Resolution Foundation

The Resolution Foundation Labour Market Outlook

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In this Labour Market Outlook, we examine how the Government should approach extending Statutory Sick Pay (SSP) to the lowest earners, and in particular what replacement rate – the proportion of their earnings that workers will get while off sick – to set for those workers who will be newly eligible.

There is a clear case for strengthening the UK's SSP system, but the Government faces the challenge of balancing income protection with the risk of absenteeism. A replacement rate of less than 100 per cent is appropriate to mitigate the latter risk – especially given that 'waiting days' are also being removed, meaning that workers can access SSP from the first day off sick. But we argue that the Government should err on the side of protecting incomes: those workers who will be newly eligible for SSP are disproportionately low-income, with almost a third (32 per cent) in poverty compared to one-in-ten (9 per cent) of other employees. For this reason, we propose a replacement rate of 80 per cent for these newly eligible workers, consistent with the recommendations of a previous government consultation, as well as the Coronavirus Job Retention Scheme.

The 'Lifting the Lid' section looks at the differences between Labour Force Survey estimates in Great Britain and Northern Ireland (where the survey is administered differently), wage growth for graduates relative to the minimum wage, and the extent to which the Government's industrial strategy will target areas most in need of a pay uplift.

Spotlight | Reforming the UK's Statutory Sick Pay system

The Government introduced the Employment Rights Bill in October 2024 as part of its 'Plan to Make Work Pay' – arguably the biggest overhaul to employment rights since the introduction of the minimum wage. But the Bill marks only the first step on a long road to reform. There are lots of policy details to be worked out, and the Government is (rightly) consulting on some of the key decisions.

One of the areas being consulted on is the strengthening of the UK's Statutory Sick Pay (SSP) system. There is a clear case for doing so: the UK's system currently provides a lower level of minimum protection to sick workers than most other OECD countries. This is because sickness absences shorter than four days are not covered, the lowest earners are excluded and the current SSP rate of £116.75 per week is simply too low. The Government's planned reforms will address the first two of these (although not the third), and the recent consultation focused specifically on extending SSP eligibility to workers earning less than £123 per week, who currently do not qualify. For these workers, the Government plans to set SSP as a share of earnings but is consulting on what the exact replacement rate should be. In this spotlight, we outline the key considerations and the reasons why we propose that the Government adopts an earnings replacement rate of 80 per cent for newly eligible workers.[1]

1 This Spotlight is an extended version of the Resolution Foundation's response to the Making Work Pay: Strengthening Statutory Sick Pay consultation.

Policy makers need to balance income support with a risk of absenteeism

This decision matters because the workers affected will, by and large, be eligible for sick pay coverage for the first time. As well as being excluded from SSP by virtue of the policy design, very few will currently have coverage via their employer: a 2014 survey found that part-time workers (a category which includes all those earning below £123 a week) were less likely than full-time workers to have access to occupational sick pay (42 per cent versus 61 per cent).

The main policy consideration is a 'moral hazard' trade-off. Set sick pay too low, and workers who are too unwell to work face an unacceptably large financial hit – and if those workers work through illness to avoid this hit, there are negative health consequences for the individual and wider society. But set sick pay too high, and there is the risk that some workers take false sick days. This is why most countries' sick pay systems either set mandatory sickness payments at a level below workers' normal earnings or include 'waiting days' (days' illness where there is no eligibility for sick pay).

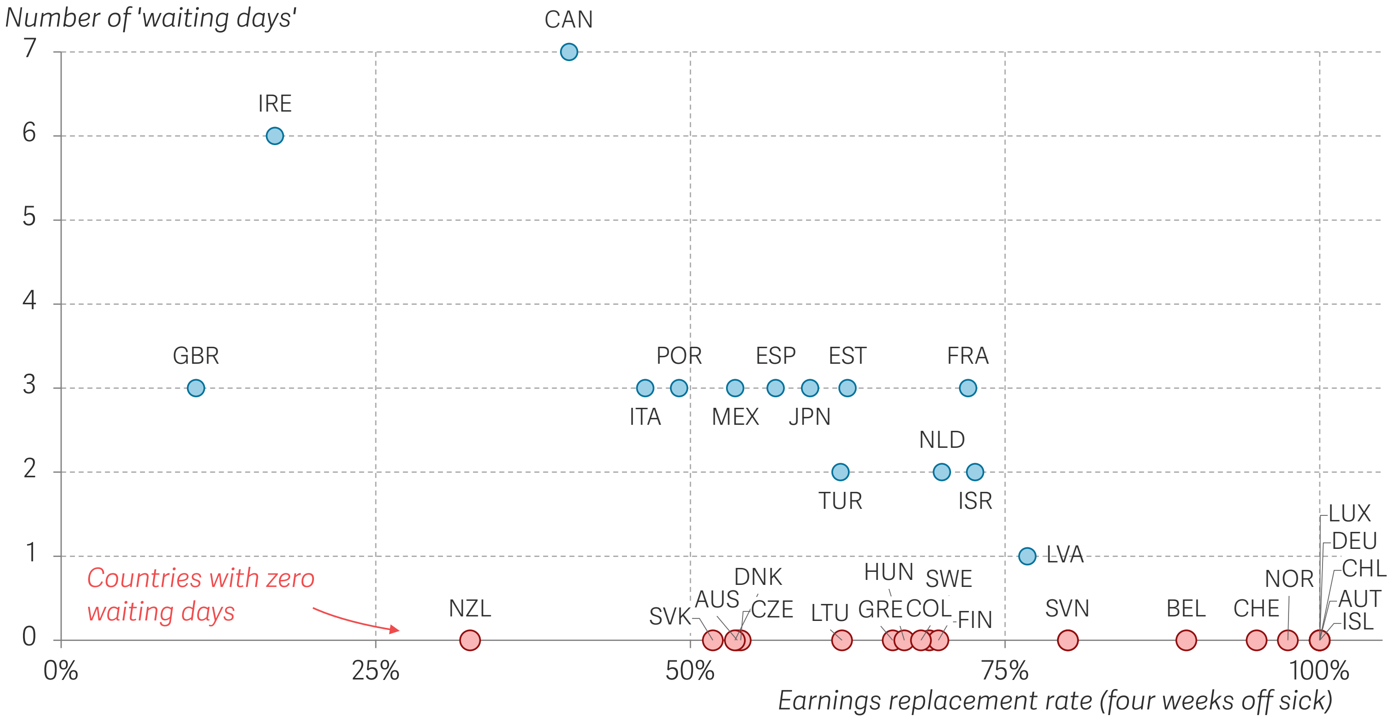
The UK's current system has both features – a three-day 'waiting period' as well as a very low rate of earnings replacement for the average worker covered. (Since SSP is a flat rate, however, the earnings replacement is high for those workers just eligible.) But waiting days are set to be removed – and so balancing sickness insurance and absenteeism risks will come down entirely to the choice of earnings replacement rate. This means it is appropriate, in our view, to set an earnings replacement rate below 100 per cent.

As Figure 1 shows, this would be in line with the practice in many other rich countries.[2] A handful of countries (including Luxembourg, Germany, Chile, Austria and Iceland) do provide full earnings replacement from the first day of sickness, but this is fairly unusual, and often accompanied by more stringent requirements to certify illness through the healthcare system. Among countries whose sick pay system does not have any waiting days, the typical earnings replacement rate (in Finland) is 70 per cent.

2 A version of Figure 1 first appeared in: N Cominetti, Low Pay Britain 2024: Examining the Government's proposed employment reforms, Resolution Foundation, September 2024.

FIGURE 1: **Most countries without waiting days have sick pay replacement rates below 100 per cent**

Earnings replacement rate (horizontal axis) and number of 'waiting days' before payments start (vertical axis) in countries' sick pay systems: OECD countries, 2019



NOTES: Earnings replacement relates to four weeks' absence for a worker on average private sector pay. Includes mandatory payments. 'Waiting days' are the initial number of days of a sickness absence during which the worker is not entitled to statutory sick pay.
SOURCE: OECD, Disability, Work and Inclusion in Korea, May 2023.

The cost to employers is also a relevant policy consideration – but one the Government should address separately

On top of this moral hazard problem, there is a second trade-off: both raising sick pay and expanding coverage raise costs for employers. This is both because a greater share of sick days would become eligible for SSP, and because workers would almost certainly take more sick days: cross-country evidence shows that workers take more sick days in countries with more generous sick pay provisions. Of course, more sick days are not universally harmful for businesses, to the extent that they reduce unproductive presenteeism and the spread of illness. But nonetheless, just as concerns exist about the employment effects of the costs imposed on businesses by the minimum wage, higher sick pay costs could also pose risks of job losses.

Our view, however, is that this trade-off should be handled separately from decisions about the replacement rate for low earners. The policy levers are different: the Government could, for example, compensate employers facing high sick pay costs, as it has done in the past.[3] Moreover, the proposed reforms look set to have a relatively low impact on businesses as a share of their wage bills: taken together, extending eligibility and removing waiting days are estimated to increase employers' sick pay costs from 0.06 per cent of their wage bills to 0.09 per cent.

3 Until 2014, the Government reimbursed employers facing high SSP costs as a proportion of their wage bill, and during the Covid-19 pandemic the Government temporarily re-introduced reimbursements for small and medium-sized businesses.

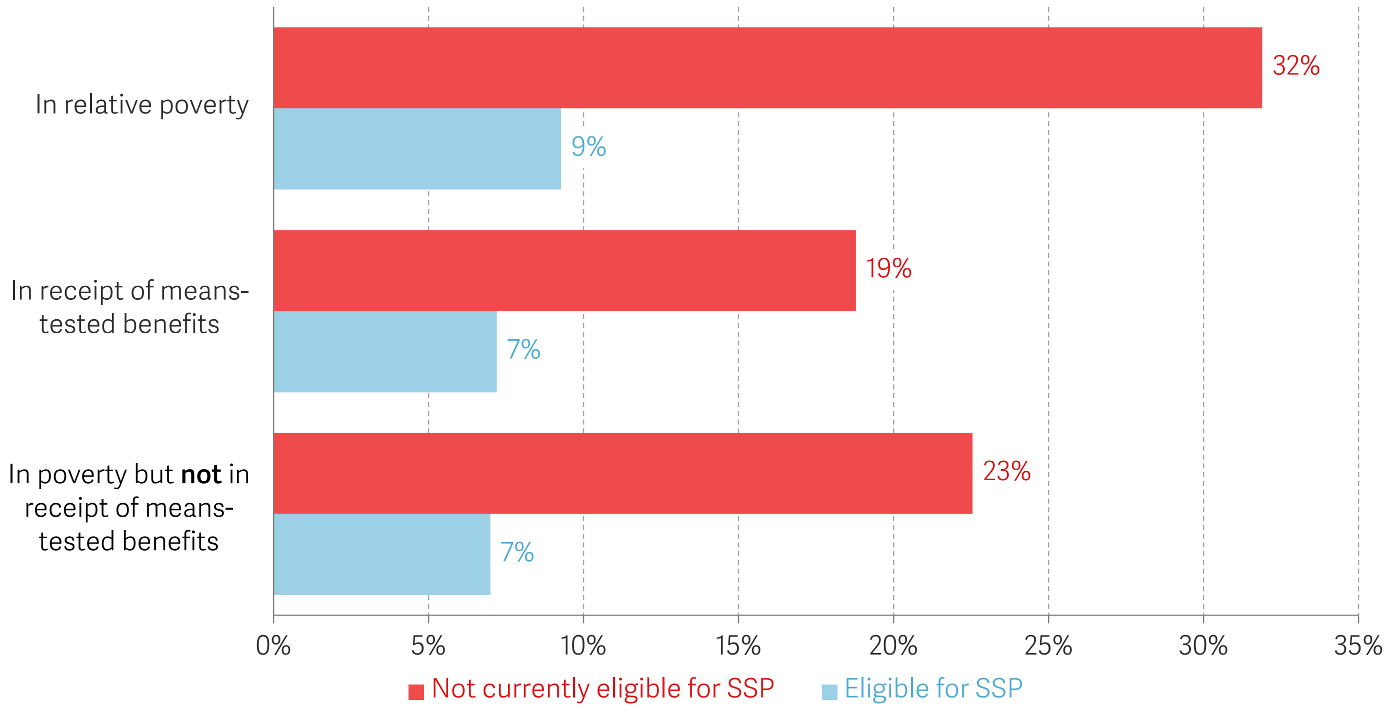
Given that the policy change would affect people on low incomes, there a stronger case for income protection

So, how should the Government weigh up balancing insurance against work incentives for workers newly eligible for SSP?

The first requirement of a sick pay scheme is that it protects workers' incomes when sick – and given that the proposed policy change affects those on the lowest earnings, who often have precarious financial situations, there is a strong case for ensuring SSP provides a good level of income protection to the lowest earners. Workers earning below £123 per week (who will be newly eligible for SSP) are disproportionately likely to live in lower-income households: as Figure 2 shows, one-third (32 per cent) of employees earning below this level are living in relative poverty compared to 9 per cent who earn above this threshold.

FIGURE 2: **Employees who earn too little to get SSP are three times more likely to be in poverty than other employees – and a quarter are both in poverty and do not receive means-tested benefits**

Proportion of employees who are in relative poverty, in receipt of means-tested benefits and in poverty but not in receipt of means-tested benefits, by whether eligible for Statutory Sick Pay (SSP): UK, 2022-23



NOTES: For employees with multiple jobs, SSP eligibility refers to whether someone is eligible for SSP in any of their jobs. Poverty is defined as having a household equivalised income below 60 per cent of median household after housing cost income.
SOURCE: RF analysis of DWP, Family Resources Survey.

The social security system will help to mitigate the financial impacts for some (albeit with a month's delay), but nearly a quarter (23 per cent) of employees who will be newly eligible for SSP are living in poverty but do not receive UC or equivalent.[4] Those workers and their families are likely to be among

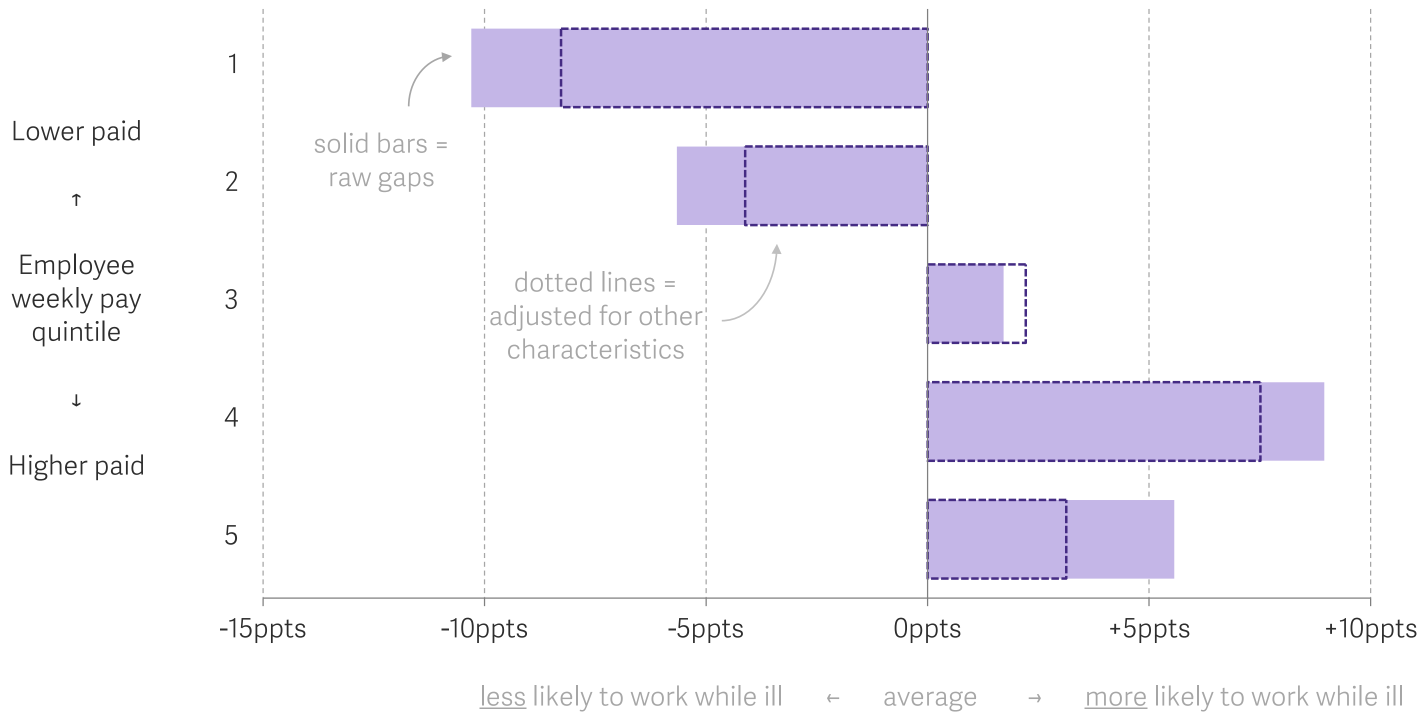
4 Source: RF analysis of DWP, Family Resources Survey.

the least able to weather the financial hit of uncompensated time off sick, pointing towards adopting a high earnings replacement rate. Moreover, as the Covid-19 pandemic demonstrated, those in lower-paying jobs are more exposed to health risks at work, so the health benefits of enabling people to stay home when sick might be greatest for this group of workers.

However, there are reasons to believe that the absenteeism risks of generous sick pay support might be higher for the lowest earners than for higher-paid workers. As Figure 3 shows, low earners are less likely to work through sickness than higher earners – even though their sick pay arrangements tend to be weaker – and one possible reason for this could be a greater willingness to take time off work.[5] In 2017, 52 per cent of the lowest-paid fifth of workers reported having worked while sick in the previous 12 months, compared to 68 per cent of the highest-paid fifth – and note that this data comes from before technological developments that meant office jobs could be easily done from home.[6]

FIGURE 3: **Lower earners are less likely to work through sickness than higher-paid workers, even after accounting for the different jobs they do**

Difference with the average proportion of employees who report working while sick in the past 12 months, by employee weekly pay quintile: UK, 2017



NOTES: Dotted lines adjust for age, sex, and respondents' reported importance in their job of dealing with people; counselling, advising or caring for customers or clients; physical stamina; and physical strength.
SOURCE: RF analysis of UK Skills and Employment Survey.

This differential could also reflect that low-paying jobs in sectors like care, hospitality and retail are often harder to do while under the weather than higher-paying jobs – but even after adjusting for job characteristics that may make it harder to work while sick, such as the importance of physical stamina or dealing with other people, the pay gradient in who does so remains (the dashed lines in Figure 3).[7] If

5 Another reason for low earners' sick pay arrangements being weaker (on top of the lowest earners not being eligible for SSP) is that they are less likely to have access to occupational sick pay schemes than higher-paid workers.
6 Source: RF analysis of UK Skills and Employment Survey 2017.
7 Source: RF analysis of UK Skills and Employment Survey 2017. Based on a regression of whether individuals have worked while sick (conditional on having been sick in the past 12 months) on age, sex, and reported importance of dealing with people, caring for

it is the case that the 'moral hazard' risk is higher among lower-paid workers, this would point towards adopting a lower rate of earnings replacement, especially given there is no longer any absenteeism disincentive via waiting days, which are being removed.

The Government should err on the side of protecting incomes and choose a replacement rate of 80 per cent

But even if the risk of absenteeism is higher among low-paid workers, our view is that the Government should prioritise protecting incomes.8 The planned policy change would specifically target low-earning – and often low-income – workers, who might be expected to be vulnerable to absolute, rather than simply proportional, earnings losses. These reasons, in our view, would justify an earnings replacement rate of 80 per cent.9 As the Government noted in its consultation, this would be consistent with the proposal in the 2019 Health is Everyone's Business consultation. And an 80 per cent earnings replacement rate also has precedent in the form of the Coronavirus Job Retention Scheme. (As with the minimum wage, the impact of the policy should be monitored and recalibrated if necessary – and this will require the Government to collect better data on the use of SSP.)

Finally, while extending SSP to the lowest earners and removing the waiting days are positive steps, broader reform is needed. At just £116.75 a week, the current level of SSP leaves many workers facing significant financial strain when they fall ill – particularly low-paid workers, as higher earners are far more likely to benefit from occupational sick pay schemes. The Government should therefore complete its SSP reforms by raising the overall level of SSP to ensure adequate support for all workers.

others, physical strength and physical stamina in the respondent's job (on a five-point scale from 'essential' to 'not at all important/does not apply').

8 Arguably, absenteeism among low-paid workers in low-income households could be more sensitive to a small cut in the replacement rate below 100 per cent, mitigating this risk somewhat. In addition, we note that under the current system, the replacement rate is higher than 80 per cent for workers who earn just enough to qualify, because it is a flat rate (excluding the effect of waiting days). For example, someone who just meets the earning threshold of £123 a week and receives SSP of £116.75 would have a replacement rate of 95 per cent once waiting days are removed.

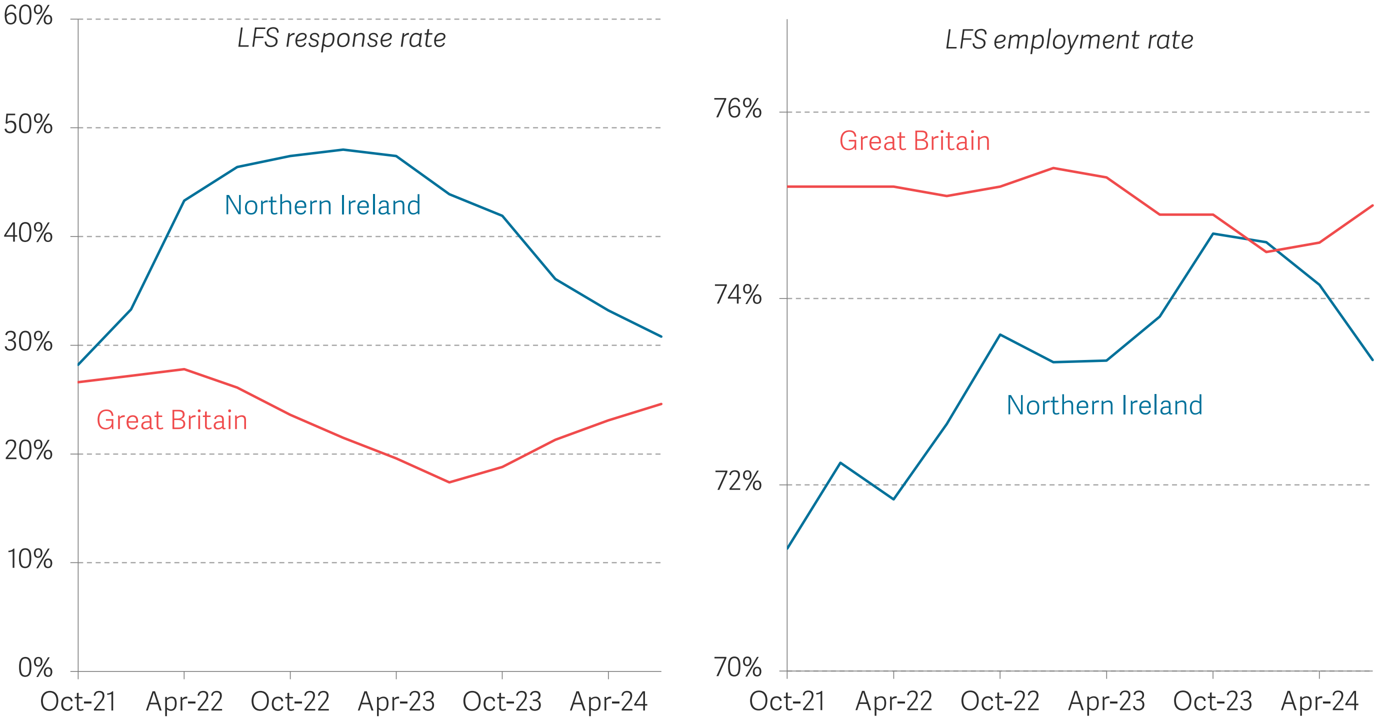
9 Under the terms of the Government's consultation, this would also be capped at £116.75 per week.

Lifting the lid | The picture across different groups and areas

Here we explore a few of the most interesting labour market developments for different groups of workers and different parts of the country.

FIGURE 4: **Response rates to the Northern Irish Labour Force Survey held up during 2022 and 2023 relative to those in Great Britain – and trends in the employment rate were more consistent with administrative data over that period**

Labour Force Survey (LFS) response rates (left panel) and 16-64 employment rate (right panel), by nation: UK

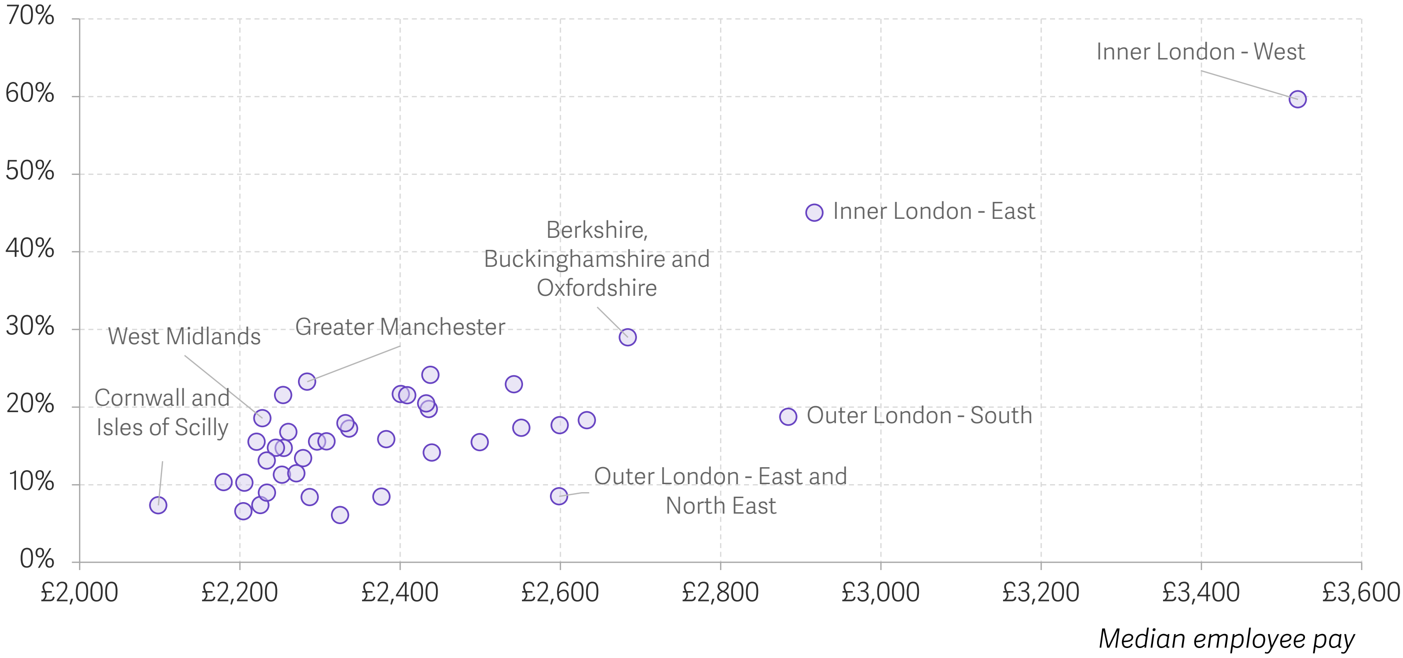


SOURCE: RF analysis of NISRA, Labour Market Report; ONS, Labour market statistics.

Problems with the Labour Force Survey (LFS) have made it challenging to fully understand the labour market, with its estimates out of step with administrative data. A key issue has been falling response rates, which have introduced more volatility and potentially bias. But this decline has not been uniform across the UK. As shown in the left panel of Figure 4, in Northern Ireland – where the LFS is administered by the Northern Ireland Statistics and Research Agency (NISRA) – response rates rose in 2022 and remained relatively steady throughout 2023 before falling again in the first half of 2024. By contrast, in Great Britain, response rates were falling in until late 2023, when the Office for National Statistics (ONS) introduced measures to improve data quality.

Our previous work has suggested that falling response rates have biased LFS employment estimates downwards, as groups with higher employment rates have become disproportionately less likely to respond. The right panel of Figure 4 is consistent with this finding: the employment trend in Northern Ireland has been more consistent with estimates based on administrative data during the period when its response rates remained strong. This is far from conclusive evidence on the effects of non-response bias in the LFS – not least as employment trends in Northern Ireland cannot be expected to mirror those across the rest of the UK – but adds another piece of the puzzle.

FIGURE 5: **The Government's industrial strategy is skewed towards high-paid parts of the country**
Proportion of Gross Value Added (GVA) in growth-driving sectors (vertical axis) and median employee pay (horizontal axis), by ITL2 region: UK, 2022 and 2024



NOTES: High-value sectors approximate the Green Paper list and are defined as SIC 07 codes 26, 27, 28-30, 35-39, 58-63, 64-66, 69-75 and 90-91. GVA figures are from 2022, and median employee pay are for January-November 2024.
SOURCE: RF analysis of ONS, Regional accounts; ONS/HMRC, Earnings and employment from Pay As You Earn Real Time Information.

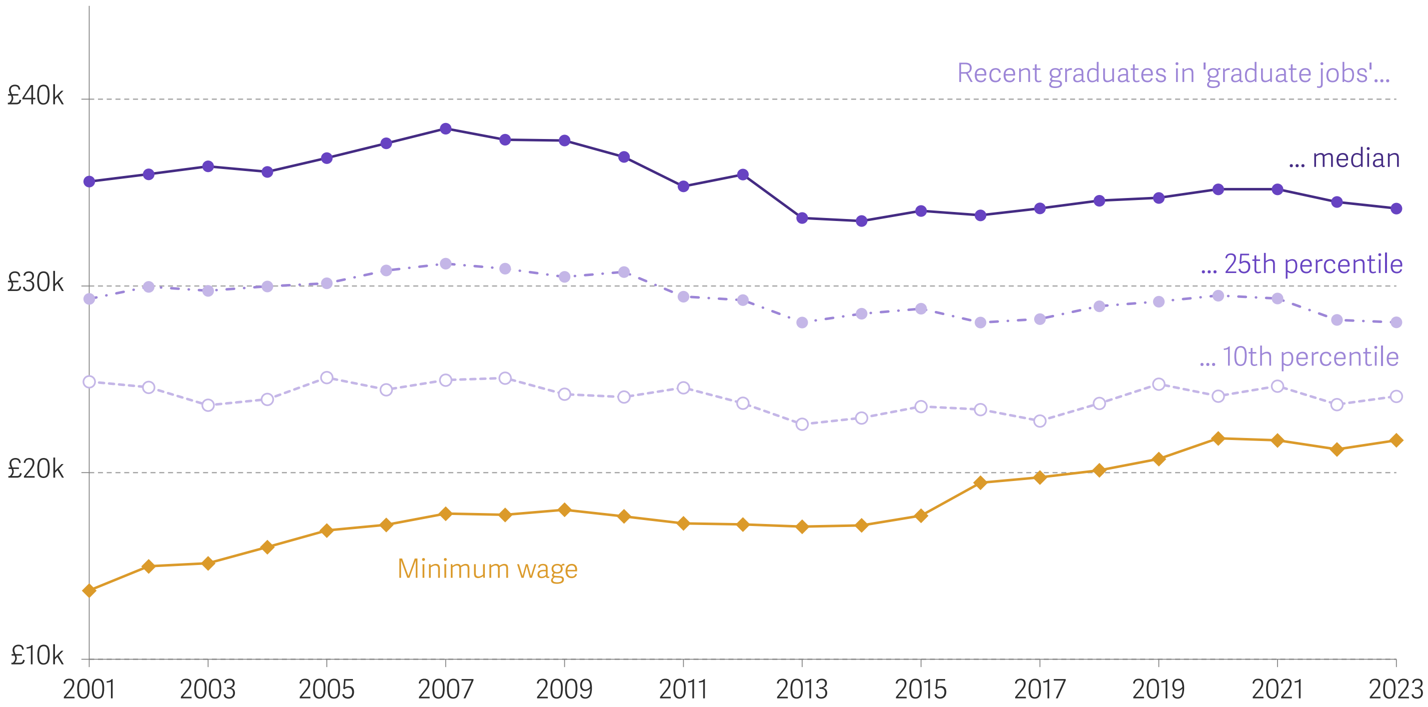
In a recent Resolution Foundation report, we assessed the Government's Green Paper on its new industrial strategy and highlighted – among other findings – that its plan to support eight high-productivity sectors would disproportionately channel funding to richer parts of the country. Figure 5 shows that the same is true for wages: places with higher typical employee pay tend to have a greater share of their Gross Value Added (GVA) concentrated in these 'growth-driving' sectors.[10]

There is a clear case for supporting these industries to leverage the UK's competitive advantages and boost UK-wide growth. But the Government should also consider whether its industrial strategy could do more to promote high-paying jobs in regions with a lower concentration of these sectors – particularly in the UK's underperforming second cities, Manchester and Birmingham.

10 A version of Figure 5 first appeared in: G Thwaites & D Willetts, The art of strategy: How to make a success of the Government's new Industrial Strategy, Resolution Foundation, December 2024.

FIGURE 6: **Graduate salaries have stagnated while the minimum wage has risen, leading to convergence between the two**

Real full-time annual earnings for someone on the minimum wage and different categories of graduates: UK



NOTES: Adjusted for CPI inflation. Recent graduates defined as those with a qualification at Level 4 or above and who have left education in the last five years. Graduate jobs defined using four-digit occupation codes set out in: P Elias & K Purcell, Classifying graduate occupations for the knowledge society, Institute for Employment Research Working Paper 5, February 2013, which defines non-graduate occupations as those in which the associated tasks do not normally require the knowledge and skills developed through higher education to perform these tasks in a competent manner. Full-time minimum wage equivalent assumes 40 hours a week.
SOURCE: RF analysis of ONS, Labour Force Survey.

The rising minimum wage has been a bright spot amid stagnating average wages. Figure 6 illustrates how this trend has affected recent graduates. The purple lines show that graduate salaries have stagnated in line with wages as a whole: in real terms, entry-level graduate salaries are now lower than they were before the financial crisis. By contrast, full-time minimum wage workers are doing far better than pre-financial crisis.

These differing trends have led to convergence between the minimum wage and entry-level graduate salaries. Two decades ago, the median graduate in a 'graduate job' had a salary 2.5 times that of a minimum wage worker. But by 2023, the typical graduate earned only 1.6 times the salary of someone on the wage floor. And the lowest-earning graduates now earn only marginally more than full-time minimum wage workers: those at the 10th percentile of earnings now have salaries just 11 per cent higher than someone on the wage floor, compared to 82 per cent higher back in 2001.

The Resolution Foundation is an independent research and policy organisation. Our goal is to improve the lives of people with low to middle incomes by delivering change in areas where they are currently disadvantaged.

We do this by undertaking research and analysis to understand the challenges facing people on a low to middle income, developing practical and effective policy proposals; and engaging with policy makers and stakeholders to influence decision-making and bring about change.

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