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Rt Hon Leon Brittan QC MP
Secretary of State for the Home Department
Home Office
Queen Anne's Gate
LONDON SW1

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COMMITTEE OF ENQUIRY INTO PROPOSALS TO AMEND THE SHOPS ACT

Thank you for sending me a copy of your letter of 16 November to Tom King, enclosing a copy of the Committee's report. I have also seen a copy of your letter of the same date to Willie Whitelaw.

I agree that the role of Wages Councils needs to be handled carefully. I therefore think we should try to separate this issue as much as possible from the rest of the report, as a question which needs to be considered in a wider context. We should be able to defend this approach - not least because the Committee in putting forward its recommendation on Wages Councils was, on its own admission, exceeding its terms of reference. But in any case, I do not find the reasons which the Committee adduces for its concern compelling. I understand that the two relevant Wages Councils cover less than half the total employees in retailing and that many of the major chains pay minimum wages above the Wages Councils' minimum.

The study by Home Office and Department of Employment officials of alternative means of protection for employees if the Wages Councils are abolished is clearly necessary. I should be grateful if Treasury officials could be kept closely in touch with the work. (Nick Monck is the Deputy Secretary concerned here.) I am sure it would be wrong to start with the presumption that some protection would be needed. Employee protection measures generally impede the flexible working of the labour market and we do not want to find ourselves proposing them simply to buy off the anti-deregulation lobby. But I am sure you and Tom King will have this point well in mind.

You also mentioned the IFS study. Economists here have examined this and produced a paper which I am enclosing. You will be

particularly interested in the first six paragraphs which set out the main economic consequences they think likely to stem from deregulation. You will see that they are expecting an early gain in employment and better use of resources in the longer term. I am sure these points are well worth emphasising.

I am sending a copy of this letter and the appraisal of the IFS review to the Prime Minister, the members of H Committee, the Secretary of State for Trade and Industry and the Minister of Agriculture and to Sir Robert Armstrong.

NIGEL LAWSON

THE ECONOMIC EFFECTS OF DEREGULATING SHOP HOURS

Deregulation of shop hours would constitute a major relaxation in the regulations affecting retailing, and would be the most significant change in them since the abolition of Resale Price Maintenance in 1964. The most obvious result would be the increase consumer choice over time of shopping, but the economic review carried out by the Institute of Fiscal Studies (IFS) suggests that there will also be gains in terms of lower prices and greater efficiency from deregulation.

2. The main economic consequences are likely to be:-

- about a half retail capacity (by turnover) is likely to open on Sundays; Sunday opening and extended hours will be concentrated in particular locations.
- in the short run this will lead to additional jobs in retailing. Additionally (not covered in IFS report) greater flexibility in shopping hours will increase flexibility in other parts of the labour market; workers will no longer be deterred by difficulties in finding shops open in the evenings and on Sunday.
- at unchanged wage rates earnings of employees will rise - perhaps by as much as 2½% - as Sunday and evening working increases and weekday working declines. Deregulation of wages could decrease the size of this gain but will not eliminate or reverse it.
- although costs will rise in the short term, competition will keep prices down.
- in the longer term, greater competition will lead to greater efficiency and lower costs. There will be a 10% increase in capital productivity and an increase of about 1% in labou productivity. As a result prices are expected to fall, reducing the RPI by about ½%.

3. While the IFS stress the uncertainty surrounding their projections, and point out that the effects are small in relation changes already under way in retailing, it nonetheless appears th deregulation will bring considerable gains both to consumers and employees.

4. The gains to consumers are twofold: lower prices and greate choice. IFS argue that, while retailing costs will increase in

short term, before capacity reductions take place, competitive pressures in retailing will result in these being taken up by reduced margins rather than by higher prices. In the longer term, as the least profitable outlets close, or to curtail expansion plans, costs will fall below even their present levels both because existing stores will be using capital more intensively (opening for longer hours) and because the current trend to larger, more efficient, stores will be reinforced. As a result of these cost reductions, net margins would be restored at a lower price level. The overall reduct in costs would be of the order of £½ billion (at current prices) and would reduce the RPI by about 0.4 per cent.

5. The second effect on consumers would be greater choice about when to shop. Surveys carried out for the IFS suggested that around 30 per cent of people would like to shop on Sundays, with particularl high demand from those in full-time employment, and in areas where th was a high proportion of working women. IFS project total sales on Sundays of 7 per cent of total retail sales, with about half of retai outlets (by turnover) opening. The long term reduction in retailing capacity would, of course, reduce consumers' choice about <u>where</u> to shop; but changes already taking place in retailing suggest that consumers are more concerned about prices and hours of opening than the total number of outlets.

6. The gains for employees are perhaps less clear cut, but noneth less appear to be real. The immediate effect of Sunday trading woul be to increase the number of jobs in retailing. Experience suggests that there would be a high proportion of part-time jobs, with some people working only on Sundays, thereby increasing significantly employment opportunities for young people or married women unable to work on weekdays. In the medium term, weekday employment will fall line with the reduction in weekday sales, leaving a small net addit to total jobs (but small reduction in full time equivalents). As capacity is reduced, there would be further job losses of about 20, (1 per cent of total retail employment), largely concentrated among managers.

7. At present, double time is generally paid on Sundays in line with Wages Council rates. Retail earnings consequently increase wi

Sunday trading, even in the medium and long term. IFS project a total increase in earnings of £250m, 2½ per cent of the present total. At a premium of double time, experience indicates that demand for Sunday jobs exceeds supply; indeed Asda is able to get sufficient Sunday labour at a premium below the Wages Council level. This suggests that, were the Wages Councils to be abolished, the market would establish a premium for Sunday working below the present level. IFS have calculated the effects of a premium of time and a half: Sunday opening would be more extensive (86 per cent by turnover), and the long term reduction in capacity would be greater, but the effect on prices and on employment would be very similar. If anything, as would be expected, employment would be slightly higher if the premium was reduced.

8. IFS do not consider the possible level of the "market" premium for Sunday working, nor whether abolition of the Wages Councils would lead to lower wages on weekdays. However, it should be noted that less than half total employees in retailing are covered by the two Wages Councils, while many of the major chains pay minimum wages which are above the Wages Councils' minima. Moreover, the main job losses following deregulation would be among managers rather than the lowest paid shop assistants.

9. Most of the numerical conclusions reached by the IFS are based on their Retail Cost Model, which is as yet not documented. It is therefore not yet possible to assess whether this has been soundly constructed. However, the qualitative conclusions drawn by the IFS about the nature of Sunday trading do seem to be supported by experience in other countries where Sunday trading is legal. In Sweden, for example, Sunday opening is concentrated in the Stockholm area; food sales are lower than sales of household goods; and few clothing shops open. According to the 1977 Report on the Committee on Business Hours, deregulation did not lead to an increase in the overall price level, despite double time being paid, while firms appeared to have no problems recruiting staff.

10. It should be emphasised that the approach adopted by IFS was to compare a situation where no illegal trading took place with deregulation. There is already a considerable amount of illegal

trade, especially in those areas like DIY (included in the "household sector) where conditions were found by IFS to be most favourable to Sunday opening. (For instance, 63 of 109 B & Q outlets are open on Sundays, and a further 30 have been closed under threat of proceedin Only 16 are closed by commercial decisions.) Consequently some of the changes projected by the IFS will already have occurred, but it is impossible to be sure how far these changes have gone.

11. As the IFS stress, the projections in the economic review are subject to a wide margin of uncertainty. The speed of change is als uncertain: it is likely that in some areas, particularly in London and the South East, moves to Sunday trading could occur quite quickl after deregulation. In other areas, the spread of Sunday trading would be much slower. However, the conclusion that deregulation wil have generally beneficial economic effects appears to be robust.

THE REGULATION OF RETAIL TRADING HOURS - ECONOMIC REVIEW BY THE INSTITUTE OF FISCAL STUDIES

Introduction

The IFS Review considers the effects of removing restrictions on trading hours on the structure of the retail industry, on retail sales, on prices and on employment and earnings. This Annex explains briefly how the IFS examined these questions and summarises their conclusions.

Background

2. The retailing sector has experienced dramatic changes since the Second World War. Increased ownership of cars, freezers and refrigerators, changes in population distribution, the growth of TV advertising and the greater number of working women have all contributed to changes in shopping habits, while the pattern of purchasing has changed with increased real incomes.

3. One major change has been the increase in store size, which has accelerated with the development of out-of-town superstores. This has accompanied a fall in the total number of outlets, predominantly among Co-ops and independents. Retailing preferences and habits can be changed extremely quickly, with high rewards for successful innovation and severe penalties for slow adaptation.

The short-term effect of Sunday trading on retail costs and prices

4. As a basis for considering the effects of extended opening hours the IFS assembled a database on retailing costs, much of it obtained specifically for this Review. This covered a representative range of establishments, and was weighted to ensure that the different type of retailing were given their proper importance. This Retail Cost Model was the basis of all the IFS calculations, and its accuracy is thus central to their conclusions. It should be stressed, however, that the IFS do not claim accuracy for their detailed conclusions: they put more weight on the conclusion that the effects are small, particularly in the context of other changes affecting retailing, rather than on the changes being of a particular size or even in a particular direction.

5. Opening on Sundays will have the immediate effect of increasing costs, but not necessarily in proportion to the addition to total trading hours. Labour costs, the largest item of cost for all types of retailer, rise more than proportionally, because double time is generally paid on Sundays, whereas fixed premises costs (the second largest item) will be unchanged. The average short term increase in costs for a retailer opening 8 hours on a Sunday (a 13 per cent increase in trading hours) is estimated to be about 10 per cent.

6. Whether it is worth incurring this cost depends on several factors, in particular the amount of business that would be done. In aggregate, it is unlikely that increased trading hours would significantly affect total retail sales. There is no reason to believe that total savings would be reduced, or that there would be a sizeable reduction in spending on non-retailing items, such as holidays or meals out. Sunday sales would therefore represent a switch from spending on other days.

7. IFS estimated the nature and magnitude of this "switch", for different types of retailing, in two ways. They commissioned survey (undertaken by MORI) to determine current shopping habits (including evenings and Sundays), and changes if trading hours were extended. Demand for Sunday trading seemed to fall into two main categories: those items associated with "leisure" pursuits (DIY, gardening materials), where the existing law is already under greatest pressu and those items where a considerable amount of time is required to compare alternatives (clothing, major household items, furniture etc Food was another item which a considerable number of people -particularly those in full time employment - would undertake on Sundays i shops were open.

8. Regional patterns of demand for Sunday opening also emerged. Demand was highest in London and the South East, and was lowest in, Wales and the North. These differences closely followed the patter of economic activity for women across Great Britain.

9. IFS estimate the number of shops opening on Sundays by compari the loss of sales if they remain shut with the cost of opening. Th

loss of sales from remaining shut depends, for instance, on customer loyalty and the number of other shops open. For food shops, the los of sales is likely to decrease as more shops open, so that the likely outcome is that a proportion only open. The same could be true of DIY shops. Major shopping centres, by contrast, would tend to have losses which increase as more shops open. The outcome might then be some centres with widespread opening, and others with very little opening. This has, for instance, been the pattern with opening on Bank Holidays.

10. Overall, they estimate as a central case that sales losses woul exceed costs for shops comprising 48 per cent of turnover, and hence it would be worthwhile for these shops to open on Sundays. The figures for different sectors are 100 per cent in household goods an drink, confectionery and tobacco,46 per cent in food, and 23 per cen in clothing (where the cost structure is unfavourable to Sunday opening). About 7 per cent of total retail sales would, on these assumptions, take place on Sundays.

11. Survey evidence suggests that Sunday trading will be drawn disproportionately from weekday peaks (evenings and Saturdays in the case of food, Saturdays for clothing). Sunday trading is likely therefore to extend the trading week rather than shift it. Any reduction in weekday costs following Sunday opening would therefore be felt more slowly, for instance as staff levels were adjusted. Even after these medium term changes, costs per unit of sales would be higher, on average, than before deregulation. IFS estimate the increase would be equivalent to ½ per cent of turnover.

12. IFS assume that, because of competitive pressures in retailing, these higher costs would generally be reflected in lower net margins rather than higher prices. In the long run, this reduction would lead to the closure of less economic outlets and a fall in new investment. Such reduction in capacity would increase sales per square foot in remaining outlets, and act to restore margins.

13. On the assumption that capacity is determined equally by peak demand and average demand, the overall reduction in capacity is

estimated to be 9 per cent. However the effect is different in different sectors. In drink, confectionery and tobacco, where Sunda opening is expected to be widespread, the reduction is estimated to be 17½ per cent. The effect would be even greater in the household goods sector (30 per cent), but would be only 6 per cent for food and 3 per cent for clothing. Such reductions in capacity could actually lead to reductions in costs, so that current net margins were achieved at lower price levels. The overall effect on the RPI could be a reduction of about 0.4 per cent.

14. IFS acknowledge that their estimates of changes in costs and capacity are subject to a wide margin of uncertainty, and depend crucially on the projected level of Sunday opening. Different assumptions about Sunday trading levels, changes in total sales, the premium for Sunday working and the determinants of total capacity have significant effects on the level of opening: for instance, if the wage premium is reduced from the present double time to time and a half, the level of opening increases from 46 per cent to 86 per cent for food stores, and from 23 per cent to 94 per cent for clothing stores. However, the implications for cost and capacity all work in the same direction, so the conclusions that there would be a small downward effect on prices appears to be robust.

15. The overall effects on employment are similarly expected to be small. The initial effect of Sunday opening will be an increase in employment in order to meet labour demands on that day. The experience of retailers already opening on Sundays suggests that a high proportion of the additional employment will be young people working part time. The IFS conclude that, at the current premium of double time for Sunday working, the demand for this part time employment would exceed the supply.

16. Total labour requirements in retailing appear to be determined predominantly by total sales, rather than by store size or levels of peak demand. Thus, given the base assumption that Sunday trading does not lead to an increase in total retail sales, additional employment on Sundays would, according to IFS, be almost exactly offset by a reduction in weekday employment: 110,000 additional jo

on Sundays, plus 30,000 on weekdays as a consequence of Sunday trading, would be offset in the medium term by reductions of 135,000 in weekday employment, leaving a net gain of 5,000 jobs (but fall o 5,000 in full time equivalents). In the longer term, as the number of outlets was reduced, there could be a further loss of up to 20,000 jobs (mainly among shop managers). However, the total net loss of 15,000 jobs must be set against a fall in retail employment between 1980 and 1982 alone of 166,000 jobs (100,000 FTE). Moreove because of the premium for Sunday working, remuneration would certainly increase. Even after the long term effects on capacity, total remuneration would be about £250m higher than at present, equivalent to 2½ per cent of the current total.

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