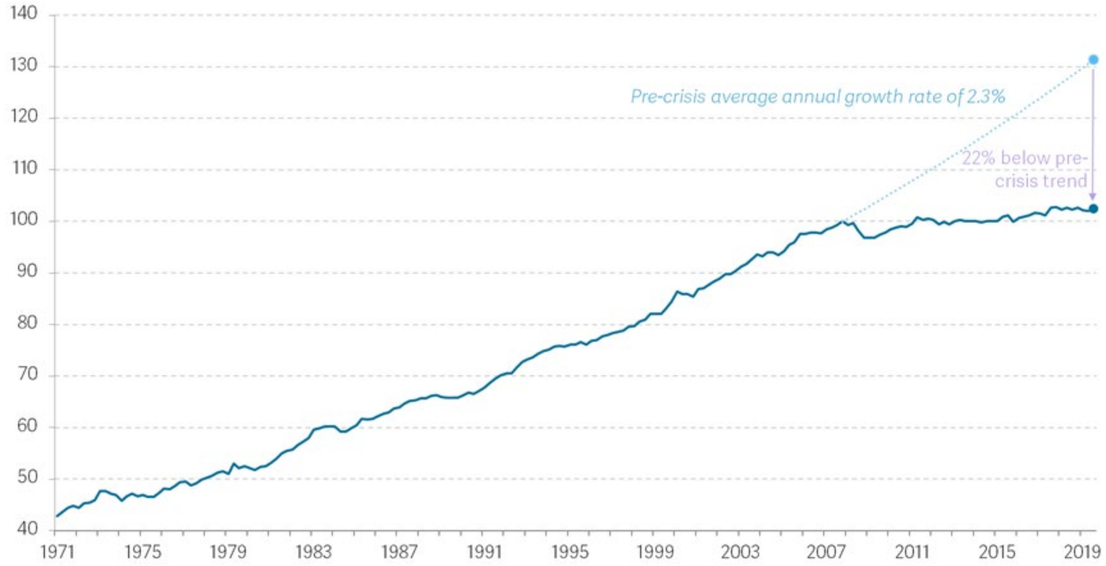
With over a million under-25s entering the labour market for the first time each year[2] – peaking in the third quarter, when the economy will probably be only just starting to open up again – today's young education leavers will pay a high price from the necessary public health measures being taken.

**Weak income and productivity growth are here to stay**

Closing non-essential businesses and putting people out of work (albeit often temporarily) will clearly have an immediate impact on economic output as well as household incomes. On the productivity side, measures of output per worker will crash if (as we expect) furloughed workers continue to be counted, while social distancing measures adhered to by many continuing workers will constrain how productive they can be.

Looking further ahead, prospects are far less clear, but we start from a weak position. Productivity never materially recovered from the financial crisis over a decade ago, and remains more than a fifth lower than where it would have been if the pre-crisis trend had continued, as Figure 5 shows. In their largely pre-virus March forecasts, the Office for Budget Responsibility suggested that growth will average just 1.4 per cent a year in the coming years, well below pre-crisis trend growth rates.

Figure 6 **Productivity has flatlined since the financial crisis**
Productivity per hour worked (2007 = 100): UK




Source: RF analysis of ONS, Labour Productivity.

The impact of the crisis on earnings may be particularly big given that we are almost overnight waving goodbye to the tight labour market that was at last driving earnings growth up, and meant that earnings finally returned to their pre-crisis peak as recently as December. One way to think about our post-crisis world is that we'll be living with the aftermath of a trilogy of hits to incomes and productivity: the financial crisis, Brexit, and now coronavirus.

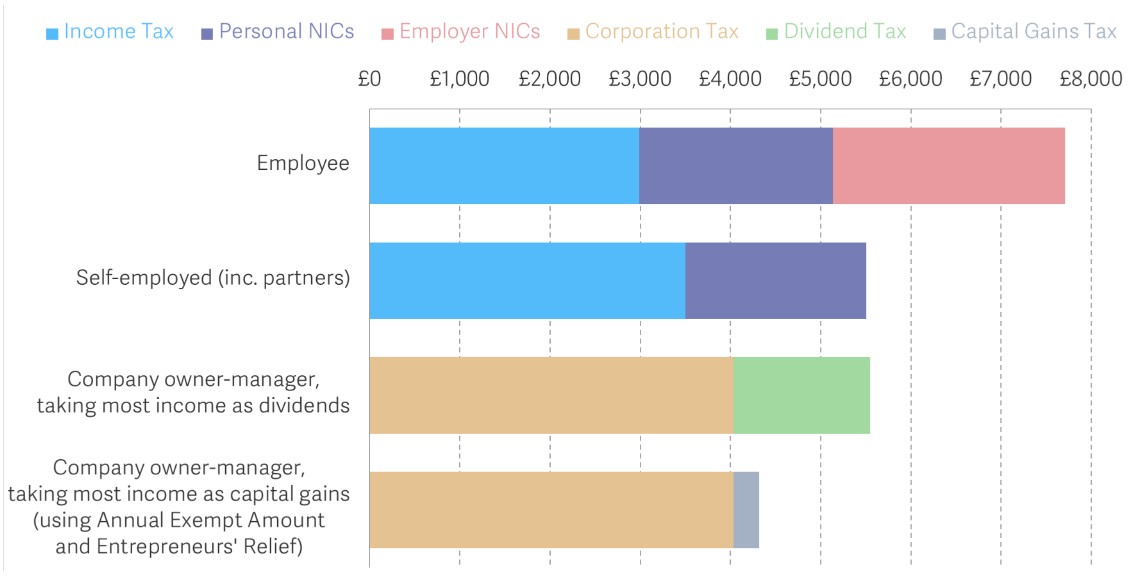
**Some trends will go into reverse – like the growth in self-employment**

While the argument of this paper is that post-crisis trends may well build on actual or latent patterns in our economy, others may mark more of an about turn. But even here they are most likely to be those where there were reasons to expect a change anyway.

While other forms of atypical work may be expected to rise post-crisis, as labour market slack returns, self-employment stands out as an area where the long-term trend could be reversed.

The pandemic crisis could well trigger falls in self-employment. In part that might be because it has thrown into sharp relief the risks of this form of working, which won't always be underwritten by the kind of support available now. But more importantly, the support for the self-employed announced by the Chancellor – more generous than the support for employees – came with a quid pro quo in the form of higher taxes down the line, to equalise the treatment of the self-employed and employees. As Figure 7 shows, the tax gap between the two is considerable, largely due to the lack of an equivalent of employer National Insurance contributions for the self-employed.

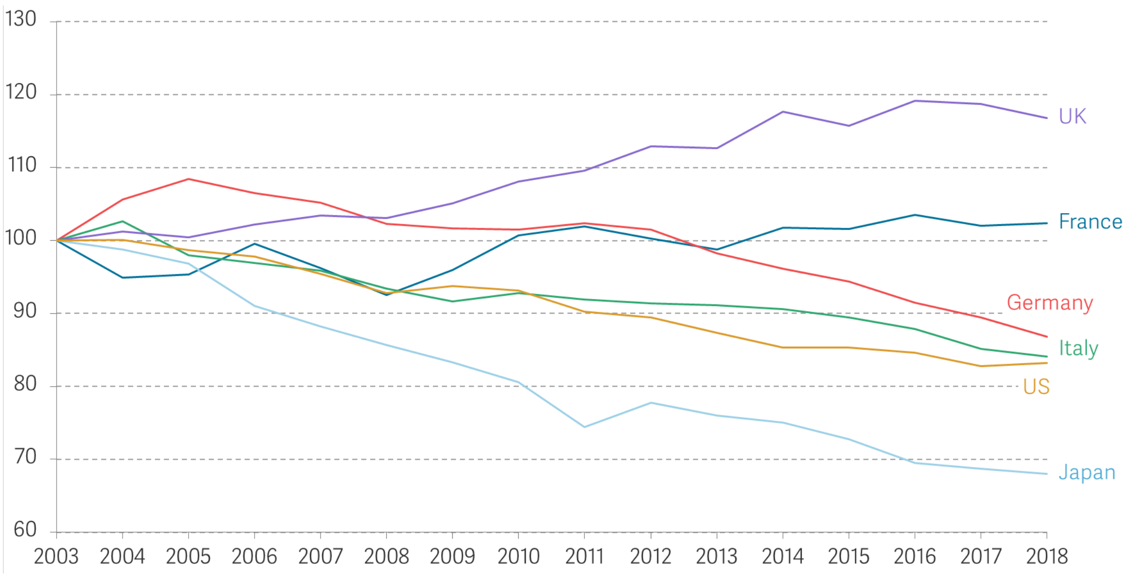
Figure 7 **The self-employed have a tax advantage over employees**
Tax paid on £30,000 of market income, by legal form: 2020-21




Notes: Employee salary is £27,400 after employer National Insurance contributions. Example company owner-managers pay themselves a salary equal to the employer National Insurance contribution threshold (tax-free) and in both cases take advantage of the dividend allowance.
Source: RF analysis.

This tax gap has been a bigger driver of the UK's self-employment growth than the technological advancements that people like to ascribe it too. After all, technological change has been common across developed economies but the huge growth in self-employment is very UK specific, as shown in Figure 8.

Figure 8 **Self-employment has grown faster in the UK than elsewhere**
Index of self-employment as a proportion of total employment (2003 = 100)




Source: RF analysis of OECD, Self-employment rate (indicator).

## Conclusion

There are lots of reasons for getting your crystal ball out at present. Our world has changed more in the past few weeks than any of us thought was remotely possible. And change will continue in the months and years ahead, as we wrestle with a shock of this scale. But as we do so, it's worth having an eye not just on the crystal ball but the rear-view mirror, too. That's how we maximise our chance of understanding where Britain's labour market may head after this crisis.

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2 Source: RF analysis of ONS, Labour Force Survey Two-Quarter Longitudinal Dataset.