The Great Stagnation: Briefing 6

The Labour Market

By Len Shackleton

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Summary

- An efficient labour market adjusts quickly and effectively to change in the global and domestic economies, reallocating workers from declining to expanding sectors.
- An important reason for Britain's slow growth in productivity and output since the financial crisis is the increasing reach of labour market regulation, which has gummed up this process of adjustment.
- This has been the result of new employment laws, the extension of existing laws through Employment Tribunal decisions, and the spread of occupational regulation.
- Wage adjustments play a major part in reallocating people between jobs, but wage signals are now distorted by government fiat.
- Around 20 per cent of all employees have their pay directly or indirectly determined by the minimum wage, while in the public sector powerful trade unions distort pay rates and structures.
- Tightened legislation on unfair dismissal inhibits firms' ability to change their employment patterns and slows the process of creative destruction.
- Movement between jobs is increasingly restricted by occupational regulation, with 22 per cent of all employees now requiring a government licence, up from 13 –14 per cent in 2011.
- Expansive interpretation of equal pay legislation means that many jobs have to be paid the same even though market conditions differ, creating a mismatch between supply and demand.
- In addition, other aspects of the economy – tax and benefits, education and training policy, housing shortages – have restricted the opportunities and altered the incentives facing workers and made it difficult for them to respond rapidly to changing employment opportunities.

About the author

Len Shackleton is Professor of Economics at the University of Buckingham and Research and Editorial Fellow at the Institute of Economic Affairs.

About the publication

This briefing is a version of a chapter that will appear in a forthcoming IEA book, *The Great Stagnation: Why Britain Stopped Growing*, along with contributions from other authors. Each chapter presents and analyses a distinct explanation for the decline in British economic growth over the last two decades.

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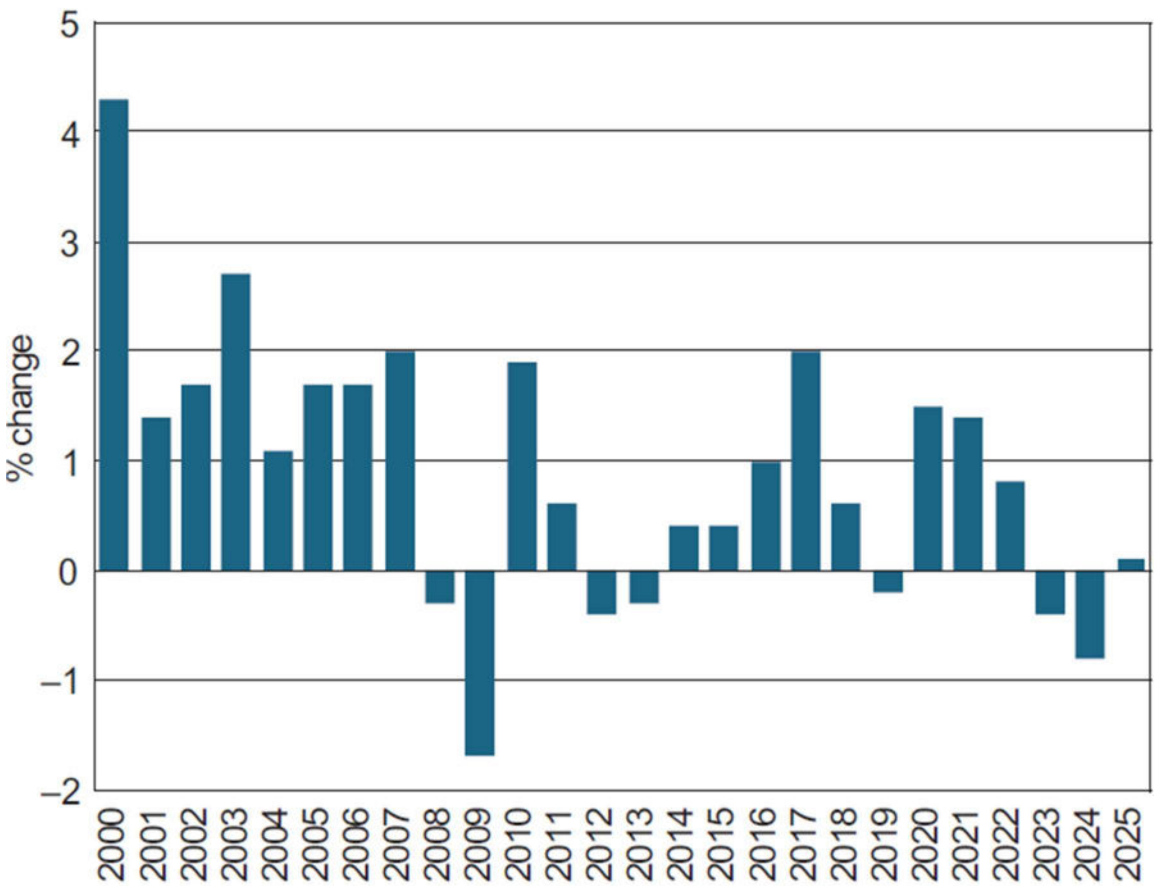
Introduction

There is no single or simple explanation of Britain's poor productivity performance – illustrated in Figure 1 – since the financial crisis of 2008/09. But at least part of the story is the impact which rapidly increasing regulation of the labour market, and regulation in other contingent areas, has had on businesses and workers.

This regulation has involved the Labour Party, the Conservative–Liberal Democrat Coalition and the later Conservative administrations. In the period before Brexit, the European Commission was also a significant player. Rather than seeking to blame any particular actors, however, it is worth observing that growing intervention in the labour market has had support across the political spectrum, from trade unions, EDI-minded business people, civil servants, 'progressive' pressure groups, the ever-increasing lanyard-wearing classes and human resource managers, all of whom seem to imagine that without the latest regulatory boondoggle greedy capitalist employers would exploit helpless workers. Indeed, these groups have in some cases helped to introduce further distortions into the jobs market in addition to those produced directly by government.

Figure 1: Annual percentage change in UK output per hour worked 2000–25



Source: ONS (https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/labourproductivity/timeseries/lzvd/prdy).

How labour markets work

Economists who spend time thinking about labour markets, however, tend to take a more sceptical view of such interventions. They start from a model which sees employment as a mutually beneficial transaction between employers and employees, both of whom have agency and can choose between alternatives. Mainstream economics envisages the optimal level of employment – that which maximises well-being – as one where the wage rate paid is equal to the revenue produced by the marginal hour of work provided. If it costs £15 to employ an extra bar worker or fruit-picker for an hour and that hour brings in £40 of additional revenue, it's worth employing them. If it brings in only £10, it's not. At £15, the worker is just generating enough income to cover the cost of their hour's employment.

As for the employee, the £15 received is just sufficient to compensate for giving up an extra hour of 'leisure' (or work in the home, such as looking after children or elderly parents, or digging up their allotment). In an idealised competitive market, these two aspects of the wage are equalised, and all who want to supply work at the going rate are able to do so, while employers can obtain all the labour they want at this wage. Both parties are 'price takers' in the labour market. Profitable output is maximised and no individual or firm can be made better off without making someone, somewhere, worse off.[1]

This is a static and hopelessly over-simplified picture. Labour markets never settle in one state: they are a dizzying kaleidoscope. Patterns of demand alter all the time as fashions and tastes mutate; so do production possibilities as technologies change. Entrepreneurs dream up new goods and services to offer or puzzle out cheaper ways to produce existing commodities. Meanwhile the labour force constantly reshapes as people enter and leave work, retrain for new skills, partner up and have children, or change their preferences between types of job and between work and leisure.

In a dynamic context, an optimal labour market adapts instantaneously to change and moves seamlessly and costlessly from one quasi-equilibrium to another. Of course, no labour market there has ever been or ever will be can precisely match the static and dynamic conditions for optimality.

More realistically, well-functioning real-world labour markets are those which adjust rapidly to change. They reallocate people as quickly as possible if their previous employment dries up or new opportunities are presented. The process is rarely painless, but a labour market that does this is going to be associated over time with increasing labour productivity, rising wages and greater employee and consumer satisfaction.

Critics point to a number of real or potential 'market failures' which are held to justify government intervention. There may be insufficient competition between employers, giving them market power which they abuse; incomplete information or employer discrimination may prevent employees from getting jobs they would prefer; inadequate

[1] Of course, businesses wish they could pay less, while workers wish they could be paid more, but in this situation the two parties are voluntarily making the best deal they can.

access to capital may limit access to training or education which would raise productivity and enhance their earning power.

There have long been forms of regulation which attempt to mitigate these problems. Some such interventions may indeed be justified. But increasingly government meddling in employment matters has not been primarily motivated with offsetting objective weaknesses in markets. Rather it has been in pursuit of 'social justice', which can be used to justify any intervention, however cack-handed. Misconceived intervention can then give rise to government failures if it raises costs to employers and employees, and distorts incentives in such a way as to discourage or misallocate employment – with negative implications for productivity and the growth of national income.

Increased employment regulation

Before the financial crisis, it was often argued that the UK had got the balance between market forces and regulation of employment roughly right. The labour market reforms of Margaret Thatcher and John Major had greatly reduced the power of trade unions, which had blighted Britain's economic performance in the 1960s and 70s. Government wage-setting both by prices and incomes policy, and in dozens of industry-based Wages Councils, was a thing of the past. While overt discrimination against women and ethnic minorities was now illegal, and unfair dismissal legislation limited the ability of employers to fire workers, regulation was nowhere near as strict as in most of continental Europe, where unemployment was typically higher and labour force participation sometimes much lower. Britain's 'flexible labour market' was held up as a strength. Although a Labour government had been elected in 1997, it did little to reverse the Thatcher–Major reforms. While it did introduce a National Minimum Wage for the first time, this was set relatively low, and a semi-independent Low Pay Commission, which made annual recommendations about the minimum wage, was enjoined to bear in mind the state of the economy and the labour market – so that in periods of economic downturn lower increases were set.

Figure 2: The Heritage Foundation's Labor Freedom Index 2000–25

Source: Heritage Foundation, Economic Freedom Index (https://economicfreedom.heritage.org/pages/all-country-score).

However, following the financial crisis things began to change with a movement towards greater and greater interference by government in employment matters. This can be illustrated graphically in Figure 2, which plots the values of the Heritage Foundation's 'Labor Freedom Index' for a twenty-year period. The index reflects various aspects of the legal and regulatory framework of employment, including the minimum wage, laws inhibiting dismissal, severance requirements and conditions on hiring.[2] A high value represents a relatively unregulated labour market, so the trend shown is of an almost continuous increase in regulation.

This only concentrates on a limited number of formal indicators. Nevertheless, it is a pointer to the way in which successive governments have placed greater regulatory constraints on the operation of the UK labour market. If this has adverse effects, it will make for slower adjustment to changes in the demand for and supply of labour – manifested in mismatch between job seekers and vacancies.

A cross-economy sign of this could be given by estimates of the UK's Beveridge curve, which shows the relationship between the unemployment rate and the vacancy rate. There is some evidence (Hobijn and Sahin 2013; Cepparulo 2024) that the curve may

[2] The index is derived from six quantitative factors: ratio of minimum wage to the average value added per worker, hindrance to hiring additional workers, rigidity of hours, difficulty of firing redundant employees, legally mandated notice period, and mandatory severance pay. It is based on data collected in connection with the World Bank's 'Doing Business' study.

have shifted to the right since the financial crisis, meaning that a higher unemployment rate is now associated with a given vacancy rate, a greater mismatch between workers and the jobs potentially available to them.

The increase in employment regulation has many dimensions and comes to us in different ways.

New domestic legislation

A complete listing of new employment laws – some of which resulted from discrete Acts of Parliament while others were based on delegated powers under earlier legislation – would take a great deal of space. A few headline examples of the former include the Pensions Act 2008 (implemented in 2012, this required employers to offer enrolment in private pensions and make a contribution), the Equality Act 2010 (which introduced the term 'protected characteristics' and strengthened equal pay rules), the Children and Families Act 2014 (introducing shared parental leave), the National Minimum Wage (Amendment) Act 2016 (introducing the National Living Wage) and the Employment Relations (Flexible Working) Act 2023 (which strengthened the right to request flexible working). The Employment Rights Act came into law at the end of 2025: it is likely to have greater implications than any other single piece of employment legislation, but parts of it do not come into operation until 2027 and its consequences will take some years to work through.

Examples of the use of delegated ministerial powers include the Blacklist Regulations 2010 (which prohibited blacklisting of construction trade unionists), the Agency Workers Regulations 2010 (which gave agency workers the right to the same conditions as permanent workers after 12 weeks), the requirement for all businesses and private institutions employing 250 people to publish sex pay gap statistics under Equality Act regulations and the National Minimum Wage Regulations (which allowed Sajid Javid to raise the target for the National Living Wage to 66 per cent of median hourly earnings). Some laws have been piggy-backed on other legislation; for example the Apprenticeship Levy (which obliges larger employers to pay a levy based on their wage bill) was brought in via the Finance Act 2016, and subsequent delegated powers.

Court or tribunal judgements

Many other extensions of employment law have come through interpretations of statutes or common law judgements in employment tribunals, appellate courts and higher courts. These judgements can stretch legislation into areas which were not necessarily intended and probably never discussed during the passage of Acts through Parliament. Unlike planned changes in employment legislation, tribunal judgements are never costed even though their consequences can be extremely expensive to employers.

Examples include the case of Uber drivers who were held to be 'workers' rather than self-employed contractors, and thus entitled to a number of rights such as minimum wages, holiday pay and rest breaks; equal pay decisions which focused on 'work of equal value' at Asda, Next and Birmingham City Council (where judgements have contributed to a semi-permanent financial crisis and continuing industrial action); minimum wage adjudications requiring employers to pay for on-call workers, clothes requirements and travel between clients; widening the definition of protected characteristics to include a variety of quasi-religious beliefs and categorising loosely defined mental health problems and obesity as forms of disability to which employers must adapt.

Occupational regulation

The instances mentioned so far are measures which affect businesses and other organisations right across the economy. But in addition there is occupational regulation, typically through licensing of individuals. UK governments determine not only the status of historically regulated professions such as medicine and law, but who can be everything from a gas engineer to an architect to a racehorse trainer to an art therapist.

Following the financial crisis there has been a considerable expansion of roles which require some form of certification including in some cases formal licensing. But there are also new regulatory requirements for social workers, nursery workers, various paramedical professions, security guards, building workers, CCTV operators and train drivers. The result is that now some 22 per cent of the workforce are believed to work in a licensed profession (Koumenta 2024). Fifteen years ago the estimate was only 13–14 per cent (Humphris et al. 2010; Forth et al. 2011).

Occupational regulation raises costs (and may restrict access) to the public. Because it usually involves significant costs to individuals (fees, exams, continuing training), unnecessarily extensive regulation may indirectly act to exclude people from jobs for which they would otherwise be suited.[3]

Other labour market impacts of government policy

In addition to direct regulation of employment, many other aspects of government intervention have implications for the functioning of the labour market. Changes in a variety of policy areas since the financial crisis will have impacted on jobs and pay.

Taxation and benefits

The effect of taxation on the workings of the economy is a subject in itself (and is discussed in the previous briefing in this series), but there are some points worth making here. All taxation of earnings (income tax and national insurance) creates a gap between what employers pay and what workers receive in disposable income and complicates the simple model of the labour market sketched earlier.

[3] As Koumenta (2024: 12) points out, once an occupation is licensed, there is nothing to stop its gatekeepers 'regularly introducing tougher entry restrictions … lowering the pass rate on licensing exams and lowering the number of available places in educational institutions'. This will reduce the number of applicants (especially those from disadvantaged backgrounds) and increases the economic rent obtained by incumbents.

Tax and NI contributions have fluctuated since the financial crisis but the overall percentage tax take has increased. In recent years this has partly been the effect of failing to raise tax thresholds in line with inflation. A particularly egregious example is the '£100k trap'. From 2010, as annual earnings rise above £100,000 the personal allowance (on which no tax is chargeable) begins to be reduced. This means that the marginal rate of income tax rises from 40 to 62 per cent – more if you are repaying a student loan – up to the point where all the personal allowance is exhausted (at £125,140). The point is that the nominal threshold has not changed since it was introduced, despite more than a decade and a half of inflation. Whereas only around 600,000 were caught in the trap in 2010/11, in 2025/26 the figure appears to have risen to just short of 1.5 million.

Sharp increases of this kind in the marginal tax rate must surely have an impact, and there is some evidence, for example, that there is 'bunching' at incomes just below £100,000 (Joyce and Xu 2019). This may involve people under-reporting incomes, or retiming bonuses, or increasing salary sacrifice into pensions. However, it may also affect labour market behaviour such as reducing hours worked or turning down promotions.[4]

If effective marginal tax rates on higher earners may affect labour market behaviour, this is also true of the steep withdrawal taper faced by people on income-related benefits. The introduction of Universal Credit from 2010 onwards made some improvements to the incentives facing the unemployed and low earners, but they are still problematic. When you add together the effects of Universal Credit withdrawal, tax and NI contributions, around two-thirds of previously unemployed workers would face a 'participation tax rate' of more than 50 per cent. Two-thirds of those already working part-time would face a 'tax rate' of more than 60 per cent if they increased their hours, with 9 per cent losing at least 70 per cent of each extra £ earned (Ray-Chaudhuri and Waters 2024). With entering work or increasing hours in low-paid jobs being 'taxed' so heavily, it is not surprising that large numbers of potential workers are tempted to remain on benefits. If the financial benefits of taking jobs are limited, they need a degree of chivvying. Although pressure on claimants to take jobs appears to have increased under the Coalition from 2010 to 2015, this has been relaxed since – especially during and after Covid.

Higher education policy

Since the financial crisis, the numbers of home students in higher education have continued to rise: from 1.58 million in 2008/09 to 1.76 million in 2024/25. From 2015/16 onwards, there were no longer limits on student numbers (except for expensive medicine and dentistry courses). The fees which universities were allowed to charge failed to keep pace with inflation, and so they reacted by increasing intake to share overheads among larger student numbers – including ever-growing numbers of foreign students, whose fees were not fixed, and many of whom stayed behind after graduation to swell the numbers of graduates seeking employment.

[4] A related issue is the effect of new limits (introduced in 2016) on free-of-tax pension contributions. According to a BMA survey (Brady 2019), this caused some senior hospital doctors and GPs to reduce hours or retire early.

Critics argue that universities behaved irresponsibly by dropping entry standards and taking students onto low-cost courses which could easily scale but which did little to enhance employability. Whatever the truth of this claim, the rapid expansion of higher education has meant that the returns to education have declined – to the point where an IFS study (Britton et al. 2020) suggested that 20 per cent of graduates would be better off over their lifetime if they had not been to university. Poor returns reflect the finding of Vecchia et al. (2023) that only just under half of employed graduates are in 'graduate jobs' in the field for which they studied, while 30 per cent of graduates work in non-graduate jobs. The authors of this study conclude that mismatch on this scale indicates 'a misallocation of resources that can contribute to the UK productivity slowdown'.

Training and apprenticeships

Given the problems with higher education, it is often argued that we should place more emphasis on offering apprenticeships to young people. There is certainly a demand for apprenticeships; it is suggested (Wolf 2025) that there are three applications for every place among those about to leave school. And advocates point to skill shortages which employers had been mitigating by importing workers, something which should be ended, or at least much reduced.

The Conservatives introduced a new funding mechanism in 2017: the Apprenticeship Levy. This was in effect a 0.5 per cent payroll tax on employers with a wage bill of at least £3m. Organisations could claim money back if they committed to providing apprenticeships in a standard, nationally determined framework which had several different levels.

After the levy began, there was an initial crash in the number of apprenticeship starts. The new scheme, which replaced older direct funding from government agencies, was said to be too bureaucratic and complicated, and was widely criticised. Some employers felt that an apprenticeship structure did not fit their training needs. Particularly in fast-changing technology sectors, the classic apprenticeship model involving mastering a set of known and established skills may seem outdated.

However, starts began to pick up as organisations began to understand they could use the funding system to their advantage. But, as frequently happens, unintended consequences flow from apparently well-intentioned government schemes. Ministers had said they wanted to improve the skill levels of workers. Many big employers, including many in the public sector, took them at their word and started to use the scheme to support higher level 'apprenticeships' for managers and other relatively senior employees. By 2024/25, more than half of all new apprentices were aged 25 and over; 16 per cent of them were already graduates when they began their apprenticeships: 4 per cent even had master's degrees. These Advanced Apprenticeships – for operations managers, project managers, HR consultants and so forth – were crowding out lower-level apprenticeships for school-leavers. Meanwhile there were continuing shortages in construction trades, engineering and digital skills.

Following mounting criticism (including that in Alison Wolf's scathing 2025 report for the Social Market Foundation), some changes have been made, including removing funding for older apprentices on masters-equivalent programmes and redirecting it to younger people, while rebadging the scheme as a 'Growth and Skills Levy', thus giving employers the flexibility to offer shorter skills-based modular training. But some would argue the scheme should be scrapped in its entirety.

Housing policy

Since the financial crisis, housing construction – increasingly bogged down by energy and environmental mandates – has not kept pace with the increase in population resulting from substantial net migration. The private rented sector has become much more tightly regulated since around 2015 with increased tenant rights and landlord mandates, while mortgage costs have risen. The consequent rising costs and reduced availability of accommodation have discouraged mobility between areas. The number of people aged 25–34 moving home and starting a new job fell from 30,000 a year in 1997 to 18,000 in 2018 (Bell 2019)

A particular issue has been the decline in the mobility of young graduates. Those who graduate in regions outside London and the Southeast and remain there after graduation are more likely to be in non-graduate jobs and earning less than they could elsewhere. This implies that they are less productive than they could be if freer to move in search of better jobs.

Informal pressures

Since the financial crash, Labour and Conservative governments have also exerted pressure to alter labour market outcomes through changing reporting requirements for organisations in both the public and private sectors. An example is high-end pay. In the public sector there is a threshold of £174,000 pa, beyond which any pay level must be approved by the Chief Secretary to the Treasury.

In the private sector, large quoted companies have since 2019 been required to disclose the ratio between CEO pay and UK employee pay, and to explain changes and how they relate to company pay policy. This is justified as increasing transparency, as a service to shareholders, but it is also a way of putting pressure on companies to control top pay. Similar pressure is applied to the higher education sector, where Office for Students' 'guidance' requires the publication of vice-chancellor remuneration and enjoins justification for high levels of pay in terms of 'value' for money.

Government agencies have also increasingly imposed Equality, Diversity and Inclusion (EDI) requirements on business. Under Financial Conduct Authority rules, for example, listed companies must report on board diversity against targets such as 40 per cent women on boards, at least one senior board position to be held by a woman and at least one board member from an ethnic minority. Failure to meet targets requires a published explanation and it is expected that companies will commit to remedying the deficiency. These targets are not motivated by productivity criteria, despite blather from politicians.

The rise of HR culture

The increase in the range and extent of employment regulation – and the concomitant penalties for non-compliance – has meant that organisations have had to put much more emphasis on ensuring that they don't fall foul of the law. Hence we have seen a proliferation of people whose jobs largely consist of ensuring that employees stick within rules which the government has imposed and otherwise add little directly to output of goods and services. We have seen this in the financial services sector, but a more relevant issue here is the expansion of employment in 'human resource' jobs. A widely disseminated estimate was produced by the Chartered Institute of Personnel and Development in 2020.[5] They calculated that 562,000 were employed in HR-related occupations in 2019, up from 438,000 in 2011 – an increase of 28 per cent in eight years. The numbers have probably risen further; an indicator is the membership of CIPD (the body for HR professionals), which has grown by 7 per cent since 2019.

While HR professionals may perform useful work, their increasing significance within organisations may have led to compliance which goes beyond what was intended by legislators. There may be a culture of risk minimisation which in effect 'gold-plates' government regulation, with, for instance, extensive compulsory training on unconscious bias for all staff, changes to recruitment and elaborate promotion procedures which minimise (though they can never completely eliminate) the risk of contravening legislation on discrimination, equal pay or other employment issues. This is likely to raise costs beyond the levels anticipated in the impact assessments conducted when regulation was introduced.[6]

Impatience with the excesses of the HR function within businesses has frequently bubbled over into public discussion. An extreme example was the recent decision by Ryan Breslow, the young CEO of the US company Bolt, to dispense with his entire HR team – which in his view was 'creating problems that didn't exist' and that disappeared when he let them go (see Fore 2026). It is difficult to imagine a UK CEO daring to do anything similar here, with the vastly greater degree of regulation in our labour market, despite the temptation.

Gumming up the works: the impact of regulation

The increasing formal and informal restrictions on the operation of the labour market outlined in this briefing have the effect of gumming up the works: delaying adjustment by businesses to changing economic opportunities and slowing down the rate of productivity improvement.

Wages

Take wages. The wage rate, like other prices, acts as a signal. To employers, it indicates how much it costs to employ a particular type of worker. When it goes up

[5] 5 Employment in HR soars over past decade, 6 July 2020, CIPD (https://www.cipd.org/uk/views-and-insights/thought-leadership/cipd-voice/employment-hr-soars-past-decade/).

[6] For example, the 2024 impact assessment for making the right to request flexible work a default estimated its cost per application at just over £30 – the cost of half an hour's time for an HR manager to process the claim. This ignores, for instance, the cost of the time for consulting all relevant parties and the costs of rearranging work schedules (including those for other employees who might be affected). See Shackleton and Lesh (2024).

sharply, it encourages the search for alternatives: different ways of employing workers (think use of temporary workers, zero hours contracts, outsourcing or transfer of production abroad) or substitution of machines and AI for employees. To potential workers: a sharp rise in the wage in a particular sector or area encourages an increase in applicants, geographical or occupational mobility, retraining for new skill demands.

Yet wages are becoming a less effective signal as government intervention increases. An obvious case is the national minimum/living wage. Big increases in the wage floor – with the NLW now linked arbitrarily and indefinitely to two-thirds of median hourly mean earnings – mean that by April 2025 2.02 million – 6.6 per cent of all payrolled employees – were paid at the relevant minimum wage rate (Low Pay Commission 2025). In addition, many employers deliberately set pay at a little more than the minimum; the major supermarkets (e.g. Tesco, Sainsbury's, Asda, Lidl) pay between 30p and 50p per hour more than the law requires.[7] Altogether in 2024 2.3 million (7.6 per cent of employees) were paid up to 50p more, with a total of 6.07 million (19.9 per cent) paid up to £1 more. Most of these employers will semi-automatically raise their pay rate in line with changes in the minimum wage. So in effect the government sets pay for up to 1 in 5 of employees.

Having the same wage rate in many different sectors in many different parts of the country inevitably produces problems as it creates a mismatch between demand and supply. For instance in some parts of the country the NLW is very close to the median hourly wage rate. In Wigan, for example, the minimum wage is now over 80 per cent of the local median wage.[8] This upsets relativities and compresses wage distributions, making it more difficult to recruit first-line managers. Unemployment in these areas tends to be high, especially for young unskilled workers, but the wage (and other costs such as employer NICs and pension contributions) for entry level jobs in bars, catering and shops is too high to make it worthwhile employing people.

There are few low-paid workers in the public sector, however. There are just over 6 million public sector workers, most of whose pay is set directly or indirectly by the government. Around 2.8 million of these fall under Pay Review Bodies. In the public sector, unions are strong (with 50 per cent unionised, as against less than 12 per cent in the private sector).[9] Pay settlements rarely reflect the outcome of supply and demand in the conventional sense. And at the high end of public sector employment, all high salaries need to be personally approved by the Chief Secretary and will be constrained by the political optics rather than market forces. This is even more true of the remuneration of Parliamentarians. Political considerations dictate that the salaries

[7] This is partly to afford compliance problems, as there are many pernickety requirements for what counts as working time, for example, and partly for reputational reasons, to signify that they are 'good' employers.

[8] Uplift to minimum wage brings wage floor closer to typical earnings in Doncaster and Wigan (https://www.centreforcities.org/press/uplift-to-minimum-wage-brings-wage-floor-closer-to-typical-earnings-in-doncaster-and-wigan/).

[9] A high proportion of private sector unionists are in previously nationalised industries. As the train franchises – where unionisation is probably of the order of 60–70 per cent – are gradually being reabsorbed into the public sector, the proportions in each sector will change.

of MPs and ministers are much lower than their continental counterparts and mean that few people with established expertise, good career prospects and a family to support are willing to take the gamble on standing for the House of Commons. Hence the place is full of ex-SpAds and political obsessives.

Another way in which pay is determined outside market considerations is the increasing acceptance by employment tribunals and higher courts of reference to 'work of equal value' in equal pay claims. In the Asda and Next cases (Shackleton 2024), for example, the work done by largely female supermarket workers and largely male depot workers is held to be of equal value and therefore they should be paid the same. This is because the Equality Act 2010 says that equal value relates to the 'effort, skill and decision-making' associated with a job. This ignores the way in which a free market would also reflect other factors which help determine people's choice of jobs. If working in a cold, isolated warehouse or depot is less attractive than a warm, centrally located supermarket, the warehouse job needs to have what economists call a 'compensating differential' in higher pay or otherwise it will find it difficult to recruit workers while supermarkets will have queues for available jobs. More generally, the 'equal value' argument undermines attempts by employers to recruit shortage workers by raising pay. Where they attempt to do this, they are constrained by economically irrelevant imperatives to recruit a balanced mix of men and women, something which involves higher costs and itself may lead to discrimination claims.

This all inhibits productivity as wages determined by government fiat rather than market forces no longer put out a clear signal to employers and potential employees.

Adjustment processes

Even where wages are free to adjust and send out appropriate signals, government intervention in the labour market and other aspects of the economy may slow the process of adjustment to those signals.

From the employers' side, unfair dismissal law and TUPE[10] regulations act as an inhibitor to major changes such as large-scale redundancies and transfer of company ownership. In the period since the financial crisis tribunal judgements emphasising the need for formal processes and protection for a wider range of beliefs have increased the risks to an employer of dismissing a worker. The changing demographics of the workforce in the last twenty years – more women, more ethnic minorities – has meant that more unfair dismissal cases are also accompanied by discrimination claims, for which there has for many years been no upper limit to compensation.

The increasing risks associated with dismissing workers – where even clear cases of fair dismissal can be invalidated if the process is accidentally mishandled[11] – may

[10] Transfer of Undertakings (Protection of Employment) regulations protect the employment rights of employees when ownership of the part of the organisation they work for changes.

[11] A classic case involved a hotel chef who went berserk after a few drinks and attacked a policeman sent to the hotel to restrain him. The chef bit the officer and spat blood at him. He was jailed for 18 months and was dismissed from his job while in prison. But his employer had failed to follow the correct procedure and he received £11,000 compensation. Head chef sacked while in prison for biting police officer wins £11k payout (https://www.telegraph.co.uk/news/uknews/law-and-order/11707382/Head-chef-sacked-while-in-prison-for-biting-police-officer-wins-11k-payout.html).

mean that inadequate performance is tolerated too often. This problem is likely to get worse as the period before unfair dismissal legislation kicks in is reduced from two years to six months in the Employment Rights Act, as it reduces the window for assessing performance of new workers before job protection begins.

Perhaps more importantly, the legislation inhibits employers from dismissing workers in an economic downturn, motivating the 'labour hoarding' which some commentators have seen as a factor in low productivity levels in the UK. The contrast is drawn with the US, where a downturn sees proportionately many more being laid off. The evidence suggests, however, that recovery in employment is quicker in the US as employers are willing to take people on more quickly in an upturn – and are able to pick and choose who they take back. Labour is reallocated more rapidly, the duration of unemployment is typically shorter, and productivity tends to grow faster as the process of creative destruction is less inhibited than in the UK and other European economies (Caballero et al. 2013).[12]

On the side of employees, finding a new job on entering or re-entering the labour market has arguably been made more difficult as a result of trends since the financial crisis. The worsening housing shortage has made moving for work – geographical mobility – more difficult, while the growth in licensing has made entering intermediate level occupational mobility increasingly problematic too. Getting into jobs such as care manager, nursing associate or security manager is now significantly more difficult. Even where qualifications are not required by regulation, there has been a growth of 'credentialism': partly as a result of the excess supply of graduates, employers now require a degree qualification for a job which a few years ago was done quite adequately by people without degrees. People with experience and skills but with no formal qualifications find it difficult to find work except at the most basic level.

This all means that there is a growing mismatch in the labour market, with many workers operating at levels below their potential. Reduced mobility opportunities are reflected in fewer job moves (Brewer and Murphy 2023). Movement between jobs is the most effective way of raising wages at the individual level, and from the viewpoint of the economy as a whole such reallocation of labour raises productivity. That people are not moving as frequently is another sign of growing dysfunctionality in the labour market.

Mandates, uncertainty and the business of business

A final way in which government employment regulation creates problems for the effective functioning of the jobs market is the proliferation of mandates such as parental leave, 'reasonable adjustment' for the needs of people with disabilities, and the right to request flexible working. All thFree of these mandates introduce greater uncertainty into employment relations. Women on maternity leave do not have to give

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[12] However, authors such as Davis and Haltiwanger (2014) suggest that the US advantage in this respect fell after the 1990s as a result of reduced labour market flows, which were partly the result of increasing employment regulation and exceptions to the 'contract at will' which formerly dominated.

a clear indication of when they will return, which creates planning problems and costs when temporary cover is hired or existing colleagues are asked to ‘act up’. What constitutes a reasonable adjustment for disability is often difficult to discern, particularly when someone is presenting with one of an increasing range of mental health issues – and the costs of getting it wrong and ending up in a tribunal can be very significant. The consequences of flexible working arrangements, now hard to refuse, are difficult to discern in advance: the long-term effects on productivity of widespread working from home since Covid or the embryonic movement towards a four-day week cannot be known in advance, but may not all be positive. It is not surprising that defensive HR practices, which raise costs, are common.

The government pressure for diversity in hiring practices, or on companies to reduce pay gaps between the sexes (and soon, probably, ethnic pay gaps) also have potential to undermine performance if they lead to policies which elevate box-ticking over the bottom line. For example, the need to have some board members appointed on the basis of sex or ethnicity rather than simply skills and experience can present problems, and there is no guarantee that the diversity created will have a positive effect on performance.[13] And attempts to manipulate half-understood company pay gaps by altering recruitment practices or by restructuring to outsource low-paid female work could go badly wrong.

There is a more general case for saying that attempts to turn capitalist enterprises into vectors for social justice are unhelpful if we sincerely want to raise productivity and boost growth. The business of business is business, and greater emphasis on this truism might help us to ungum the labour market.

[13] Indeed, there is some evidence that ‘quotas for women on corporate boards have mainly decreased company performance’ (Yu and Madison 2021: 377).

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