Introduction

In the last 13 years, the application of Living Wage standards by UK companies has led to increased business performance, reduced staff turnover and enhanced corporate reputations whilst lifting over 60,000 families out of working poverty.¹

Since 2011, ShareAction has co-ordinated a collaborative investor initiative to encourage all FTSE 100 companies to apply Living Wage standards in their UK operations (The Investor Collaborative for the Living Wage). While only two of the FTSE 100 were Living Wage employers in 2011, today that figure stands at 18 fully accredited employers, and an additional 10 applying the Living Wage standard.

This briefing provides information on: the Living Wage standard, the impact for investors, benefits to businesses of being an accredited Living Wage employer, the macro-economic benefits arising from the application of Living Wage standards, and the opportunities to participate in the Investor Collaborative for the Living Wage.

The Living Wage

What is the Living Wage?
The Living Wage is the minimum hourly wage necessary to provide housing, food and other basic needs for an individual and their family. Living Wage rates are based on Minimum Income Standards (MIS) methodology and take account of real costs for essential goods and services. Within London, the Mayor’s Office announces the Living Wage figure each year – currently £9.15 per hour. Outside London, the Centre for Research in Social Policy at Loughborough University, which houses the MIS Team, has calculated a single rate for the rest of the UK which is £7.85 per hour.

Living Wage employers

Living Wage employers ensure all their own staff and those of on-site contractors working on their premises are paid at least the Living Wage across the UK. The Living Wage Foundation (independent of ShareAction) provides technical support and advice on implementation of Living Wage standards and administers the accreditation scheme for compliant employers.¹

Since the launch of the Living Wage Foundation in 2011, momentum has been rapidly building for the Living Wage. Over 1000 employers in the public, private and

¹ Accreditation fees are charged on a sliding scale. The highest fee is £1000 per annum.
voluntary sectors have become accredited Living Wage employers. The earliest Living Wage accreditations were London-based employers in professional and financial services. However, Living Wage standards are increasingly becoming a norm for socially sustainable business behaviour and today are applied across the UK in a wide range of sectors and even in such household names as Nestlé and ITV. We anticipate further high profile accreditations in the coming year.

The Living Wage also has widespread public support from across the political spectrum. Prime Minister David Cameron has said: “Where companies can afford to pay the Living Wage, I think they should.” Mark Carney, Governor of the Bank of England, also spoke to its importance: “Employment does much more than provide the means to support workers and their families; it is essential to personal fulfilment and human dignity. Part of that dignity is being paid a Living Wage.”

ShareAction’s initiative began when only two of the FTSE 100 were accredited Living Wage employers. Through investor engagement and dialogue with the Living Wage Foundation, 18 of the FTSE 100 are now accredited as Living Wage employers; while another 10 state that they apply the standards but have not accredited. More than half of FTSE 100 firms are now in dialogue with investors on the issue. The case for investor engagement as explored in the next section is based upon a combination of corporate risk management, business benefits, commitment to corporate citizenship, and wider societal and economic benefits.

**The investment case for Living Wages**

Adopting the Living Wage impacts a range of company stakeholders, from investors to managers, employees and consumers.

**The investor impact**

The increase in momentum for the Living Wage is arguably connected with growing concerns over income inequality by citizens, the media and policy-makers. In particular, the disparity in earnings between top executives and low-paid employees has been increasingly making headlines. The Living Wage serves as a tool to mitigate the associated reputational risk. Proactive management of this risk is being welcomed by many shareholders, particularly those investors that have managed their own risk exposure to the same concerns by becoming a Living Wage employer. As one SRI Fund Manager stated: “Failing to provide a decent living wage and safe working conditions is unacceptable for any company in any sector. Consumers understand this. There exists a clear financial opportunity for companies that take a lead, and considerable risks for those who do not.”

Moreover, the up-front cost of this mutually beneficial risk management can be seen to be relatively modest in comparison with the potential risk of pay related reputational damage, particularly for consumer-facing businesses. ShareAction has undertaken analysis of the implications for corporate earnings of introducing Living Wage standards for three FTSE 100 firms in different sectors (see Appendix 1). We show that introducing the Living Wage, even for a major retailer, results in single digit net earnings reduction (i.e. between 1-6% of corporate earnings for the sample companies selected).

**Business Benefits**

Beyond the role of the Living Wage as a risk management tool, adopting the standard has been found to create benefits at all levels of company operations. Overall, 80% of employers surveyed in a GLA Economics survey of Living Wage employers believed that the Living Wage had enhanced the quality of work performed by staff. In the survey, all employers reported that they would, if faced with the same choice today, implement the London Living Wage.
Employers that have implemented the Living Wage standard report benefits particularly in:

- employee retention and turnover,
- reduced absenteeism and improved morale,
- increased productivity.

**Turnover and retention**

In regards to turnover and retention, the GLA Economics survey of 11 accredited employers found a positive impact on recruitment and retention of staff for all but one employer consulted. Two-thirds reported that the Living Wage had a significant impact on reducing staff turnover. KPMG for example found that “turnover has more than halved” for contracted staff. Wendy Cuthbert, head of UK corporate real estate services for Barclays Group, reported that catering staff retention rates increased from 54% to 77% following an introduction of the Living Wage and cleaning staff retention rates jumped from 35% to 92%.

For service-providing or consumer-facing businesses, as well as reducing the costs of recruitment and training, a lower turnover helps ensure customers are satisfied and return. Kevin Prince, the general manager at Space Station Group self-storage centres reported that: “Every time we lose a member of staff it costs us around £20,000 in lost business.” Space Station pays above the Living Wage because, “if you have to spend evenings short staffed because people come and go and you can’t recruit good quality, and people use your service just once and then never come back, then suddenly that [extra] pound an hour seems very cheap business.”

**Absenteeism and morale**

Similarly, the Living Wage has been shown to reduce absenteeism and improve morale in the workplace. A Jane Wills and Brian Linneker study from Queen Mary University concluded that the Living Wage leads to reduced “sickness” in Living Wage workplaces. One employer surveyed by GLA Economics reported that following the introduction of the Living Wage for workers employed through contractors, absenteeism fell by as much as 25%.

On the related issue of employee engagement, the High Pay Commission reported that: “Within companies pay inequality matters too. It has an impact on employee engagement. When employees feel they aren’t getting their fair share or see unjust rewards for those at the top they are less likely to feel engaged with the company, and businesses are increasingly recognising this.”

The 2013 study, ‘Investigating the effect of the London Living Wage on the psychological wellbeing of low-wage service sector employees: A feasibility study’, showed that 50.3% of Living Wage employees had above average wellbeing compared with 33.9% of non-Living Wage employees. In the Wills and Linneker survey of staff who were working at a company when it transitioned to the Living Wage, the most common impact reported was that “People are happier about the work.” GLA Economics similarly found that the Living Wage “significantly boosted worker morale and motivation.”

**Productivity**

The productivity benefits of implementing the Living Wage are particularly pronounced for companies that accompany higher wages with greater investment in staff skills and operations management. For example, Zeynep Ton, of the MIT Sloan School of Management, documented the advantages for large retailers which have moved away from the typical retail sector model of low pay and low levels of training. She found that companies which invest in employees as an asset rather than focusing solely on minimising the cost of wages, realise benefits to labour productivity, customer service, cost-cutting, innovation, and flexibility.

The big difference was the impact on morale across all employees... it just made everybody feel good about working for a company that had taken the time to address the issues of the Living Wage.

- Elaine MacLean,
  Group HR Director at Legal & General

The big difference was the impact on morale across all employees... it just made everybody feel good about working for a company that had taken the time to address the issues of the Living Wage.
improvement that the UK Living Wage brings in operations flexibility is confirmed in key surveys of employees impacted.\textsuperscript{8}

Zeynep Ton describes the benefits: “Highly successful retail chains … not only invest heavily in store employees but also have the lowest prices in their industries, solid financial performance, and better customer service than their competitors. They have demonstrated that, even in the lowest-price segment of retail, bad jobs are not a cost-driven necessity but a choice. And they have proven that the key to breaking the trade-off is a combination of investment in the workforce and operational practices that benefit employees, customers, and the company."\textsuperscript{20}

**Corporate Citizenship in action**

Being an accredited Living Wage employer is fast becoming an established mark of commitment to corporate social responsibility, bringing powerful reputational benefits. For the first time, the number of households experiencing in-work poverty now outstrips the number of workless households in poverty.\textsuperscript{22} As of October 2013, 5.24 million were paid below the Living Wage in the UK, more than a fifth of the UK’s workforce.\textsuperscript{23} Women and young people are disproportionally represented in this group. With a growing public debate over the cost of living, companies which publicly become Living Wage employers can improve their relationships with consumers and attract higher quality candidates for recruitment. As one PR company, Bray Leino, wrote: “For those companies that pay it (The Living Wage), there is a great story to tell. It’s a very human and emotive subject, and appealing to the media."\textsuperscript{24}

Of the Living Wage employers surveyed by GLA Economics, 70% reported increased consumer awareness of their organisation’s commitment to being an ethical employer.\textsuperscript{25} Moreover, a recent survey of more than 1,000 consumers by KPMG found four out of ten said they would not hesitate to shop elsewhere if their preferred store did not pay the Living Wage.\textsuperscript{26} 52% of those surveyed even stated that they were willing to pay higher prices if the money goes directly into employees’ pockets.\textsuperscript{27}

The reputational benefits, in addition to the higher wages offered, contribute to attracting higher quality candidates for positions. For example, the decision of Gap to increase hourly wages in the US is reported to have grown the number of applications by at least 10% overall and more so in some stores.\textsuperscript{28} Gap’s CEO and Chairman Glenn Murphy explained the decision: “Our instincts are that … this is a race for talent … And if we have the best talent in our office, in our distribution centres, in our call centres and mostly in our stores, then we’re going to win. And we’ve got evidence already … Applications to Old Navy since our announcement are up 20 percent.”\textsuperscript{29} Sandy Begbie, Group Operations Officer of Standard Life, similarly reported that: “Being a UK Living Wage employer has supported us in attracting high quality candidates who want to stay and we are also seeing a positive impact on our employee engagement and the overall quality of the work we do.”\textsuperscript{30}

By collaborating as shareholders to call for the UK’s largest listed companies to apply the Living Wage standard, institutional investors are making clear that application of such standards is an important practical demonstration of the corporate citizenship values espoused by most FTSE100 companies.
Economic Growth
The remuneration practices of employers impact the wider UK economy by determining consumer spending power. Paying Living Wages stimulates the economy by adding materially to consumer spending power and confidence at a time when this is a particularly vital determinant of business success and profitability. Investors with a well-diversified portfolio of UK stocks therefore have an interest in promoting the payment of Living Wages.

It is argued that increasing wages for those with low spending power stimulates the economy more than stimuli at other income levels because consumers on low wages spend the vast majority of their income immediately. Moreover, this spending tends to support the local economy. A US study showed that low-paid Chicago workers spent their entire minimum wage increases in the local economy while a 2005 study by Staffordshire Business School showed that for every extra £1 per hour paid to low paid workers in Stoke on Trent, the local economy benefitted by an additional £0.63 of income creation. This multiplier of £1.63 found in Stoke on Trent is consistent with studies in other regions of the UK.

Perceived Barriers
The cost of implementation
Assuming a 38-hour week and the national Living Wage rate of £7.85 per hour, moving a full time worker from National Minimum Wage (£6.50) to the Living Wage is approximately £2,400 a year in additional wages. Where workers earn more than £6.50, the cost is lower. Companies which outsource cleaning, catering and other facilities services must require their contractors to pay at least the Living Wage to qualify for accreditation. Where low-paying services are outsourced, the cost of introducing Living Wages is often shared between contractor and client. The research cited above by GLA Economics has shown that implementation costs can be offset by a range of cost-saving strategies.

Employment Effect
The Living Wage is a voluntary commitment made by employers who choose to make it a priority and can afford it. This mitigates against the risk of negative employment effects. As stated above, the payment of Living Wages helps to increase spending power in the economy, which also boosts job growth.

Modelling by the Resolution Foundation has shown that even in a scenario in which all private sector employers in the UK were forced to pay the Living Wage, the impact of the Living Wage on employment would then be less than 4% of the four million employees in the private sector that would benefit from the pay rise. They state that this figure represents a worst case scenario for employment and it does not take into account the beneficial macro-economic impacts nor the business benefits earlier discussed. The Resolution Foundation notes that this same predictive model would have foreseen that the introduction of the national minimum wage led to the loss of 22,000 jobs, but in fact Low Pay Commission research suggests that there were no job losses associated with the introduction of the NMW.

Contractor relations
For most of the FTSE 100, the great majority of direct employees are paid above the Living Wage rates. It remains the case, however, that staff employed by contractors on a non-Living Wage employer’s UK premises, such as cleaners, security guards, and catering staff, are likely to be paid below Living Wage rates.

Some listed companies have raised concern over their capacity to ensure Living

---

iii | In this calculation, we assume a workforce on the adult minimum wage of £6.50 per hour, annual hours of 1976, incremental NIC of £368 and a corporate tax rate of 21%.
Wages for staff employed through contractors, given the indirect employment relationship. Though certainly implementation for contracted staff requires an extra step of contract renegotiation, the Living Wage Foundation provides considerable support in the practicalities of this. The 1000 accredited Living Wage employers which have extended the standard to their contracted staff illustrate that this is clearly possible and any complications are surmountable.

Moreover, the impact of implementing the Living Wage standard for on-site contracted staff has been shown to stimulate benefits across all levels of company operations. In the case of cleaning staff in particular, a 2014 report by the Equality and Human Rights Commission cites that cleaning firms consulted on the impacts of the Living Wage reported that they benefited from reduced absenteeism and staff turnover. They add that, “Some firms reported that since paying the Living Wage their turnover has reduced to less than 1 per cent. This has a positive impact for clients, who also reported that payment of the Living Wage has led to an improved service, with higher productivity rates.”

The Investor Collaborative for the Living Wage
The Investor Collaborative for the Living Wage is a group of institutional investors who encourage UK-listed companies to adopt the Living Wage standard across their UK operations. Since the launch of this ShareAction-led initiative in May 2011, strong progress has been made. Investors in the collaborative receive from ShareAction regular updates on engagement taking place with firms on the Living Wage as well as details on new accreditations and notable developments towards implementations of the standards. We would be pleased to provide interested investors with these progress reports on FTSE100 companies.

In 2014, ShareAction has coordinated investors to write jointly signed letters to the CEOs and other top executives of the FTSE 100 about the Living Wage in advance of their Annual General Meetings. Coupled with questions at 44 of these Annual General Meetings on the topic of the Living Wage, this initiative sparked engagement with more than 50% of FTSE 100 on the issue and substantive progress in dialogue and implementation of the standards.

The goal of the Collaborative is to have 75% of FTSE 100 firms become accredited Living Wage employers by 2020.

For investors interested in supporting or knowing more about this Living Wage collaborative initiative, we would be pleased to discuss this further.

Contact
Catherine Howarth
Chief Executive
ShareAction
Catherine.howarth@shareaction.org
0207 403 7827

Lisa Nathan
Research and Engagement Officer
ShareAction
Lisa.nathan@shareaction.org
0207 183 4184

About ShareAction
ShareAction (Fairshare Educational Foundation) is a registered charity that promotes responsible investment practices by pension providers and fund managers. ShareAction believes that responsible investment helps to safeguard investments as well as securing environmental and social benefits.

Disclaimer
ShareAction is not an investment advisor, and does not make any representation regarding the advisability of investing in any particular company or investment fund or vehicle. A decision to invest in any such investment fund or entity should not be made in reliance on any of the statements set forth in the investor briefing. While the organisation has obtained information believed to be reliable, it shall not be liable for any claims or losses of any nature in connection with information contained in such document, including but not limited to, lost profits or punitive or consequential damages.

The opinions expressed in this publication are based on the documents specified in the end notes. We encourage readers to read those documents. Online links accessed 2 November 2014. Fairshare Educational Foundation is a company limited by guarantee registered in England and Wales number 05013662 (registered address 16 Crucifix Lane, London, SE1 3JW) and a registered charity number 1117244.
Appendix 1
To illustrate the modest costs of the Living Wage as a corporate risk management tool, we analysed the impact on corporate earnings and earnings per share of becoming a Living Wage employer for three FTSE 100 companies in different sectors: service, industrial, and retail. We selected companies that were mainstream players in their sectors.

We looked at the impact of moving all staff onto the Living Wage on the three companies’ earnings by working on a set of deliberately conservative assumptions detailed below in table 1.

Table 1:
Our assumptions are as follows:
Hours Per Week: 37.5 for the service and industrial companies, and 36.5 for the retailers
NMW: £6.50/h for all employees
NLW: £7.85/h
Pension contribution: 3% of salary, despite full phase-in requirement only in 10/2018
Employer NIC: 13.8% on Salary & Pension, despite the actual rate being paid is lower
Corporate Tax Rate: Actual applied tax rate rather than prescribed 23%
Outputs: Both in tabular and graph formats are anonymised.
Other assumptions: Number of staff with salaries below Living Wage rates and/or on NMW rates.

As one would expect, the lowest corporate earnings impact from moving the relevant portion of employees up to the national Living Wage rate is experienced by the industrial company in our sample of three. Here we see earnings per share reduce by just 1.2%, with the sales-driven service company coming a close second (earnings per share loss of 2.5%). The big retailer sees the highest impact, but earnings per share are compressed by a still modest 7.4%.

In risk management terms, the higher earnings impact for the retail company is arguably offset by the greater exposure of this recognisable high-street brand to both the risk of negative headlines and the disproportionate business impact should that risk occur. Thus, for both management and shareholders, there would seem to be a shared interest in bearing the moderate costs of addressing this issue head on.

The chart below sets out current earnings per share of each firm as well as the Living Wage-adjusted earnings per share. Further analysis, including on P/E multiples is provided in table 2 below.

<table>
<thead>
<tr>
<th>Adjusted Anonymised Outputs</th>
<th>Services Co</th>
<th>Industrial Co</th>
<th>Retail Co</th>
</tr>
</thead>
<tbody>
<tr>
<td>Share Price</td>
<td>1202p</td>
<td>2055p</td>
<td>2256p</td>
</tr>
<tr>
<td>Current EPS</td>
<td>93.25p</td>
<td>131.01p</td>
<td>126.66p</td>
</tr>
<tr>
<td>Adjusted Current EPS</td>
<td>90.92p</td>
<td>129.46p</td>
<td>117.33p</td>
</tr>
<tr>
<td>EPS Difference</td>
<td>-2.5%</td>
<td>-1.2%</td>
<td>-7.4%</td>
</tr>
<tr>
<td>Current P/E</td>
<td>9.02x</td>
<td>10.98x</td>
<td>6.23x</td>
</tr>
<tr>
<td>Adjusted Current P/E</td>
<td>9.25x</td>
<td>11.11x</td>
<td>6.73x</td>
</tr>
<tr>
<td>Required P/E Expansion</td>
<td>2.6%</td>
<td>1.2%</td>
<td>7.9%</td>
</tr>
</tbody>
</table>
Endnotes
6 | Ibid.
7 | Ibid.
8 | Ibid.
18 | Citizens UK. Living Wage Week 2013.