



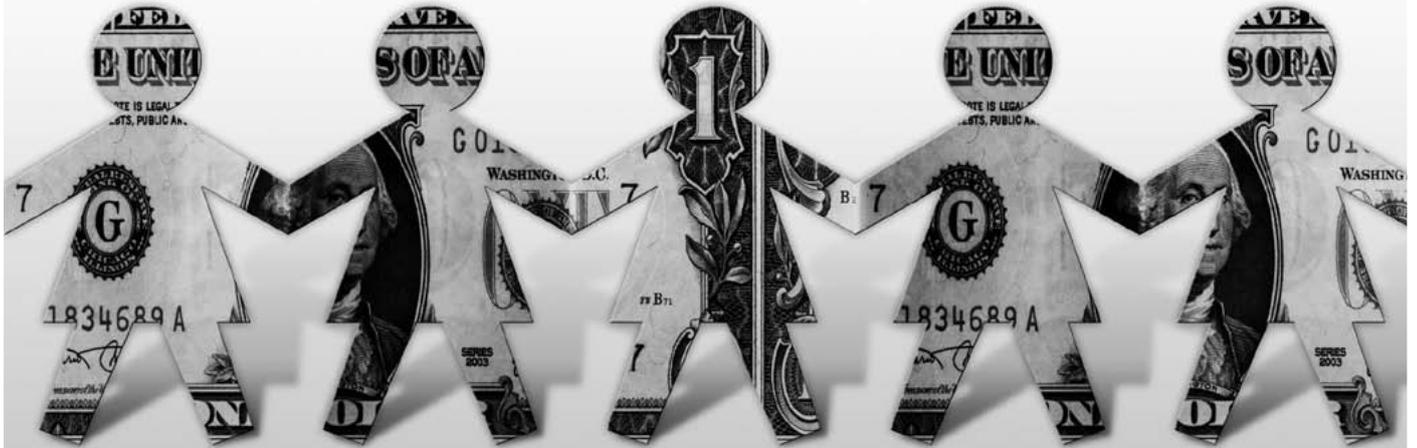
## A Bit Rich:

Calculating the real value to society of  
different professions

**nef** is an independent think-and-do tank that inspires and demonstrates real economic well-being.

We aim to improve quality of life by promoting innovative solutions that challenge mainstream thinking on economic, environmental and social issues. We work in partnership and put people and the planet first.

**nef** (the new economics foundation) is a registered charity founded in 1986 by the leaders of The Other Economic Summit (TOES), which forced issues such as international debt onto the agenda of the G8 summit meetings. It has taken a lead in helping establish new coalitions and organisations such as the Jubilee 2000 debt campaign; the Ethical Trading Initiative; the UK Social Investment Forum; and new ways to measure social and economic well-being.



In this report **nef** calculates the value to society of a number of different jobs and advocates a fundamental rethink of how the value of work is recognised and rewarded.

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# Executive summary

Pay matters. How much you earn can determine your lifestyle, where you can afford to live, and your aspirations and status. But to what extent does what we get paid confer 'worth'? Beyond a narrow notion of productivity, what impact does our work have on the rest of society, and do the financial rewards we receive correspond to this? Do those that get more contribute more to society? With controversial bonuses being paid out this Christmas in bailed-out banks, we believe that it is time to ask challenging questions such as these.

## Introduction

We are in the wake of the worst financial crisis for a century. Yet this Christmas, many highly paid employees of City banks that are responsible for creating this crisis are being paid extravagant bonuses. This comes at a time when wage inequality remains stubbornly high, due in large part to the increased concentration of very high and very low earners in the economy.

The controversies over City bankers' bonuses raise fundamental questions not only about the remuneration of senior executives and public servants but also about the relative value of the work of everyone in our society. How should we assess the wider contribution our work makes?

In this report **nef** (the new economics foundation) takes a new approach to looking at the value of work. We go beyond how much different professions are paid to look at what they contribute to society. We use some of the principles and valuation techniques of Social Return on Investment analysis<sup>1</sup> to quantify the social, environmental and economic value that these roles produce – or in some cases undermine.

Our report tells the story of six different jobs. We have chosen jobs from across the private and public sectors and deliberately chosen ones that illustrate the problem. Three are low paid – a hospital cleaner, a recycling plant worker and a childcare worker. The others are highly paid – a City banker, an advertising executive and a tax accountant. We recognise that our incentives are created by the institutions and systems around us. It is not our intention therefore, to target the individuals that do these jobs but rather to examine the professions themselves.

## Why wage inequality matters

In the UK we live in a society of extremes. The incomes of the very rich and the very poor continue to pull away from each other. This is influenced by many factors but wage inequality is at the heart of them. It is a corrosive, destabilising issue that is linked to a range of social problems. It disproportionately affects some groups – particularly women, who predominate in low paid (and unpaid) work. The least well paid jobs are often those that are among the most socially valuable – jobs that keep our communities and families together. The market does not reward this kind of work well, and such jobs are consequently undervalued or overlooked.

### Why a minimum wage is not enough...

The idea of a subsistence salary goes back to the early classical economists. We still set wage floors today to ensure there is a minimum below which employers are not allowed to hire. However these minimums are often set very low. The UK minimum wage is not indexed to average wages, which means it slips behind pay levels in the rest of the economy. The impact of globalisation has made matters worse, contributing to an increasing specialisation of the workforce that has seen many previously well-paid, semi-skilled jobs being replaced by low-skilled, service-based jobs with few options for progression.

### ...and why an upper limit is required

Low pay is only one part of the issue. There is little political appetite for reining in high pay, and the idea of setting a ceiling on the remuneration of top executives has failed to gain any meaningful momentum. One reason why a minimum wage has become the norm is that it has been accepted that employers have the power to set wages. By the same token, in some sectors, a shortage of skills or the exploitation of monopoly power has allowed a privileged few to capture very high rates of pay. Sectors such as finance are notorious for sky-high salaries and big bonuses, as remuneration committees are self-regulating and accountability to shareholders is often weak.

### From surplus value to social value

Early theories of value neglected the extent to which the production and trade of goods and services may have a wider impact on society that is not reflected in the cost of producing them. These 'externalities' are often remote or hard to see but that does not mean that they are not real or that they do not affect real people – either now or in the future.

Because social and environmental costs are not properly accounted for, the market tends to oversupply products that may have a significantly negative environmental or social impact – such as cheap consumer goods and complex financial products. In the same way we underpay work that has a high social value, creating high vacancy rates in our most important public services such as nursing and social work. By making social value creation an important societal goal we could set the right incentives to maximise net social benefits, ensure a greater return to labour rather than capital, and a more equal distribution of economic resources between workers.

### A closer look at six professions

We have tested our theory by taking a close look at a sample of highly paid and low paid jobs. We found that some of the most highly paid benefit us least, and some of the lowest-paid benefit us most. Although this will not always hold, it does point to a massive flaw in the system and highlights the need for reform.

High-earning investment **bankers** in the City of London are among the best remunerated people in the economy. But the earnings they command and the profits they make come at a huge cost because of the damaging social effects of the City of London's financial activities. We found that rather than being 'wealth creators', these City bankers are being handsomely rewarded for bringing the global financial system to the brink of collapse. **While collecting salaries of between £500,000 and £10 million, leading City bankers to destroy £7 of social value for every pound in value they generate.**

Both for families and for society as a whole, looking after children could not be more important. As well as providing a valuable service for families, childcare workers release earnings potential by allowing parents to continue working. They also unlock social benefits in the shape of the learning opportunities that children gain outside the home. **For every £1 they are paid, childcare workers generate between £7 and £9.50 worth of benefits to society.**

Although the role of an **advertising executive** has high status, the impact of the industry has always been a point of controversy. It encourages high consumer spending and indebtedness. It can create insatiable aspirations, fuelling feelings of dissatisfaction, inadequacy and stress. In our economic model we estimate

the share of social and environmental damage caused by overconsumption that is attributable to advertising. **For a salary of between £50,000 and £12 million, top advertising executives destroy £11 of value for every pound in value they generate.**

**Hospital cleaners** play a vital role in the workings of our healthcare facilities. Not only do they clean hospitals and help maintain standards of hygiene to protect against infection but they also contribute towards wider health outcomes. The importance of these cleaners is often underestimated and undervalued in the way they are paid and treated. **We estimated, however, that for every £1 they are paid, over £10 in social value is generated.**

Determining the right amount of tax payable is a specialist skill and often requires professional support. However, some highly paid **tax accountants'** sole purpose is to help rich individuals and companies to pay less tax. We found that the positive benefits to society of these activities are negligible. However, every pound that is 'avoided' in tax is a pound that would otherwise have gone to HM Revenue. In our model we looked at how this lost revenue could have been better spent. **For a salary of between £75,000 and £200,000 tax accountants destroy £47 of value for every pound in value they generate.**

**Waste recycling workers** do a range of different jobs that relate to processing and preventing waste and promoting recycling. Carbon emissions are significantly reduced when goods are recycled instead of sending them to incineration or landfill. There is also a value in reusing goods, and we have included this in our model. **Our model projects that for every £1 of value spent on wages, £12 of value will be generated.**

## The myths of pay and value

This report sets out to shatter some myths about pay and value. Chief among them – and the point of the research – is to show that there is not a straightforward relationship between high financial rewards and good societal outcomes. This isn't just an intellectual exercise – it has big implications for the way in which our society and economy are structured. Financial incentives are very powerful, and we tend to shower them on some of the professions that are the most socially and environmentally costly. This promotes undesirable behaviour, while positive activities are discouraged.

### Myth 1: The City of London is essential for the UK economy

Access to finance for everyone is vital for the UK economy to function. Yet the City of London has primarily been concerned with an aggressive quest for profits. This has heaped the worst financial crisis for a century on all parts of the economy. Even those closest to the City are increasingly sceptical about its value to the UK economy. On best estimates it contributes 3 per cent a year in value added compared to 12.5 per cent value added contributed from manufacturing.

### Myth 2: Low paid jobs create a ladder for people to work their way up – opportunities to advance are open to all

The level of income inequality in the UK means that high earners can protect their position and that of their children by buying education, assets and advantage. The ladder that might offer a way up for those on low incomes is effectively kicked away. The only way to improve equality of opportunity *and* outcome is to shorten the ladder in the first place.

### Myth 3: Pay differentials don't matter, so long as we eradicate poverty

Of course poverty matters. But increasingly it is not absolute levels of poverty alone but the differences between people that contribute to social problems such as crime, ill health, poor educational attainment and addiction. In focusing so much on improving the lot of those on very low incomes, we have ignored the differentials that underpin what has become a two-tier society.

#### **Myth 4: We need to pay high salaries to attract and retain talent in the UK**

Our case studies show that high salaries don't necessarily reflect talent. Even if they did, it is not clear that the best and brightest would be prepared to uproot their families and hike across the world for higher wages. The evidence suggests that more equal countries manage to retain their fair share of innovation and cultural capital.

#### **Myth 5: Workers in highly paid jobs work harder**

People at the bottom of the income distribution scale spend more time on domestic and caring responsibilities than their highly paid counterparts. They are also more likely to have more than one job, and for many that is the only route out of poverty. When we take this into account, it becomes clear that those who are paid less work just as much (or even more) than the better off.

#### **Myth 6: The private sector is more efficient than the public sector**

Work that is cheap is not necessarily work that is effective. This myth that the private sector is more efficient has motivated the increase in competitive tendering of public services to private contractors, and has been used to justify lower unit costs (and lower wages). However, lower prices are sometimes secured at the cost of service quality, suggesting that paying higher wages could in fact be more efficient.

#### **Myth 7: If we tax the rich, they will take their money and run**

Intuitively we understand that decisions on whether to emigrate are far more complex than how much people earn. They depend on a multitude of factors – not only financial circumstances but also cultural familiarity, environment, proximity to friends and family, and quality of public services.

#### **Myth 8: The rich contribute more to society**

The rich pay proportionately less tax than the poor, and many of our tax streams such as council tax and VAT are highly regressive. The rich even give less in relative terms to charity than the poor.

#### **Myth 9: Some jobs are more satisfying, so they require less pay**

Job satisfaction is related to a number of factors. Autonomy, control in the workplace, income and status all contribute towards a sense of satisfaction and fulfilment at work. If high pay is partly intended to compensate for risk, stress and long hours then we would expect dangerous jobs to be well rewarded. Fishing is the most dangerous job in Britain, with roofers and scaffolders also high up on the danger list, and waste recycling collectors are at number 18. Yet in none of these industries are rank-and-file workers highly paid.

#### **Myth 10: Pay always rewards underlying profitability**

It is becoming increasingly apparent that there is only a weak correlation between pay and executive performance. In 2008, for example, the UK's top companies lost almost a third of their value while the bosses of these companies enjoyed a 10 per cent leap in their basic salaries. Empirical studies have demonstrated that pay arrangements are geared towards serving the financial interests of managers, not shareholders.

### **Conclusions**

This report is not about targeting any individuals in the highly paid jobs it scrutinises. Neither is it simply suggesting that people in low paid jobs should be paid more. The point we are making is a more complex one – that there should be a relationship between what we are paid and the value our work generates for society.

We need to overcome deep structural issues to act on the implications of this report. Many of these were recently spelled out in a **nef** report *The Great Transition*, which charts the change from our current growth-based economic system to a more sustainable and equitable one.<sup>2</sup> The stakes are high: without proper checks and balances we believe our economic system could squeeze out those aspects of life that people value most. We urgently need to align incentives with the social and environmental value that are generated by the workforce.

## Some policy recommendations

- **End the policy silence on high pay.** nef has previously advocated a national maximum pay differential. This has been echoed recently by Compass and others with calls to establish a High Pay Commission. Its task could be to examine what the appropriate differentials should be. The Royal Navy, for example, has had a de facto differential of eight, whilst some Japanese firms voluntarily impose pay ratios limiting the gap between the top and bottom pay. Determining these multiples should be informed by the concept of social value creation.
- **Learn from the successes of anti-discrimination legislation.** Explore the possibility of positively discriminating towards people from low-income backgrounds to level the playing field in access to highly paid professions.
- **Build social and environmental value into prices.** Until goods and services reflect the real costs and benefits of their production, incentives will be misaligned with the kinds of positive behaviours society wishes to promote. Getting the prices right would affect relative profitability and so would align what wages could be paid with the value that is created. Consumption and corporation tax are two vehicles for doing this, but they need to be applied in a progressive way.
- **Introduce more progressive taxation.** The wealthiest do not pay their fair share of tax and the very wealthy may pay none at all. Redistribution, particularly of assets and land, is an effective way both to offset inequality and to reward jobs that the market does not. Closing tax loopholes would also be a good place to start.
- **Launch a green industrial policy.** We have an unprecedented opportunity to make environmental progress while also addressing wage inequality. The time has come for a new industrial policy, creating green jobs to replace the middle-income, semi-skilled jobs that have been wiped out in manufacturing.
- **Encourage new forms of ownership.** Mutually owned building societies, co-operatives and land trusts are all models in which ownership takes a more collective form, and benefits are more evenly shared.
- **Radically reform the role of the City.** It is time to return finance to its role as servant, not master of the economy. Instead of a monoculture of mega-banks deemed too big to fail and answerable only to the demands of private shareholders, we need a range of different financial institutions that are focused on social value creation. Initiatives such as a financial transaction tax would also reduce the harmful effects of trading.
- **Invest in universal child care and paid parental leave.** Child care provision in the UK often reflects and reinforces socio-economic and gender divisions. Making high-quality, affordable care available to all gives parents – particularly women – a better choice over returning to work and provides children with greater equality of opportunity. Extending parental leave, especially to fathers, would be a further investment in positive child development for the benefit of society.<sup>3</sup> These provisions could be entirely met by recouping the money lost to society through tax avoidance by the wealthiest. This valuable investment would also increase gender equality by improving career options for women.

# Introduction

*'How long will it be necessary to pay City men so entirely out of proportion to what other servants of society commonly receive for performing social services not less useful or difficult?'*

**John Maynard Keynes, 1913<sup>4</sup>**

*'In judging whether Corporate America is serious about reforming itself, CEO pay remains the acid test. To date, the results aren't encouraging.'*

**Warren Buffett, 2004<sup>5</sup>**

There is no doubt that wages measure things, and important things. They play a large part in shaping our lifestyles. Our aspirations, ambitions and status are often influenced significantly by what we earn. But to what extent is people's income a fair measure of the contribution they make? How much does what we are paid reflect our 'worth' to society? While income can approximate to the 'utility' we can enjoy in exchange for our labour, can it give us any other measure of ourselves?

Prevailing wisdom would say yes: pay is a reward that reflects merit. Those who contribute more get more in return. This stems from orthodox economic teaching, which asserts that the distribution of earnings is the outcome of an efficient working of the market, in which workers are paid according to their 'marginal productivity'.

In the private sector 'value' is closely associated with economic value or profit. The 'worth' of an employee is measured in terms of his or her perceived contribution to the bottom line, whether directly or indirectly. Even on its own terms this is problematic, as it is a very narrow measure of economic value that doesn't account for any impact on a company's long-term viability. In addition, some of the most valued staff – in terms of the day-to-day running of a company (e.g. administrators) – are the most poorly paid. This occurs simply because their skills are relatively plentiful. It is easy to see how the value of employees to a company and their financial rewards have become badly misaligned.

This issue has attracted much attention recently. In a climate where most feel the threat of job losses, pay freezes and reduced working hours, the issue of pay is a contentious one. The bonuses paid to traders in bailed-out banks have been roundly denounced. Public opinion also seems to be hardening on issues of low pay and inequality. One recent survey found that a majority of people thought City bankers, Premier League footballers and other high earners were overpaid.<sup>6</sup> Another indicated that a majority think the growing income gap is bad for our society.<sup>7</sup>

It is time to apply a different way of thinking to the value generated by different types of work. We should be looking beyond the narrow definition of economic productivity to calculate the broader social and environmental value of the work we do.

When we extend our concept of value in this way, the relationship between pay and value breaks down further. All forms of work create and destroy social, environmental and economic value. But this often bears little relationship to the way in which wages are allocated. In economics the unintended consequences

of market activity are known as 'externalities'. These may be remote and hard to see (sweated labour in Asia, for example), or they may not emerge until some time in the future (climate change). But someone is bearing the cost of them nonetheless. Private companies tend to bear a disproportionately small share of the burden, enabling them to inflate their profits and pay high wages. Conversely, those producing positive externalities may enjoy no economic benefit from this, which means their employers find it difficult to reflect societal value in the wages they are paid.

Some employees that are doing the most necessary work – care workers, classroom assistants and park rangers – are the least well paid. People's skills and abilities are not necessarily being deployed in the most useful way. The best people are not being attracted into the most important roles.

Neither are incentives for broader value creation being built into job descriptions. This allows, or even promotes, irresponsible behaviour and harmful business practice. A mortgage may be sold to someone who can't afford it, for example, because this earns a large commission – regardless of the costs to the individual and society that this produces.

For the first time **nef** is attempting to put a value on what different types of employment are worth to our society. Our work in this area draws on the principles of Social Return on Investment analysis. This approach enables us to quantify the social, environmental and economic value that people's work produces – or in some cases the value that is undermined or destroyed. In doing this we hope to throw light on the way in which our society rewards certain activities that might have little social benefit, while discouraging particularly valuable forms of work. We found that some of the jobs that are perceived to be the lowliest are actually the most useful.

This report tells the story of six different jobs. Three are low paid – a hospital cleaner, a recycling plant worker and childcare worker. The others are highly paid – a City banker, an advertising executive and a tax accountant. By looking at how these jobs are producing value and their corresponding financial rewards, we have sought to understand what this tells us about ourselves: what we value, and the kind of society we live in.

The report is structured around ten myths about pay and worth. Our case studies provide evidence that challenges these myths and demolishes them one by one. We begin, however, with the politics of this issue: a description of how we have reached this point, whom it affects most and why it matters.

# Inequality and high pay in the UK

*‘People on all levels of income are better off than they were in 1979... he would rather that the poor were poorer, provided that the rich were less rich. That way one will never create the wealth for better social services, as we have’*

**Margaret Thatcher, 1990<sup>8</sup>**

*‘More private wealth means more public wealth too’*

**John Major, 1992<sup>9</sup>**

*‘It’s not a burning ambition for me to make sure that David Beckham earns less money’*

**Tony Blair, 2001<sup>10</sup>**

*‘You are the wealth creators, the men and women who make our nation more prosperous...’*

**Gordon Brown in a speech to the City, 2003<sup>11</sup>**

## Introduction

In the UK today there are huge disparities in levels of pay for different occupations. Over the past decade the ratio between the average rate of pay for chief executives and the average earnings of employees has risen from 47:1 to 128:1. Executive pay has risen by 295 per cent in this period, compared with a rise of 44 per cent for employees.<sup>12</sup>

There is growing public unease over the extreme rewards bestowed on some in favoured sectors of the economy. This unease suggests that there is a limit to people’s tolerance of highly unequal pay, and that this limit is being severely tested. But it also reflects an underlying sense that the real value to us all of different jobs and workers is not being captured in market-led pay scales.

A recent breakdown<sup>13</sup> of the taxpaying population in the UK revealed that the top 10 per cent of adults, those on incomes of £36,000 per year or more, take home a disproportionate 40 per cent of UK income. This leaves only 60 per cent of the pot for 90 per cent of the adult working population to share. Some – particularly those in the caring professions, the retail sector, catering and environmental services – are not only earning low wages, but in some cases being paid below the statutory minimum.

## The costs of inequality

In the past 30 years the UK has seen a 44 per cent increase in inequality. On one measure it has switched from being one of the most equal developed countries to being one of the most unequal.<sup>14</sup>

It is now widely recognised that inequality is not only unjust but also inefficient and wasteful.<sup>15</sup> The most equal countries perform best on most social, environmental and economic indicators.<sup>16</sup> **nef** has calculated that restoring Danish levels of equality in the UK could generate about £7.35 trillion of social value between now and 2050.<sup>17</sup>

When inequality was comparatively low, many free market economists believed that increasing it was not only inevitable but also essential – a mechanism to create incentives and help ensure market efficiency. It is unlikely that these previous generations of economists envisaged that inequality would reach its current levels, where within the same company some employees may earn only two pence for every £10,000 earned by others.<sup>18</sup> And yet even at the beginning of the decade the International Monetary Fund's outgoing executive director, Michel Camdessus, argued that the gap between the rich and poor within nations (as well as between rich and poor nations) was morally outrageous, economically wasteful and potentially socially explosive.<sup>19</sup>

Most of the increased disparity that has emerged in the UK has been seen in the form of an increased concentration of very high and very low earners. The changing composition of UK industry – away from manufacturing and towards services and finance – has led to a hollowing out of the middle-income tier of the economy.

Not only are there more highly paid and low paid jobs than there used to be, but the returns for those jobs have increased at the top and decreased at the bottom.<sup>20</sup> This has implications both for inequality in general and for people's ability to move up and down the income distribution ladder – for some it is now a ladder with broken rungs. The causes behind this outcome are complex and are currently being explored by the new economics foundation in conjunction with the Joseph Rowntree Foundation.

The International Labour Organisation points out that depressed wage levels have forced many workers and their families to fund not only investment (predominantly for housing) but also consumption through debt.<sup>21</sup> The consequences of this were sharply demonstrated during the sub-prime mortgage crisis in the United States. As well as contributing to systemic instability, higher indebtedness inevitably reduces the ability of the low paid to weather an economic downturn, in which many are likely to lose their jobs.

Just as inequality has damaging effects on society at large, so it is damaging for business performance. A survey of human resources professionals in 2003<sup>22</sup> found that respondents overwhelmingly believed that overpaying top executives was detrimental to staff morale, commitment and product quality. The suggestion was that employee relations, and productivity, began to suffer once those at the top of an organisation earned fourteen or more times what was paid to those at the bottom.

This understanding is not new. The Royal Navy, John Lewis department stores and the Ben and Jerry's ice-cream company have all at times imposed limits on wage differentials in the belief that a measure of equality would benefit organisational performance. The fact that limits on differentials have had to be abandoned in some cases does not mean that pay differences don't impact negatively on productivity. The problem is that sometimes the executive elite uses its controlling bargaining position to overturn differential limits, as discussed in the next section.

### **The emergence of the super-rich**

The rise of the 'super rich' is very much an Anglo-American phenomenon, with the United States leading the way. According to the ILO, average chief executive annual earnings were 500 times the level of the average worker's earnings in 2007.<sup>23</sup> More eye-opening still is the fact that this was up from 300 times a mere four years earlier. Differentials between top and lowest earnings in a number of European nations, including France, Germany and Sweden, are typically lower than in the US and UK.<sup>24</sup>

The main reasons for lower disparities in income and earnings in some countries are higher levels of unionisation and collective bargaining, particularly where that bargaining takes place above the level of the company concerned.<sup>25</sup> Some countries that have pursued a social-corporatist approach have established a system that implicitly recognises the contribution of the average worker to economic performance and social value, and acts to share returns more equally among workers. In addition to high wage differentials, the US and UK have relatively low tax rates compared to their European counterparts, so even if the gap between market incomes is higher, income is still not redistributed on the same scale.

## It's women's work

The vast majority of higher post-war employment for women is attributable to the service of the welfare state – jobs such as nursing and teaching. But women's contributions to formal and informal welfare have tended to be ignored by policy makers.

Women predominate in low paid jobs, making up 83 per cent of the workforce in personal services and 60 per of the public sector workforce as a whole. Only 30 per cent of senior executive positions are held by women.<sup>26</sup> Women are grossly under-represented in the most highly paid jobs, holding only 11 per cent of FTSE 100 directorships.

This is not just a problem in boardrooms. A recent report by the British Medical Foundation found that after excluding differences owing to age, experience and area of specialism, there is an average salary gap of £15,245 between men and women among the UK's 135,000 medics.<sup>27</sup> On average women working full time earn 18 per cent less per hour than their male counterparts.<sup>28</sup> The difference in hourly earnings increases to 25 per cent when women working part time are included.<sup>29</sup> Although the gap had been closing in the second half of the twentieth century, convergence has slowed in recent years. There has been little change since the mid-1990s.

Gender pay inequalities are exacerbated by a perverse system in which a very high or low value is placed on certain jobs quite arbitrarily. This problem occurs not only within the mainstream economy but also outside the formal labour market – in home working, for example. Women have always provided most of the informal, unpaid welfare within the family. They still contribute twice as much time as men on housework and caring for children and other relatives.<sup>30</sup>

UK policy in recent years has tended to regard women with children first and foremost as “citizen-workers” rather than as “citizen-mothers”. This raises the possibility that the unpaid work of caring for and bringing up children is currently valued and prioritised very differently by policy-makers on the one hand, and mothers themselves on the other.<sup>31</sup> Growth in the service sector and the availability of part-time and casual employment mean that for many women the most formidable challenge in the labour market is not getting off benefits into paid employment but finding a way to advance yourself once you have a job of some kind. For women, in particular, there is a high risk of getting caught in low-skilled, part-time work without a hope of promotion or receiving any substantial training.

The goal of economic equality for women in high-income countries has been widely accepted as a laudable one. But it is a long way from being achieved. This may be partly due to gender bias, with employers tending to recruit men into top positions.<sup>32</sup> But a more radical and perhaps convincing reason for why greater equality for women has not been achieved is that markets as constructed in our economy naturally favour men – in the tendency for long working hours to be required, for example.

Reforming and restraining markets so that they support and foster the non-economic aspects of life – the things that people really value – could arguably do more for women than all the positive discrimination in the world. Positive discrimination and any measures to promote women in non-traditional roles fail to recognise the extent to which our very economic systems are male constructs. Our economic structures reflect the values and strengths of men and the power distribution of existing gender relations. There is a built-in predisposition towards inequality.

# Wage-setting: the iron law of wages and the race to the bottom

‘Labour, like all other things which are purchased and sold, and which may be increased or diminished in quantity, has its natural and its market price. The natural price of labour is that price which is necessary to enable labourers, one with another, to subsist and perpetuate without either increase, or diminution’

David Ricardo, 1817<sup>33</sup>

## The iron law of wages

The classical economists – Smith, Ricardo and Malthus – first theorised about a subsistence or living wage in the eighteenth century. They all followed the ‘iron law of wages’, or in Adam Smith’s words the belief that “a man must always live by his work, and his wages must at least be sufficient to maintain him”.<sup>34</sup>

In Ricardo’s view,<sup>35</sup> progress required the accumulation of capital, and landowners were the passive, faultless beneficiaries of this. Ricardo reflected that this was a miserable deal for the landless worker but that the alternative – starvation – was worse. The iron law, therefore, was the law by which wages should be regulated “...and by which the happiness of far the greatest part of every community is governed”.

To ensure the best societal outcomes Ricardo thought that wages “should be left to the fair and free competition of the market, and should never be controlled by the legislature”. This commodification of labour would later inspire Karl Marx, who made famous the concept of ‘surplus value’. For Marx all exchange value is created by the worker, and this value is then appropriated by the capitalist. He predicted that this process of ‘valorisation’ would lead to the eventual collapse of capitalism, as wages would be squeezed further and further, creating a ‘race to the bottom’.

## Low-wage Britain – a race to the bottom?

Life as described for the ordinary worker by Malthus, Ricardo and Marx may sound bleak. But it is still the reality for many in low-wage Britain. While a minimum wage has become a statutory requirement, it has never been indexed to wages and no longer sets a real ‘floor’. This means that its potential for tackling inequality has largely been neutralised.<sup>36</sup> It is currently set well below the ‘living wage’ that research shows is required to subsist.<sup>37</sup> Neither should gains for the low paid be taken as a given, as evidenced by the recent Conservative private member’s bill that sought an opt-out from the minimum wage for employers.<sup>38</sup>

One of the reasons why a minimum wage has become the norm is because it has been accepted that perfect competition does not exist and that employers have ‘monopsony’ power – the power to set wages. It is increasingly evident however, that workers at the top end have the power to command salaries over and above what the market will bear.<sup>39</sup>

What Marx correctly predicted was that real wages, or returns to workers, would be eroded over time.<sup>40</sup> As the productivity of workers has increased, the associated gains have been extracted in the form of profit, rather than being distributed between those that have produced these gains. By progressively expanding the market, essentially by bringing more and more consumers into the globalised, capitalist system, capital has continued to grow.

But there are limits to how far it is possible for this to continue. At some point, when the market cannot be expanded any further, Marx's predictions could yet be borne out. In the mean time a shortage of skills in some sectors, or the exploitation of monopoly power, allows a few to profiteer at the expense of others.

The disconnection between executive remuneration and corporate performance means that high pay differentials cannot be rationalised by performance delivery. An honest analysis ought to concede that the executive elite has the power to demand and receive excessive pay without being bound to contribute greater returns. Remuneration committees are both self-regulated and self-fulfilling, comprised as they are of members of the executive elite. Shareholders have little power to contain management pay.

### **From surplus value to social value**

Early theories of value saw it either in the labour embodied in goods or services – “the toil, or trouble of acquiring it”<sup>41</sup> – or the use-value, which later became known as utility. What each of these neglects is that the production, trade and consumption of a good or service may have wider impacts on society which are hard to see, and which are not reflected in the cost of production. Consider, for example, the cost in terms of current and predicted climate change of carbon dioxide emissions from a range of economic activities. That cost has generally not been paid by those who produced the emissions, nor by those that derive utility from those economic activities. Externalities can also be positive, however – a good or service I buy can provide jobs and livelihoods to people I have never met.

We use the term ‘social value’ to refer to the combined positive externalities and individual utilities associated with goods and services – whether these accrue within or outside the market. This is complicated by the fact that we experience the world subjectively, so our perceptions of positive and negative will differ. For example, consider what might happen if a home owner decides to plant a small, commercial orchard in his front garden. If songbirds come to sing there every morning his neighbour on one side may experience this as a positive externality because he is an avid birdwatcher. But the neighbour on the other side may work nightshifts, in which case the noise of the birds is a negative externality. So the orchard grower’s business venture is creating both positive and negative externalities. In this sense, all value is subjective and what counts as social value is self-defined. In measuring social value, we explicitly include unintended consequences in the overall assessment of how positive the value creation is.

Orthodox economic thinking tells us that our utility is derived from money. The more money we make, the more utility we have. It then follows that the way to maximise social welfare is to maximise total income. However, we can’t just add up everyone’s income and call this total societal utility. Focusing on individual incomes (or utilities) is bound to be blind to side effects, and encourages undesirable behaviour from a societal perspective.

In contrast the idea of social value is that we can encourage behaviour that is positive for society. Over time a focus on social value has the potential to set the right incentives to maximise net social value, create more equal factor shares between labour and capital, and deliver a more equal distribution of economic resources between workers.

Now let us turn to our case studies, to see how this plays out in practice.

# The story of six professions

## Myth 1: The City of London is essential for the UK economy

*'I represent a seaside town which for decades had a profitable sweet factory, making a product called Chewits...I went to see the company when it was in process of retooling; it was profitable and doing rather well. It employed people who had to operate at a relatively skilled level and it provided a good mix of employment. It was then bought by a City company. The machinery was sent to Eastern Europe, the skilled work force was sacked, the job mix in the town was worsened, the carbon footprint of production was increased and the land was sold for housing. The UK economy did not benefit, but profit was made in the City'*

**Dr John Pugh, Liberal Democrat MP for Southport<sup>42</sup>**

The City of London's wholesale financial intermediation markets, which focus on high value-added financial transactions and trade in international financial instruments including 'exotics' such as derivatives, is distinct from the retail finance sector (which spans the whole UK economy). The distinction is important, because there is no doubt that retail financial services provided to businesses and individuals are vital to the health of the economy. In contrast, the activities of City traders in their aggressive search for profits has, according to the Governor of the Bank of England, heaped the worst financial crisis since the first world war on all parts of the economy.<sup>43</sup> Despite this, claims continue to abound as to the importance of the City of London to the wider economy.

The first thing to note is that the best estimate for the contribution of the City's financial activities to the UK economy is 3 per cent a year, up from around 2 per cent a year at the beginning of the decade.<sup>44</sup> This compares with UK manufacturing at 12.5 per cent,<sup>45</sup> even after the 'outsourcing' of much of our manufacturing base.

Despite contributing only a small share in value added to the UK economy, City firms do make a sizeable contribution to the Exchequer in taxes in good times. But many years' worth of tax contributions have now been wiped out directly through the taxpayer's bail-out of the sector, and indirectly through the impact of the financial crisis on the public finances – now deeply in the red. In addition the point has been made, not least in Parliament, that there are specialists in the City whose day-to-day work is to help individuals and businesses avoid paying taxes – losing revenue to the Exchequer of some £25 billion every year.

Some economists argue that there is a natural rate of entrepreneurship in the economy. But because of the financial rewards on offer, the City is likely to attract a disproportionate share of entrepreneurs. This leaves fewer entrepreneurs at the disposal of other potentially more productive and less damaging sectors of the economy.<sup>46</sup>

James Tobin, in a paper on efficiency in the financial sector, identifies a number of different types of efficiency. One is the use of the stock of human capital, where he argues that it cannot be 'efficient' for all the brightest graduates to end up in finance.<sup>47</sup> This goes beyond entrepreneurs though, as many physics and engineering PhD graduates in the UK end up in the City, rather than doing science or engineering.

## The City banker

*'Parts of the financial services industries need to reflect deeply on their role in the economy, and to recommit to a focus on their essential social and economic functions'*

Lord Adair Turner<sup>48</sup>

### WANTED

A finance professional to head up investment services to governments and corporations. Includes buying, selling, and trading securities; managing assets; and giving financial advice on capital formation, mergers and acquisitions. Relentlessly focused on short-term profit, and relaxed about misunderstanding the complex deals you will create and manage, you are likely to be male and in your twenties or thirties.

Remuneration package: Millions

High-earning bankers in the City of London are among the best remunerated people in the UK economy. For portfolio managers and traders an annual income of £500,000 means that a City banker can earn in ten working days what someone in the UK's middle income bracket earns in a year.

Although City bankers' rewards are a closely guarded secret, it is generally understood that the few senior partners in the major finance houses can take home somewhere between £5 million and £10 million a year.<sup>49</sup> A handful will earn substantially more. Meanwhile, top hedge-fund managers can end up making hundreds of millions in a year.

These enormous earnings are the result of profit taking on a huge scale. The reasons why this is possible are complex but are linked to the dominant position of finance in the economy. This domination is due to a number of factors. One is the deregulation of the financial markets that began in the 1970s. Another is the incentives that exist for clever City bankers to create complex chains of transactions to maximise the money they make – a share of which they take home in bonuses. Also, given the scale of the sums being churned through the financial system, even a small portion extracted in the form of commission or fees can add up to a very large amount of money – especially when shared between the relatively few people at the top of the financial tree.

Contrary to what we might expect, given the vociferous defence of the importance of wholesale banking to the UK economy, the City of London contributes only around 3 per cent of value added every year.<sup>50</sup> Claims have been made about the trickle down effects of wealthy City bankers' spending in the economy but there is little real evidence to back this up. We hear less about the damaging effects of the City on society.

These negative externalities, predominantly the risk and reality of regular systemic crises, do not feature in banks' balance sheets. This is because the banks do not have to pay for them, and incentives are therefore structured around profit rather than value.

Our analysis found that for every £1 in value created, £7 worth of value is destroyed by a highly paid City banker. In summary, our calculation is derived from the following:

#### Factors in value created:

- 1 Average annual contribution of the City to UK economic activity, as measured by gross value added
- 2 Tax contributions to the Exchequer
- 3 Jobs provided in the wholesale finance sector.

#### Factors in value destroyed:

- 1 The cost of the current financial crisis in terms of loss to UK gross domestic product and economic capacity
- 2 The cost of that crisis in terms of the negative impact on the public finances.

We might also have thrown the net wider and included other impacts, not least the negative impact on the global economy of the activities of highly paid investment bankers and traders. Far from being 'wealth creators', City bankers are being handsomely rewarded for socially damaging activity. They are not just overpaid; they are overpaid at the expense of others.

## **Myth 2: Low paid jobs create a ladder for people to work their way up – opportunities to advance are open to all**

Social mobility – the extent to which people move up or down the social ladder – is often used to justify wide pay differentials. If everyone has a shot at reaching the top, the argument goes, then hard work and ability will be rewarded handsomely. It is therefore in all our interests that millionaires exist because it gives us something to aim for. If we just try hard enough, we too can climb that ladder.

Rags-to-riches stories have been with us as long as storytelling itself. There is a chance that the daughters of our nursery workers may become advertising executives. The case of our low paid hospital cleaner may seem less unfair over time if her descendants are able to climb the ladder of remuneration, smoothing out the distribution of rewards across the generations. But what about the sons of our City bankers becoming hospital cleaners? How many of those stories have we heard? Where such stories are told, is it not with a hint of disappointment or disapproval for one that has fallen on hard times? If social mobility really were a reality, wouldn't the 'riches-to-rags' stories be just as plentiful?

Social mobility can only work if it is in both directions. A common measure is the extent to which a father's income predicts that of his sons. Using this measure, researchers have found that countries with the narrowest income differentials – the more equal countries – have higher social mobility.<sup>51</sup>

As has been pointed out, the 'American dream' really is only a dream if you live in America. In the UK, meanwhile, social mobility has been flat for some time.<sup>52</sup> Most people end their lives in the same circumstances as their parents and grandparents before them in terms of relative income within society.

Ultimately, there are only a very limited number of positions available as City bankers. For the ablest children of our recycling plant workers to climb the ladder, an equivalent number of City bankers' children would have to move down. Those with high incomes can protect their position and that of their children by buying assets and advantage. This means that the ladder offering opportunity to others is effectively kicked away. The only way to improve equality of opportunity *and* outcome is to shorten the ladder in the first place.

## **Myth 3: Pay differentials don't matter, so long as we eradicate absolute poverty**

UK social policy since 1997 has largely focused on those on low incomes and the unemployed. Work has been seen as a primary route out of poverty. Cash transfers have been aimed at the low paid, particularly those with children.

In addition, Labour has asked to be judged on its record on child poverty, setting ambitious targets in this area. Not only was high pay not targeted but it was actively encouraged. Peter Mandelson was famously "intensely relaxed about people getting filthy rich". The first decade of the twenty-first century has seen a new climate of tolerance for tax avoidance, corporate excess and privilege. Labour seems to have bought in wholesale to the 'trickle down' theory that it once derided. No wonder Margaret Thatcher once described New Labour as her greatest achievement.

A huge flaw in the policies of successive governments is that they have failed to grasp not only that differentials matter in themselves but also that equality is a precondition if you want to achieve low levels of poverty. We have known for a long time that social problems, such as crime, ill-health, poor educational attainment and drug addiction, are often economic in origin. What we now know as well is that it is not absolute levels of poverty alone that matter but the differences between people. Where differences exist, these can affect our well-being, levels of trust, our commitment to the stewardship of the planet and even our economic performance.<sup>53</sup>

In spite of transfers of resources to the poor, the performance of policies designed to counter child poverty has been sluggish according to the Government's own indicators – despite our having gone through a time of plenty. Letting the top earners have free rein to raise enough money to cast pennies at the bottom has not worked. High pay needs to be a target of policy in the way low pay has been, not least because it is such a huge source of market failure.

## The nursery worker

*'You've got lives in your hands ... you've got such an incredible responsibility and get paid nothing for it'*

UNISON report, 2006<sup>54</sup>

*'Although early childhood education and care benefits all children... good child care can compensate, at least partially, for a disadvantaged home life'*

Cleveland and Krashinsky, 2006<sup>55</sup>

*In many countries...employment in nurseries and day-care centres is often seen as suitable for those who are very young, unqualified, transient, or all three'*

Childcare Transition, UNICEF report, 2008<sup>56</sup>

### WANTED

A worker to look after the emotional and physical needs of small children (under five years of age) in nurseries and day-care centres.<sup>57</sup> You will ensure the children's safety and facilitate early learning. You will also have an important role in supporting parents by being aware of and available to discuss each child's growth, progress, development and needs. The successful candidate is likely to be a school-leaver or equivalent. You should expect remuneration substantially below the level of responsibility of the post, with few opportunities for career advancement.

Salary scale: £10,000–£13,000

Child care is a crucial service in the UK. It enables some parents of children under five to continue working when they have young children, with all the associated benefits that brings to individuals, families and society. In Sweden, 70% of all mothers and 80% of lone mothers have a job.<sup>58</sup> This compares with 56 per cent of lone mothers in the UK.<sup>59</sup> The high rates of maternal employment in Sweden have helped keep child poverty rates very low – at just 4 per cent.<sup>60</sup> For both families and wider society nurturing and protecting our children could not be more important. Yet child care is a profession with very low status in the UK, and is one of the most poorly paid occupations in our economy.

Of course, there is varying quality in childcare provision. Our analysis rests on an assumption of good childcare, from which there are substantial benefits. There are clear economic benefits: parents are able to continue working, with the productivity and public finance implications of that. Where childcare is good, employers are likely to see reduced rates of absenteeism and distraction at work.<sup>61</sup> There are also quality-of-life benefits in being able to work outside the home, particularly for women. Countries with widespread child care provision have high female employment, so childcare may make a contribution to gender equality.<sup>62</sup>

In addition to these benefits, there is evidence that children gain from positive early learning opportunities outside the home.<sup>63</sup> Compared with other European countries that finance universal child care systems as a critical part of their social investment, the UK carries a much higher financial and non-financial cost burden from social problems.<sup>64</sup> Evidence from studies of the impact of early child care on how deprived children fare in later life, strongly suggests that the cost of social problems could be mitigated by expanding early-years support through high-quality child care provision.

When we take account just of the lifestyle and equality benefits from being able to work outside the home, we find that every £1 paid to a childcare worker generates £7 worth of benefits for society. If we expand this to include the social value of reduced social problems as a result of children getting a better start in life, the potential benefit conferred by child care workers increases to a whopping £9.50, almost ten times their pay.

## Myth 4: We need to pay high salaries to attract and retain talent in the UK

*'...In budget after budget I want the nation...to do more to encourage the risk takers, those with ambition, to turn their ideas into reality and make the most of their talents'*

Gordon Brown, 2004<sup>65</sup>

For this myth to be true a number of other myths must also be true: that the highly paid are first and foremost rational economic actors; that social mobility is a reality that rewards people's talent and effort; and that there is perfect competition in the labour market. As we will show all of these assertions are on very shaky ground.

For this myth to be true, the best and brightest people in the UK would need to be in the most highly paid jobs. The best and brightest from across the world would need to be concentrated in a small number of countries that offered the most favourable conditions. Not only is this not true, but there doesn't seem to be a reliable relationship between talent, entrepreneurship and income.

It would appear that according to a number of indicators, the reverse is in fact true. For example, there is a weak but significant tendency for more equal societies to gain more patents per head than less equal ones. More equal countries also feature heavily at the top of the list of the countries where the most books are published per head.<sup>66</sup> Inequality, it could also be argued, wastes the talents of a large proportion of the population.

In a report for the Work Foundation, *Life at the Top*,<sup>67</sup> the following insights were shared:

- (1) Nearly 60 per cent of chief executives of FTSE-250 companies had worked in their firms for more than eight years, substantially above the average tenure of five-and-a-half years. This suggests that rather than there being a fluid market of top executives switching firms to capitalise on the best remuneration, companies nurture and retain their senior staff.
- (2) Contrary to claims that the labour market for senior executives is global, 86 per cent of FTSE-250 chief executives are of UK nationality.
- (3) While French and German chief executives are paid less than their UK counterparts, there is greater business productivity in France and Germany.

Finally, it is not possible to square the causes of this recession with the idea that we are hoarding talent in the UK. Gross incompetence at the top of many of our banks has been directly responsible for the calamity of late 2008. Surely this isn't the best our money can buy.

## Case study: Kentucky Fried Chicken<sup>68</sup>

In 2005 health concerns around food, particularly fast food, were mounting. Morgan Spurlock's film *Supersize Me* had been released the previous September, and *Jamie's School Dinners* had been screened on Channel 4. The government had begun to set and to introduce new standards for school meals. Against this backdrop KFC's sales were falling dramatically.

The company engaged an advertising agency, and ran a campaign featuring the appeal of their fast-food taste. The stated advertising objectives were as follows:

- (1) Create a desire for food, bringing KFC to the front of people's minds
- (2) Evoke a new empathy with families by identifying with mums
- (3) Prompt a craving for KFC among a youth audience.

Describing the campaign in its submission for an advertising award, the agency noted: "*Feeding the kids had become a fraught and guilt-ridden experience. Mums wanted to feel that someone understood and empathised with the realities of feeding a young family... [KFC] had to make them feel good about buying it.*"

The campaign was a great success for KFC, returning over £4 in profit for every £1 spent on advertising. It is ironic, however, that the advertising industry is able to reap further gains later by helping to rein in the very behaviour it promotes in the first place. The Department of Health recently commissioned top ad agency M&C Saatchi to develop its £75 million anti-obesity advertising campaign.

## The advertising executive

*'Whether it's lip balm or blue jeans, 'more is more' says Nita Rollins, who heads marketing intelligence at the digital marketing agency Resource Interactive. "Nothing succeeds like excess." The average number of Lip Smacker-brand lip balm and glosses owned by Bonne Bell customers is ten but, Bell notes, "the girls who have 100 make up for the ones who don't have ten".'*

USA Today, 13 April 2007<sup>69</sup>

### WANTED

Senior account executive for whom enough is not enough. Do you have a flair for convincing people they want things they don't need? The successful candidate must be able to bring research and creative processes together, and suspend his or her social and environmental conscience.

Salary range: £50,000–£12 million

The advertising industry offers the potential for high earnings and high status in a creative environment. But the role of advertising in society has always been a subject of controversy. Those in support argue that advertising provides valuable information that helps consumers to make effective choices about what they buy. Outside the market, advertising is used to try to influence other choices and behaviour – through government health promotion campaigns, for example.

Others argue passionately about the detrimental impacts of advertising. It creates insatiable aspirations and dissatisfaction, they say. It promotes feelings of inadequacy and stress. It encourages overspending, and hence indebtedness. Arguments also focus on the view that advertising is not about disseminating full information but about manipulating people through the selective use of information.

On a larger scale economists – most famously JK Galbraith – have argued that advertising has very negative effects on society. It does this by creating socially (and environmentally) wasteful 'wants' where needs have already been satisfied.<sup>70</sup> For Lippke, the aim of advertising is to turn people into consumers.<sup>71</sup> According to this view, although people are able to resist purchasing a specific item, they are unable to resist the consumer lifestyle.

As with the other highly paid professions we have examined, we have been careful to calculate the good attributed to the advertising industry as well as the bad. We wanted to ensure a fair and balanced estimate. The overconsumption that advertising generates creates jobs – someone has to make the stuff, and then someone has to sell the stuff.

But what about the negative effects of overconsumption? We have calculated the costs to UK society of obesity, anxiety-related mental health problems and indebtedness. Then there are the substantial environmental costs from climate change and resource depletion. It is estimated that in rich countries such as the UK, the level of consumption is three times as much as the planet's environmental resources can sustain.<sup>72</sup>

Advertising agencies are keen to demonstrate the returns they create for their customers. These estimates of additional sales generated allowed us to calculate the share of overconsumption attributable to advertising, and then the damage that causes. We found that for every £1 of value created by an advertising executive, £11.50 is destroyed. This is almost the exact reverse of the hospital cleaner.

## Myth 5: Workers in highly paid jobs work harder

It has been claimed that workers at the top end of the income scale work long hours and therefore 'deserve' higher earnings. There are several factors, however, that are not usually taken into consideration when calculating hours worked.

One of these factors is the fact that the poorest in our society are just as likely to work long hours in a main job and/or to take on multiple paid jobs. Many need to do so to make ends meet.<sup>73</sup> Neither does this myth take account of the number of hours worked outside the market economy. It is often argued that providing care in a family setting should not be included in national accounts because production of services within households is a self-contained activity, with limited repercussions on the rest of the economy. This, as feminists and others have shown, is simply not true. As has been extensively documented elsewhere,<sup>74</sup> the non-market economy (or the *sphere of reproduction*) is necessary for a more complete understanding of the market economy (the *sphere of production*). Without the reproduction of labour power on a daily and generational basis, productive activities would grind to a halt.

In this sense the inclusion of hours worked in the non-market economy for different income groups is crucial to the understanding of people's contributions to the economy as a whole – both in the productive and reproductive spheres. Data from ONS's Time Use Survey 2005 show that people at the bottom of the income scale spend, on average, 82 more minutes per day on 'providing housework' than their higher-income counterparts.

If these figures are disaggregated further, considerable differences arise between lower and higher income groups in providing certain types of housework, such as cooking and cleaning. In addition to this, data shows that lower-income groups provide 13 more minutes per day in childcare than higher income people do. Although the difference of care provided for adults is quite small, one could still argue that lower-income groups spend approximately 18 more minutes per day solely on care, which accounts for 8.4 extra hours of work per month. In summary, if we consider the impact of unpaid labour on paid labour, or even the interrelationships between them, we can certainly make the point that lower-income individuals work just as hard (or even harder) than their higher-income counterparts.

## Myth 6: The private sector is more efficient than the public sector, hence the higher salaries

Work that is cheap is not necessarily work that is effective. This myth about the supposed efficiency of the private sector has contributed to an increase in competitive tendering of public services to private contractors. It has also been used to justify spending less on a service. But lower prices often come at a cost.

In the case of hospital cleaning UNISON has shown how cost savings have been generated by paying staff less and allowing working conditions to deteriorate. Cost cutting can reduce the time spent on cleaning and affect the quality of the cleaning service as a whole. Competitive tendering can thus lead to all sorts of negative consequences.<sup>75</sup>

The BBC's *Panorama*<sup>76</sup> programme uncovered cleaners working 12-hour shifts for six consecutive days to earn sufficient wages to live on. There are reports of cleaners not eligible for sick pay coming into work unwell. When things like this occur, the service can fail to deliver the things that really matter to people – such as good patient care and lower Hospital Acquired infection rates. In short the savings are a false economy.

Similar trends emerge when we broaden the question to include goods and services that traditionally fall outside of public services. Our current system – in which efficiency means doing more for less – can actually crowd out many of the things that we value as a society. It means it is 'efficient' for City bankers to devise more and more creative financial products rather than provide sustainable access to finance. It means it is 'efficient' for advertisers to motivate consumers to eat more and more cake, regardless of the costs in obesity-related health problems for the state. It also means it is 'efficient' for the cake that the advertising agencies promote to be extravagantly packaged and exported half way across the world – regardless of the environmental impact. We need a new definition of efficiency, one that takes account of outcomes.<sup>77</sup> Efficiency savings will be misleading unless we include the true social and environmental outcomes of the goods or services being produced. The concept of 'efficiency wages' is useful here. This term describes the situation where it is more effective to pay staff *above* the minimum wage. It can build loyalty, increase incentives for staff to do their job effectively, and enable people to enjoy a decent standard of living.

## The hospital cleaner

*'It's very interesting that when you put a cleaner's outfit on, people don't treat you in the same way, and that's a pity because it doesn't recognise the contribution that they're making'*

Dr Mark Goldman, Chief Executive, Heart of England NHS Foundation Trust<sup>78</sup>

### WANTED

Hardworking, caring and conscientious individual required to clean hospital patient rooms, baths, laboratories, offices, halls, and other areas; wash beds and mattresses; remake beds; keep utility and storage rooms in clean and orderly condition; distribute laundered articles and linens; replace soiled drapes and cubicle curtains; disinfect and sterilize equipment and supplies; use germicides and sterilizing equipment; perform other duties as described under 'CLEANER'. You will not be concerned with the risk of infection from exposure to body fluids and faeces, nor will you care about working with corrosive cleaning products. You will support the equality, diversity, rights and responsibilities of individuals be courteous at all times and maintain patient confidentiality. You must be able to work night shifts and unsociable hours.

Salary: £6.26 per hour

Hospital cleaners don't just clean deserted buildings. As shown above, their role is inextricable from the working of the hospital and the treatment of patients.<sup>79</sup> It is recognised that cleaners play an important role in achieving wider health outcomes and in gaining the trust and confidence of patients. Despite this pivotal role their job has low pay and low status.

Cleaning services in hospitals have often fallen foul of the efficiency agenda and the disruptive reforms and cuts it tends to bring. There has been increasing specialisation of hospital work in the NHS, including the contracting out of hospital cleaning services. There used to be a presumption that this was cheaper and a more efficient use of resources. However there is widespread evidence that this has not been the case, as cheaper costs have been at the expense of pay, working conditions and service quality.

Contracting out and over-specialisation have encouraged what has been described as a two-tier workforce in the NHS. Health Minister Andy Burnham has himself described 'the distance between hospital cleaners and the rest of the NHS family'.<sup>80</sup> There are high turnover rates and high vacancy levels for cleaners.

UNISON found that outcomes for patients suffer when cleaners have no allegiance to the NHS and when there is a predominance of agency workers with short-term contracts and poor working conditions.<sup>81</sup> The costs are felt not only by cleaners, in the form of low pay and low status, but by all of us as a highly segregated workforce is poorly equipped to deliver the best outcomes in hospitals.

Attempting to disentangle cleaning contributions from overall hospital outcomes is almost impossible – cleaners are a fundamentally important part of the mix. We have therefore looked at just two discrete outcomes. Firstly, a reduction in Hospital Acquired Infections: we include how much this costs the NHS and an estimate of the costs to patients. Secondly, the contribution of cleaners to the wider social value created by the hospital.

On this basis, our research finds that we reward hospital cleaners very badly for what they contribute. For every £1 we pay them they generate over £10 in social value. This is likely to be an underestimation, as the entire functioning of the hospital relies on them. Nonetheless the case is clear; their contribution is greater than their reward.

## Myth 7: If we tax the rich, they will take their money and run

Orthodox economic theory suggests that people will choose to live and work where they stand to gain most in terms of personal finances.<sup>82</sup> Given the opportunity, the theory says, they will move from a high tax jurisdiction to a low tax one to keep a higher share of their pay.

Intuitively, however, we understand that decisions on whether to emigrate are far more complex than that. They depend on a multitude of factors beyond just the financial, including cultural familiarity, environment, proximity to friends and family, and quality of public services.<sup>83</sup>

If it were the case that higher taxes caused wealth to flee we would expect to see an exodus of the wealthier citizens of Sweden, Denmark, Norway and France – the countries with the highest tax rates. A glance at the latest Forbes billionaires list<sup>84</sup> reveals that of four Norwegians on the list all live in Norway, the two Danes live in Denmark, five of the nine Swedes live in Sweden, and eight of the ten French live in France.

And at an aggregate level there is little evidence that higher taxes reduce national income and wealth. A nation's income is measured in terms of GDP. Adjusting for different population size, we might expect to see a reduced GDP per head in those countries, like Sweden, that have the highest tax rates. But GDP per head in Sweden is \$52,057 per year, significantly higher than the levels in the UK (\$43,089) and Germany (\$44,471) where taxes are lower.<sup>85</sup> What this suggests is that economic performance or prosperity is not adversely affected simply because of higher taxes.

## Myth 8: The rich contribute more to society

Some of the super-rich like to hide behind the myth that they contribute more to our society than the rest of us. Think of all the tax they pay, the argument goes, and their very visible charity donations.

In the United States the economist Simon Head has calculated that the average weekly wages of the bottom 80 per cent of the working population fell by 18 per cent from 1973 to 1995, while the pay of the corporate elite rose 19 per cent before taxes. This increase reached 66 per cent after the tax accountants had 'worked their magic'.<sup>86</sup> In the UK executive pay increases in the past decade have vastly outstripped those for employees, on top of which the rich pay proportionately much less of their income in tax than the poorest.<sup>87</sup>

Not only do the rich pay less tax, but they often form a powerful lobby to erode the tax base of the economy. They have supported the propagation of the misguided view that tax cuts are good for stimulating growth and even increasing government tax revenues. The Nobel Prize-winning economist Paul Krugman claims that this is not true in the context of the United States. The tax cuts of the Bush administration that disproportionately benefited the most affluent had disastrous consequences for the economy. They contributed to converting the \$230 billion surplus inherited by President Bush into a \$300 billion deficit.<sup>88</sup>

Rich people who avoid paying tax often justify this by referring to the inefficiency of public services. Some hide behind a smokescreen of high-profile charity donations. However, the rich actually donate less in relative terms to charity than the poor. The top fifth of households give less than 1 per cent of their income, while the poorest tenth give 3 per cent. In fact, inequality in income terms is echoed by unequal philanthropic giving.<sup>89</sup> It is as if the small-change contributions of the super-rich are merely a salve to a guilty conscience for some. Polly Toynbee has stated that "true philanthropy in the modern world is tax-friendliness: public acknowledgement that a reputable mechanism exists to extract money from those who have too much and give to those who have nothing".<sup>90</sup>

## The tax accountant

*'My name is Ronan Voight and I'm a specialist tax adviser. I've been in this game for over 20 years and have a client list as long as your arm. I have worked closely with ex-Inland Revenue and HM Customs and Excise Inspectors for most of my working life, so I do know what I'm talking about. My clients are mostly wealthy people who I assist to avoid paying tax. One client of mine just sold his business for over £1.2 million. I arranged for him to pay just £8,000 in tax'*<sup>91</sup>

### WANTED

Are you committed to helping the super-rich avoid paying their fair share? You need to understand tax law developments to ensure clients will remain in full compliance legally with all tax laws yet will pay the lowest tax lawfully possible. While you will not be as well paid as the people you serve, you will have the satisfaction of knowing that the taxman is not getting as much as he should either.

Salary: £75,000-£200,000 plus excellent benefits package

The role of tax accountant is a job that many young university graduates aspire to. Companies such as Deloitte and KPMG have large tax sections with attractively presented tax experts. However what these experts actually do, fairly explicitly, is help rich individuals and companies pay less tax.

The work of tax accountants is legal as long as they manage to stay on the 'right' side of the thin line between tax avoidance and tax evasion. As distinct from tax evasion, tax avoidance is the practice of legally using the tax regime to reduce the amount of tax payable. In reality the distinction between the two is semantics. As the former Chancellor Denis Healey once put it: "*The difference between tax avoidance and tax evasion is the thickness of a prison wall.*"<sup>92</sup>

The amount of money lost in tax avoidance can never be precisely calculated but it is estimated that £12 billion is lost from companies and £13 billion is lost from individuals each year.<sup>93</sup> In reality, however, every pound a tax accountant saves for a client is a pound that otherwise would have been collected by HM Revenue. In our model, therefore, we have calculated the 'opportunity cost' which that £25 billion represents. On one calculation, it could have covered the annual cost of a national system of universal child care and parental leave, which is £21.4 billion. This would have generated a total social value of £50 billion per year through reduced social problems.<sup>94</sup>

This doesn't take account of a range of other potential impacts. Christian Aid has calculated that the practice of shifting profits to dodge tax bills costs developing countries over £60 billion per year.<sup>95</sup> In addition there are other costs to our economy. Markets don't function efficiently when companies don't publish the effects of tax avoidance on their profits.

Determining the right amount of tax payable is a specialist skill and often requires professional support. In this report we are not referring to everyday accountancy tasks, which may play an important social role but highly paid tax specialists who help wealthy people and companies pay less tax. The amount of value generated by these activities is negligible. We have included their salaries as a value to them, and assumed that they pay some income tax. On our calculations, therefore, tax accountants destroy £47 in value for every pound of value created. Tax avoidance is effectively ignored by government. Instead government campaigns have hounded benefit claimants over fraud. The £25 billion lost every year through tax avoidance dwarfs the £900 million lost in benefit fraud.<sup>96</sup>

Tax avoidance has been legitimised by a burgeoning profession of tax accountants who support and encourage it, rather than challenging it. Not only is this morally questionable but it means that we are all losing out. No example highlights more effectively how we have got our priorities wrong.

## Myth 9: Some jobs are more satisfying, so they require less pay

Justifying low pay through a vague concept of job satisfaction is a dangerous approach. Factors affecting job satisfaction are complex, and not determined by occupation alone. Levels of reported job satisfaction are influenced by a range of factors such as autonomy and control in the workplace, levels of income, incentive pay and bonus schemes, and the extent of opportunities to do work-related training.<sup>97</sup>

Workers in the public sector report higher levels of job satisfaction than those in the private sector. But the gap between the two has been closing. Satisfaction levels in the public sector declined especially sharply during the 1990s.<sup>98</sup> This coincided with the introduction of private-sector and market disciplines into the public sector.

If we take at face value claims that big earners get paid well to compensate for stress and long hours, then we would expect other highly stressful or dangerous professions to be highly paid. Fishing is the most dangerous job in the UK, with roofers and scaffolders also near the top of the list and refuse collectors at number 18.<sup>99</sup> Yet none of these professions are highly paid.

Perpetuating this myth has consequences for the rest of our society, because of the relationship between pay and status. It sends damaging signals about what we care about in society, and confers low status on some of the most important jobs.

The fact that some of our brightest university-educated minds are competing fiercely for jobs in advertising and investment banking, while there are high vacancy rates for nurses and social workers, suggests resources are not being directed to best use. The fact that people find work with a social purpose rewarding may be a reflection of the positive impacts of these occupations on society as a whole. Workers should therefore be rewarded, not penalised, for doing this kind of work.

## The waste recycling worker

### WANTED

Hardworking individual required. Must be fit and healthy and capable of hard physical labour. Duties include driving a 7.5-tonne truck on collection rounds, picking up materials from sacks or wheeled bins (may involve heavy lifting), warehouse duties which include unloading trucks, using a forklift truck, using baling and shredding machinery. Your commitment to environmental issues will offset the unpleasant nature of the work and the early morning starts.

Salary: £6.10 per hour.

The collection of waste from individuals and businesses is a job that is often taken for granted. We pay the people who do this low wages, and the job they do has lower status than the vast majority of employment in our society. However, when people stop collecting the rubbish society breaks down. The Winter of Discontent, in 1979, is memorable for images of overflowing bins and piled-up rubbish, even occupying Leicester Square. Those days were brought to mind again during recent industrial action in Leeds.

We have included in our analysis a profession that deals with the waste our economy produces, focusing on the contribution of a recycling worker. There are limits to what can be achieved through recycling but what we do with waste is important. Critics of recycling often claim that it may have little or no benefit to the environment due to the amount of energy used in the recycling process. However large-scale life-cycle analysis by the Waste and Resources Action Programme (WRAP) found that between 10 and 15 million tonnes of carbon are saved through recycling in the UK each year.<sup>100</sup> A large proportion of the UK's recycling is done by local authorities. This work involves hard graft, and has high injury and accident rates.

The costs of disposing of what we no longer need go beyond the problems created by landfill. In reality, we never really throw anything away. A modern glass bottle would take 4,000 years to decompose<sup>101</sup> – and even longer in landfill. This is wasted potential. In our model we have tried to estimate how people value the products that are recycled. To capture this we have looked at the waste recycled by a typical worker for a small firm called Aardvark Recycling. Aardvark distributes the compost it produces to schools, allotments, community groups, growing groups and residents' gardens.

The alternatives to recycling are not appealing. Landfill sites are unpopular with local residents and account for nearly half of all UK methane emissions. In total our model estimates that for every pound paid to a recycling worker over £12 in social value is generated. This includes:

- Cutting the social cost of carbon emissions (which are reduced through recycling)
- Reducing the disamenity or 'local nuisance impacts'<sup>102</sup> from living close to a landfill site
- The contribution of the recycling industry towards GDP
- The reuse value of recycled goods.

Even if we exclude the estimates we made of reuse value, the ratio is still over £11 for every pound spent.

## Myth 10: Pay always rewards underlying profitability

*'You have to realise: if I had been paid 50 per cent more, I would not have done it better. If I had been paid 50 per cent less, then I would not have done it worse'*

**Jeroen van der Veer, former Chief Executive, Royal Dutch Shell<sup>103</sup>**

The perceived wisdom is that high pay for senior corporate executives reflects high performance and company profitability. Executive pay has rocketed over the past decade as shareholders have accepted the argument that company performance requires top talent, and that top talent commands a very high price.

A parliamentary report on executive pay and severance deals<sup>104</sup> cited research showing that between 1993 and 2002, the median base salary for the highest paid directors rose by 92 per cent, while inflation rose by 25 per cent and average pay by only 44 per cent. This trend has continued since then. Five years ago the top ten UK executives banked some £70 million, but by 2007 they had doubled their take-home pay to £140 million. They were paid significantly more again in 2008, when their income rose to £170 million. The upper limit on bonuses also rose from an average of 40-60 per cent of salary in 1998 to 100 per cent of salary by 2003. Meanwhile the parliamentary report highlighted a lack of evidence that performance standards had toughened to reflect higher pay.

It is becoming increasingly apparent that there is only a weak correlation between pay and executive performance. In 2008 Britain's top companies lost almost a third of their value, as the FTSE plunged amid the onset of the deepest recession in living memory. But at the same time the chief executives of these companies saw a leap in their basic salaries of 10 per cent in the year. Although bonus payouts were lower than before, basic pay for this elite group increased more than three times the 3.1 per cent average pay rise for ordinary workers in the private sector.

Companies have been quick to impose pay freezes on staff and to implement redundancy programmes to lower costs, but directors' basic pay increased by more than double the rate of inflation.<sup>105</sup> Public outrage at bankers' pay didn't stop many of the chief executives of failed banks getting fat severance deals. West Bromwich Building Society had a loss of £48.8 million in the financial year ending in March 2009 but paid its former boss, Stephen Karle, a staggering £520,600 pay-off.<sup>106</sup> Lehman Brothers paid \$24 million in severance packages to the collapsed firm's top three London executives as 4,500 London staff were ordered to clear their desks.<sup>107</sup>

The understanding that executive pay relates little to corporate performance is not new. Empirical studies corroborating this finding include those conducted by Harvard professors Bebchuk and Fried in 2004.<sup>108</sup> They argued that executive pay arrangements were intended to benefit the financial interests of managers, not shareholders. They believed that shareholders, often pension funds representing the average worker's future financial welfare, were captive to executive influence on this matter.

# Conclusions

This report challenges a host of economically and socially damaging myths about pay and value. Chief among them – and the point of our research – is the idea that there is a straightforward relationship between high financial rewards and good societal outcomes. As we have seen, this simply is not the case.

Our Social Return on Investment analysis is not just an intellectual exercise – it has big implications for the way in which our society and economy are structured. Financial incentives are very powerful, and we tend to shower them on some of the professions that are the most socially and environmentally costly. This promotes undesirable behaviour, while positive activities are discouraged.

We have not aimed for precision in our calculations – there may be aspects of value that were left out. The point was to draw attention to the issue. We have not included detailed recommendations because it is clear to us that there are deep structural issues that need to be addressed, and change will not come overnight.

This does not mean that governments are powerless. Much more needs to be done to reduce inequality, and the focus of policy needs to be at the top of the income scale. There has been little or no political appetite for reining in high pay and this reflects a systemic malaise and complacency that have created a climate for market failure. It is time to learn the lessons of that failure, and to challenge high rates of senior executive pay.

It is important to separate out the professions we have examined from the people actually doing the work. This is not about picking on individuals, and many of those in the highly paid professions discussed may be very good people. We recognise that it is the institutions and systems that promote self-interested behaviour, and it is these institutions and systems that need to change. Most people are simply responding to incentives, so we need to ensure that the incentives on offer align with the social and environmental value that our economy needs to deliver.

## Some policy recommendations

- **End the policy silence on high pay.** nef has previously advocated a national maximum pay differential. This has been echoed recently by Compass and others with calls to establish a High Pay Commission. Its task could be to examine what the appropriate differentials should be. The Royal Navy, for example, has had a de facto differential of eight, whilst some Japanese firms voluntarily impose pay ratios limiting the gap between the top and bottom pay. Determining these multiples should be informed by the concept of social value creation.
- **Learn from the successes of anti-discrimination legislation.** Explore the possibility of positively discriminating towards people from low-income backgrounds to level the playing field in access to highly paid professions.
- **Build social and environmental value into prices.** Until goods and services reflect the real costs and benefits of their production, incentives will be misaligned with the kinds of positive behaviours society wishes to promote. Getting the prices right would affect relative profitability and so would align what wages could be paid with the value that is created. Consumption and corporation tax are two vehicles for doing this, but they need to be applied in a progressive way.

- **Introduce more progressive taxation.** The wealthiest do not pay their fair share of tax and the very wealthy may pay none at all. Redistribution, particularly of assets and land, is an effective way both to offset inequality and to reward jobs that the market does not. Closing tax loopholes would also be a good place to start.
- **Launch a green industrial policy.** We have an unprecedented opportunity to make environmental progress while also addressing wage inequality. The time has come for a new industrial policy, creating green jobs to replace the middle-income, semi-skilled jobs that have been wiped out in manufacturing.
- **Encourage new forms of ownership.** Mutually owned building societies, co-operatives and land trusts are all models in which ownership takes a more collective form, and benefits are more evenly shared.
- **Radically reform the role of the City.** It is time to return finance to its role as servant, not master of the economy. Instead of a monoculture of mega-banks deemed too big to fail and answerable only to the demands of private shareholders, we need a range of different financial institutions that are focused on social value creation. Initiatives such as a financial transaction tax would also reduce the harmful effects of trading.
- **Invest in universal child care and paid parental leave.** Child care provision in the UK often reflects and reinforces socio-economic and gender divisions. Making high-quality, affordable care available to all gives parents – particularly women – a better choice over returning to work and provides children with greater equality of opportunity. Extending parental leave, especially to fathers, would be a further investment in positive child development for the benefit of society.<sup>109</sup> These provisions could be entirely met by recouping the money lost to society through tax avoidance by the wealthiest. This valuable investment would also increase gender equality by improving career options for women.

# Appendix 1 – General note on method

This research has been inspired by a methodology that was developed to account for value, called Social Return on Investment (SROI).<sup>110</sup>

SROI is a method for measuring and evaluating the consequences that follow from the work of people and organisations. This is value not only in the conventional economic sense, but also in environmental and social terms – taking environmental degradation into account, for example, or changes in the well-being of individuals.

SROI aims to capture as wide a range of outcomes as possible. By aggregating the value of all of these changes, it is possible to compare their magnitude to the size of the investment. The end result is an SROI ratio, which tells us how much social value is created for each pound invested. This is the measure of how effective the work is in creating beneficial changes for everyone involved.

The case studies presented in this report did not involve full SROI analyses of the jobs featured. Instead they were informed by SROI techniques and principles. The principles were used and adapted in the following way:

- We took a multi-stakeholder approach, looking quite widely at the groups affected by the activities described. Because of time and resource limitations, we did not talk to those stakeholders ourselves. Instead we relied on existing data.
- Our analysis was based on outcomes from activities – both positive and negative. These were the things that we valued.
- We valued the outcomes that mattered most – the things that emerged from the research as having the most impact.
- We only included things that were material. These analyses are partial, and we were not aiming for exact findings. However, we are confident that we have included the most material outcomes.
- We have been transparent in how we have approached the calculations, so that the reader can follow our logic. A detailed description of each is available in Appendix 2.

As mentioned, there has been an attempt to include both positive and negative outcomes in this research. However, with the low paid jobs it was not clear to us that there were negative, material consequences. In addition, as there were no discernible wider positive impacts from the accountants' work, we have only included a value to them of receiving their salary.

## Appendix 2 – Technical appendices

This Appendix explains in more detail our methodology for quantifying the SROI value of the six professions we studied.

### City banker

Our model assumes that the financial crisis and recession would not have happened were it not for highly paid City bankers and traders engaging in extremely risky, opaque and complex transactions. We attributed the entire measurable loss to the UK's economy and public finances to an elite few thousand very highly paid financiers – those earning over £1 million in bonuses. The model balances this value destroyed with the value created during a 20-year indicative career in terms of these financiers' contribution to UK economic activity, taxes paid, and jobs supported.

To measure the loss to the UK economy, a comparison was made between the IMF's April 2008 and October 2009 forecasts for UK GDP through to 2014. We added to this an adjustment to reflect a loss of 5 per cent of UK economic capacity between the onset of the crisis and 2020.<sup>111</sup>

In its *World Economic Outlook*, published in October 2009, the IMF estimated that the UK's general government net debt will rise to 91 per cent of GDP by 2014. To calculate a cost to the UK public finances, we compared the IMF estimate with the Treasury's 2006 Budget Report, which was published prior to the crisis. This expected net debt to stabilise at 38.5 per cent of GDP. We included an allowance for debt servicing costs on the additional debt incurred.

The resulting sum of £2.7 trillion of value destroyed, or £668 million attributable to each highly paid financier, is likely to be an under-estimate. It does not take account of the costs to individuals and communities of jobs lost as a result of the recession, the long-term costs of much higher youth unemployment, and the costs of public spending cuts that will inevitably have to be made. It is also worth noting that a comprehensive account of value destroyed would factor in a cost to the global economy and society, not just to the UK. Such an account is beyond the scope of this report.

For a best estimate of value created, Office of National Statistics figures for gross value added (GVA) revealed that on average over the past decade financial intermediation in Inner London contributed 2.5 per cent to the nation's GVA. It would not be appropriate to attribute all of that contribution to the highest paid financiers, since it includes a range of value-creating activities. A share of 50 per cent was attributed to our target group, based on an indicative share of trading activity within banks' total revenues of around 50 per cent.

Tax contributions from the UK finance sector were obtained from the University of Manchester.<sup>112</sup> It was not possible to calculate an exact split of that contribution into wholesale and retail finance services. As an indication, however, the latter employs somewhere in the region of five times as many people as the former. We therefore divided total tax paid by the finance sector into contributions from retail and wholesale finance according to a ratio of 5:1.

We cannot attribute the whole of the tax contribution from wholesale finance to the most highly paid City bankers. As a conservative working estimate, we allowed for 50 per cent of the tax receipts from wholesale finance to be attributed to these City bankers.

A figure of some 200,000 jobs supported by financial intermediation services was obtained from City Research Focus (2008 data). An average net income value of £35,000 was applied to each job. This equates to an average London salary of £50,000 but the employee-related tax is accounted for in total tax paid by the finance sector as described above.<sup>113</sup>

As with the economic value generated, a share of 50 per cent of the overall benefit of jobs supported was attributed to the target group of top financiers. We also displaced this benefit by 50 per cent to allow for the fact that many of these employees could have worked elsewhere. This is significantly less than the 80 per cent figure that would be used in a standard cost-benefit analysis of employment generation.

Calculations based on the above measures revealed an overall position in which each of the highest-paid City bankers may be held to account for £33.4 million of value destroyed in Britain for every year of a 20-year career. This compares with an estimate of £4.71 million in value created each year. That balances out at £7 of value destroyed for every £1 of value created.

### **Nursery worker**

The immediate benefit from child care providers for the adult population is to allow parents to work, to earn income and to support their families. Further benefits include higher productivity in the economy as a result of an expanded workforce, higher tax receipts and lower welfare payments, more choice for employers from a bigger pool of workers, and enhanced gender equality in work and in the home. For our calculations we focused on released parental earnings as a result of access to child care. As a result our calculation is conservative because it does not measure the value of the further benefits listed above.

As a working average, we assume that each place in child care will allow for one average annual wage to be earned by a parent. This would be achieved either by one child attending full time, or two children attending part time. The model takes as an average a ratio of one child care worker to five children but we include a reduction to allow for some of the children being siblings (because siblings are involved, a portion of the income parents are able to earn must be shared across the care of more than one child). A further reduction in value attributable to one worker allows for some of the value created being attributable to the infrastructure provided by the nursery or child care centre.

Taking account of these factors, the calculations show that on average one child care worker creates value of some £78,347 per year against an indicative salary received by the worker of just £12,500. We have added to the created value the salary received by a child care worker, to express the value to these workers of their employment. This increases the total value created to £90,847. This means that for every £1 paid to a child care worker, s/he generates more than £7.20 in value.

As well as allowing parents to work, good child care and early-years education benefits children themselves. This applies most of all to children from deprived backgrounds. Research indicates that good-quality early-years child care for children from deprived backgrounds impacts positively on social skills and motivation. It also improves the chances of subsequent educational success and higher lifetime earnings (with positive future impacts for the economy). Furthermore, it lessens the risk of compromising outcomes during adolescence and adulthood (such as teenage pregnancy and involvement in crime). This means that the value created by access to good-quality child care can extend to reducing the costs to society of remedial programmes in school, social problems including crime, and future welfare support.

A recent report from Action for Children and **nef**<sup>114</sup> found that UK and Scandinavian levels of public spending on families and children were broadly comparable. But the cost of social problems in the UK was over 3.5 times that in Finland (when adjusted for population size).

The report suggested that how children fare across a range of social and economic indicators may rest not so much in what countries spend as in the way they spend it. The UK devotes a disproportionate amount to means-tested payments, as opposed to universal provision of services such as childcare. A review of the social and family policies of Scandinavian countries found that universal provision of childcare and parental leave was crucial for achieving better outcomes.

An examination of the potential should universal child care be made available in the UK, together with funded parental leave, found that there was a net return available of £612 billion over 20 years. That's equivalent to an annual net benefit of £30 billion.

For the purposes of estimating the additional value that a child care worker could offer to UK society, we assume that half this potential net benefit of £30 billion would accrue from universal child care provision. The *Backing the Future* report calculated that for the UK to deliver universal child care, some 565,000 workers would be required. The resulting potential value per worker would therefore amount to £27,090 per year. Adding this sum to the value of released parental earnings calculated above yields a total actual and potential value per child care worker of £117,937 every year. Viewed against the £12,500 indicative wage, that means £9.43 in value created for every £1 in wage costs.

### Advertising executive

The calculations for the advertising executive centred on the notion of overconsumption – that we consume more than we need and that this has damaging environmental and social impacts. We considered the pivotal role that the advertising industry plays in promoting consumption.

In our model we began by estimating the amount of unessential consumption that takes place in the UK each year. To calculate essential consumption, we took the Minimum Income Standard (MIS) developed by the Joseph Rowntree Foundation. This put a value on the level of income people think is needed to afford a socially acceptable standard of living in the UK today, and to participate in society.<sup>115</sup> We compared this with what households actually consume – 55 per cent of domestic output – and arrived at a figure of £172 billion.

Next we identified what proportion of this was due to the advertising industry. This was challenging, as it was difficult to measure. Although £18 billion is spent on advertising, this includes spending on media space. A conservative figure for the amount spent on advertising itself is the billings of the top 100 advertising agencies, which total £6 billion per year.<sup>116</sup>

Ad agencies themselves promote the amount of additional spending that is attributable to them, and this varies from 1:4 for de Beers to 1:9 for Danone.<sup>117</sup> We took an average but conservative figure of 1:5, which means that £30 billion of overconsumption – or 17 per cent – is due to advertising. This allowed us to calculate advertising's share of the costs associated with over-consumption. We identified four categories of costs: environmental (resource depletion and climate change), obesity, anxiety-related mental health and indebtedness.

First, let's take the environmental costs. All of the carbon costs associated with overconsumption (108 million tonnes by our calculations) can be assumed to be unnecessary and therefore negative. We have valued these using Lord Stern's valuation of £51 per tonne.<sup>118</sup>

We then took account of the proportion of goods and services produced domestically (80 per cent).<sup>119</sup> We know that the 20 per cent of goods and services consumed that come from overseas have a far bigger carbon footprint. For example, one study estimates that the carbon embodied in imports from China is 96 million tonnes plus another million tonnes in shipping costs.<sup>120</sup> Adjusting for the contribution of advertising and valuing, we arrive at a total climate change cost of £5.2 billion.

There are also substantial resource depletion implications. In 1997 an environmental economist, Robert Costanza, valued the ecosystem of the world at \$33 trillion.<sup>121</sup>

This was controversial then, as now. But the point he was making, which still holds, is that this was twice the GDP of the planet, or one seriously large externality. To make this cost visible, we have used this number, adjusted for GDP growth since then, and converted it to sterling. This produces the figure of £38 trillion.

Of this amount 4 per cent is being consumed by the UK if we use GDP as a proxy. Not all of this consumption is sustainable, however – the planet cannot renew itself above a particular rate of consumption. According to WWF the UK is currently consuming three times what the planet is able to renew by itself.<sup>122</sup> As advertising accounts by our calculations for 17 per cent of overconsumption, we have taken that as advertising's share of non-renewable overconsumption and arrived at a value of £85 billion.

For our social costs we have taken advertising's share of the social cost to the UK of obesity (£17.4 billion<sup>123</sup>), anxiety-related mental health (£11 billion<sup>124</sup>) and indebtedness (£67.4 billion<sup>125</sup>). The indebtedness figure includes servicing debt and repayment of principal borrowed in any one year but does not include the wider costs of indebtedness. We have not stripped out housing debt, as much of this could be attributed to overconsumption and speculation. The total cost for these to advertising is £16 billion.

We have also looked at the positives. First, 17,000<sup>126</sup> people are employed in the advertising industry, and we have given each an annual salary of £30,000. We have reduced this by 50 per cent to account for the fact that many of these people would have found jobs elsewhere if they did not work in advertising, so this is displaced value. These figures represent gross salaries, so income tax contribution is also included.

Then there are the corporation tax contributions, which we have taken as 28 per cent of the reported profits. The overconsumption that is domestic also provides jobs for people. We have calculated this by taking the returns to workers from GDP (approximately 50 per cent) and netting that off as positive. We have used the same method to calculate the corporation tax paid on overconsumption.

We have weighed all the costs incurred by advertising professionals, which amount to £1.2 million per person, against a benefit of £370,156 per person. The result is that for every £1 of positive value, £11.50 of negative value is generated.

### **Hospital cleaner**

We have taken the baseline measure for the value created by the hospital cleaner as the prevention of the spread of hospital-acquired infections (HAIs). This has been estimated by a study published in the *British Medical Journal* (*BMJ*<sup>127</sup>) that looked at the effect of an additional cleaner on the hospital ward. The study used empirical evidence to compare the effects on two different wards.

The *BMJ* study performed a cost-benefit analysis, enabling the researchers to estimate that each cleaner potentially spared five to nine patients MRSA. This study should be treated with caution, but for our purposes it does provide an estimate of infection prevented. The average cost of one hospital-acquired surgical site infection (SSI) caused by MRSA is estimated at £9,000.<sup>128</sup> This points to annual savings of between £45,000 and £81,000. We have used the midpoint of these savings in our calculations.

It should be noted that this gives the savings to the NHS but does not estimate the cost to patients of staying in hospital longer and in some cases dying in hospital due to contracting MRSA. To estimate the costs to patients we used Health Protection Agency<sup>129</sup> figures of the proportion of death certificates that state MRSA as the sole cause of death, divided by the number of reported case of MRSA in total, to give an estimate of the lives saved by cleaners. We didn't attribute this fully to the role of a cleaner and this gives us a very conservative estimate of less than one life saved per annum per cleaner. Valuing life raises a number of ethical issues, and different studies have placed an annual value of anything from \$60,000 –to \$129,000 on each life.<sup>130</sup> We have used a nominal mid-range figure of \$100,000, which at present exchange rates is £63,000.

In addition to the savings to the state from reduced infections, it is important to consider what each cleaner contributes to the working of the hospital in general. It is widely acknowledged that cleaners play a role in patient care. All in all, a hospital could not function without them. To estimate this we used statistical analysis that examined the role of insurance in relation to mortality rates in the United States. We used this analysis to approximate the value of UK hospital services, estimating that without hospital treatment there would be approximately 127,273 additional deaths.

Estimating that there are approximately 27,226 cleaners in UK hospitals, we arrive at a value of £128,344 per cleaner. This gives a ratio of over £10 of social value created per £1 spent on wages. Even if we only look in isolation at the estimated saving from having fewer cases of MRSA, this gives a value of £63,000 in savings to the NHS per cleaner – or £2.30 in social value for every £1 spent on wages.

### **Tax accountant**

The Tax Justice Network has devoted resources to estimating the loss to the Exchequer of tax avoidance by individuals and corporations in the UK. Their finding was that £13 billion and £12 billion respectively are foregone in tax receipts.<sup>131</sup>

There is clearly an opportunity cost in terms of foregone public service value that could accrue to society from having this revenue available. A convenient proxy for that value is the potential gains to society from universal child care and parental leave in the UK, as calculated in *Backing the Future* by Action for Children and nef.<sup>132</sup> For an average cost of £21.4 billion a year for 20 years, which could be met from the £25 billion of tax avoided, it was found that universal provision of child care and parental leave could deliver value to society of £50 billion per year.

As advised by the Tax Justice Network, the best estimate of the number of tax accountants delivering tax savings to their wealthy customers is 14,000. This comprises the membership of the Chartered Institute of Taxation. With 14,000 tax accountants, each on average prevents the accrual of an indicative £3.6 million per year (reflecting each individual's share of the £50 billion per year above).

The value created from tax accountancy is simply assumed to be the number of jobs supported in the sector. On average tax accountants earn a salary of some £75,000. Assuming that all of this comparatively high salary is a proxy for the value created by the sector, then a simple calculation reveals that for every £1 of value created, £47 is destroyed.

### **Recycling worker**

Recycling plays an important role in combating climate change. The alternatives, such as landfill, are costly. According to the UK Greenhouse Gas Inventory, landfill activities accounted for 3.2 per cent of UK emissions in 2007. However, calculating the carbon benefits from recycling is not straightforward.

To estimate the environmental benefits of recycling the Waste and Resources Action Programme (WRAP) used Life Cycle Analysis. This included looking at the environmental impact categories of resource consumption, global warming potential, other energy-related impacts, toxicity potential, waste generation and other factors. Although the study reported variation in different recycling techniques, overall WRAP found carbon savings of between 10 and 15 million tonnes.<sup>133</sup> Other studies give higher estimates.<sup>134</sup> We took a mid range figure of 15 million. Although this is a broad-brush figure, it gives some estimate of the carbon savings in the UK. It does not include all recycled products, and we have adjusted the number of workers to reflect this. We have valued the carbon saving using Lord Stern's valuation of £51 per tonne.<sup>135</sup>

Although landfill costs are a significant burden on local authorities, we have not included cost savings from landfill tax. This is because the benefits from reduced carbon have already been included. However, it is also necessary to include the 'disamenity' effects of landfill. People dislike living near landfill sites and

are willing to pay more for housing if it means they can avoid living near one. We have taken a value from research by Cambridge Econometrics for Defra<sup>136</sup> of £2.18 per tonne. Based on the annual amounts of paper and glass recycled each year, this gives a total saving of over £20 million.

The large contribution made by the recycling industry to the economy is often overlooked. The market value per employee in terms of Low Carbon and Environmental Goods and Services (LCEGS) measurement is £121,000,<sup>137</sup> well above the national average of £54,400. Given that environmental challenges and issues play an increasingly large part in everyday life, this industry sector is set to expand. It will support sustainable employment in the years to come, while other areas are likely to decline. In our model we used the contribution of recovery and recycling workers to GDP which is estimated at just over £6 billion.<sup>138</sup>

There is something else that recycling workers do that is not captured by looking at contributions to GDP. Consigning products to landfill creates costs that are additional to the carbon emissions generated in terms of wasted potential and wasteful use of resources. A glass bottle takes 4,000 years to decompose. Recycling workers help to reduce such costs.

In addition, some recycling organisations maximise reuse value by contributing to other community and social activities at the same time. Previous **nef** research<sup>139</sup> has modelled the benefits of third-sector involvement in waste management. It showed, for example, how projects could generate improved human capital through volunteering, training and employment.

To try to capture some of the reuse value of the products recycled, we have looked at some of the typical benefits an individual recycling worker would produce. A small local recycling company, Aardvark Recycling, recycles green waste into compost and also recycles paper and glass. The compost is distributed among local food-growing groups. We have modelled the benefits of compost to include the benefits from locally grown food, although we have only attributed a small amount of this to the recycling worker. This gives an additional value of just over £20,000 per worker. Although this estimate is very rough it is intended to try and capture some of the value of resource efficiency.

The total value created per recycling worker is £151,151.79 if you look at reduced carbon emissions and contribution to GDP. If you include resource efficiency estimates this goes up to £171,941.39. If you take the average wage of a recycling worker at £13,650, this is a ratio of over £12 in value created per £1 in salary paid. If we exclude the reuse value of goods then the ratio is still over £11 for every £1 in salary paid.

# Endnotes

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# One of the other things we do



The [centre for well-being](#) at **nef** (the new economics foundation) aims to enhance individual and collective well-being in ways that are environmentally sustainable and socially just. Set-up in 2006, the centre builds on **nef**'s established well-being programme and significantly expands our work in this area.

Our aim is to promote the concept of well-being as legitimate and useful aim of policy and to provide individuals, communities and organisations with the understanding and tools to redefine wealth in terms of well-being. We believe it is possible to lead long and happy lives without costing the earth.

We advance thinking in this area by undertaking policy-relevant research and consultancy, by measuring well-being and the factors influencing well-being, and by providing the training and tools for others to assess and positively influence well-being.

We undertake pioneering work on psychological well-being, capturing how people feel and how they function, as well as working simultaneously on environmental, social, and economic well-being to deal with the conflicts and trade offs between them.

To find out more contact us at [well-being@neweconomics.org](mailto:well-being@neweconomics.org) or visit [www.neweconomics.org](http://www.neweconomics.org)

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