

# Labor Market Flexibility: A View from the United States

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# Overview

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- **Labor Market Flexibility v. Job Protection**
  - The debate—a brief history of prevailing views
  - The weakening of employment protection laws in Europe & the growth of temporary employment
  - Parallel growth of temporary & nonstandard employment in U.S.
- **Temporary Help Employment in the U.S.: Boon or Bane?**
  - Background: Characteristics of temp help workers & why firms use them
  - Consequences for workers:
    - ▣ Wages, benefits, job security
    - ▣ Stepping stones or stumbling blocks?
- **The Great Recession in the U.S. & Worksharing**
  - Inefficient levels of layoffs
  - Short-time compensation programs in the U.S.
  - Potential jobs saved: lessons from Europe & Japan
- **Concluding remarks**

# Institutional Background: Employment at Will v. EPLs

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- **“Employment at will” largely prevails in the United States**
  - U.S. employers face few legal restrictions in firing employees – employers cannot dismiss workers based on race, ethnicity, religion, gender—otherwise no requirement that dismissals be justified
  - In case of economic dismissals, advance notice provisions only apply to mass dismissals—legal requirement recent and weak
  - Virtually no restrictions on use of temporary agency workers. Because of employment-at-will, direct-hire temporary workers not well defined; data on fixed-term contracts not regularly collected.
- **Contrasts with employment protection regulations in continental Europe**
  - Protections against individual dismissal
  - Stronger protections against collective (mass) dismissal
  - Restrictions on use of temporary help agencies & and fixed-term contracts

# Perceived desirability of countries' labor market institutions fluctuated with relative performance of economies

- U.S. had persistently higher unemployment rates than many European countries in post-WWII period—until 1980s/1990s

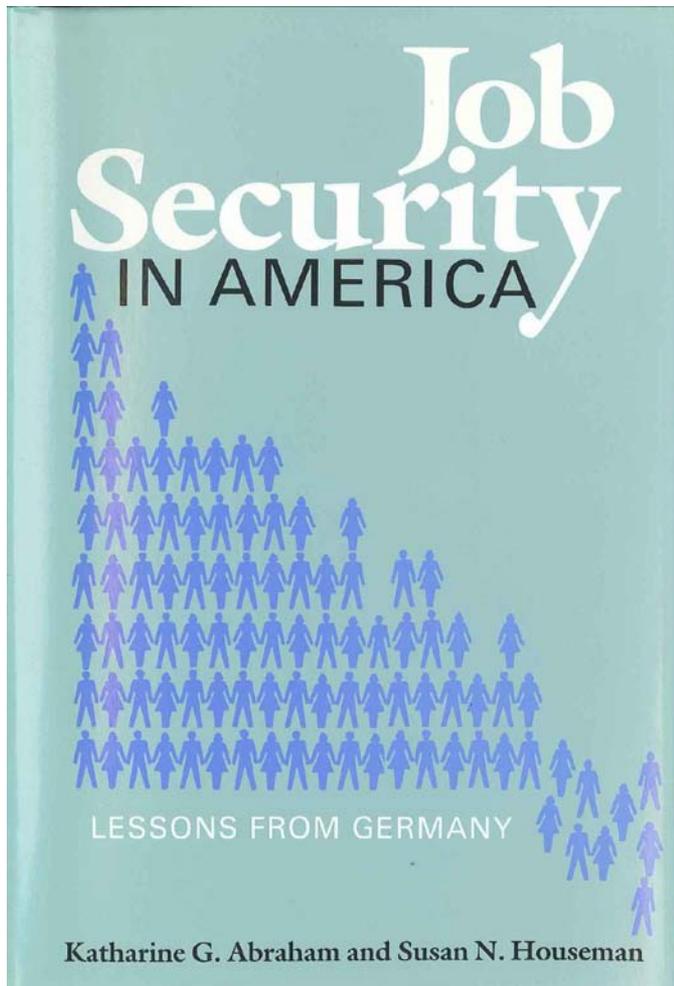
Unemployment rate, 1955-2009, selected countries



Source: U.S. Bureau of Labor Statistics

# 1970s & 1980s: U.S. looks to European Labor Market Institutions for Lessons

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- Widespread view that institutions with strong employment protection (low external flexibility) coupled with high levels of “internal flexibility” (e.g. job rotation) equitable and efficient
  - Strong attachment between workers and firms results in greater training, development of firm-specific human capital, better morale, higher labor productivity
  - Inefficient levels of churn in the U.S.

# 1990s: U.S. Has Model Labor Market Institutions

- Unemployment rate in Germany, other countries rises relative to U.S.
- EPLs seen as
  - impediment to structural change, as Eastern Europe integrated with Western Europe; trade expands and rapid shifts in global sourcing of production.
  - providing protection for “insiders,” raising unemployment for “outsiders”

Chart 2.1. **The overall summary index and its three main components**

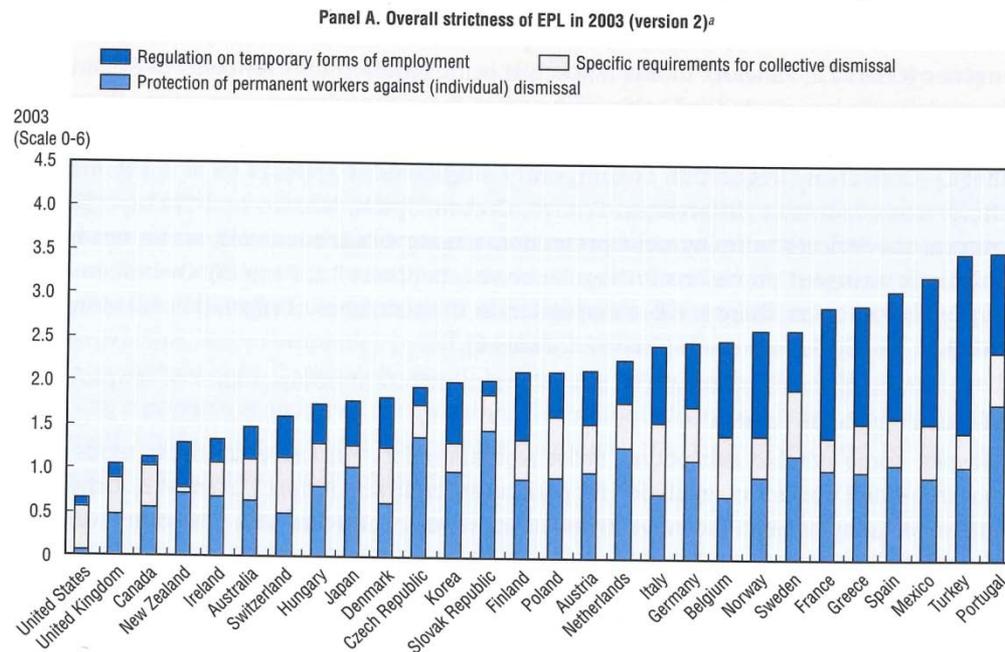
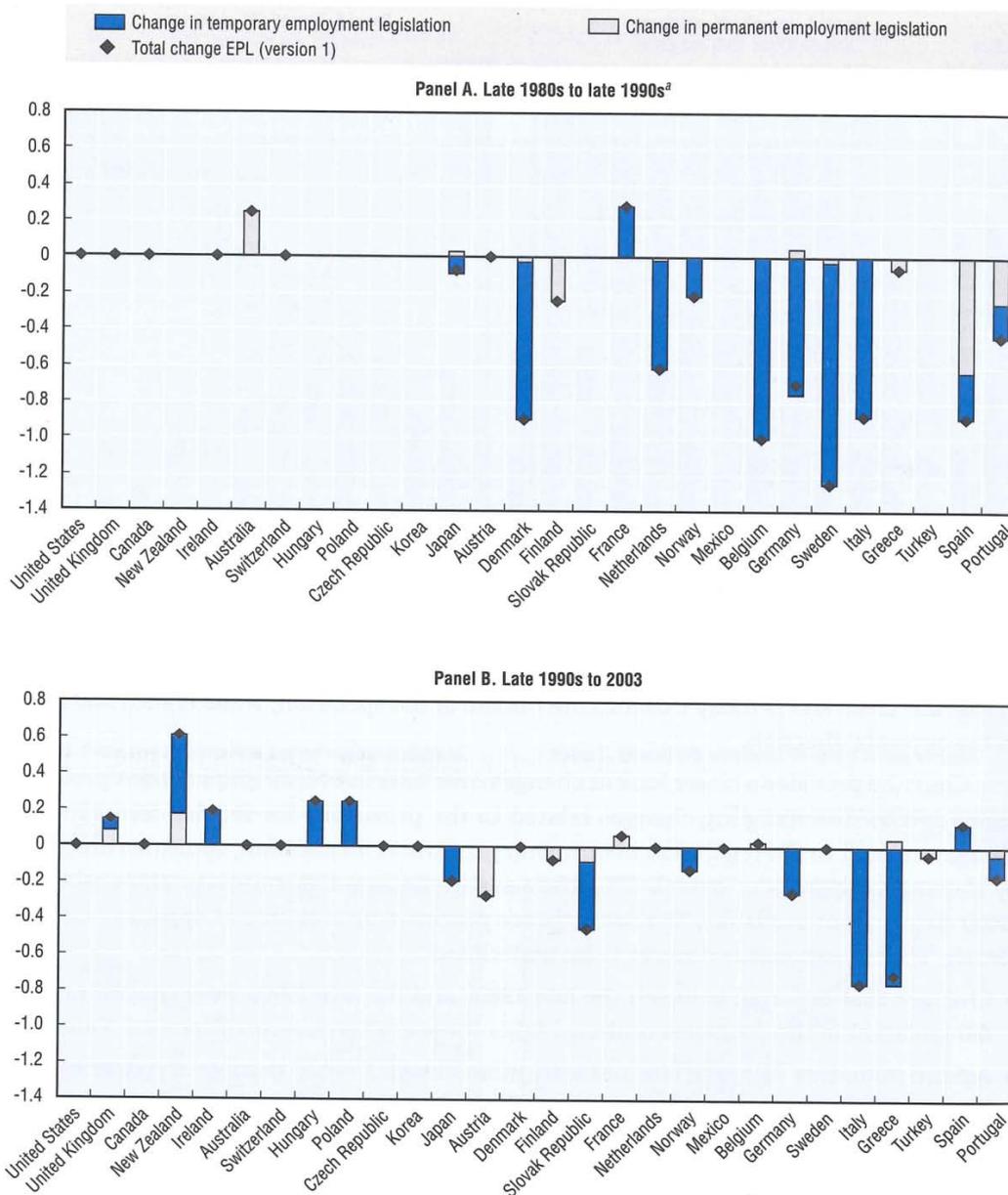


Chart 2.3. **Deregulation of temporary work as the most prevalent path of EPL reforms**

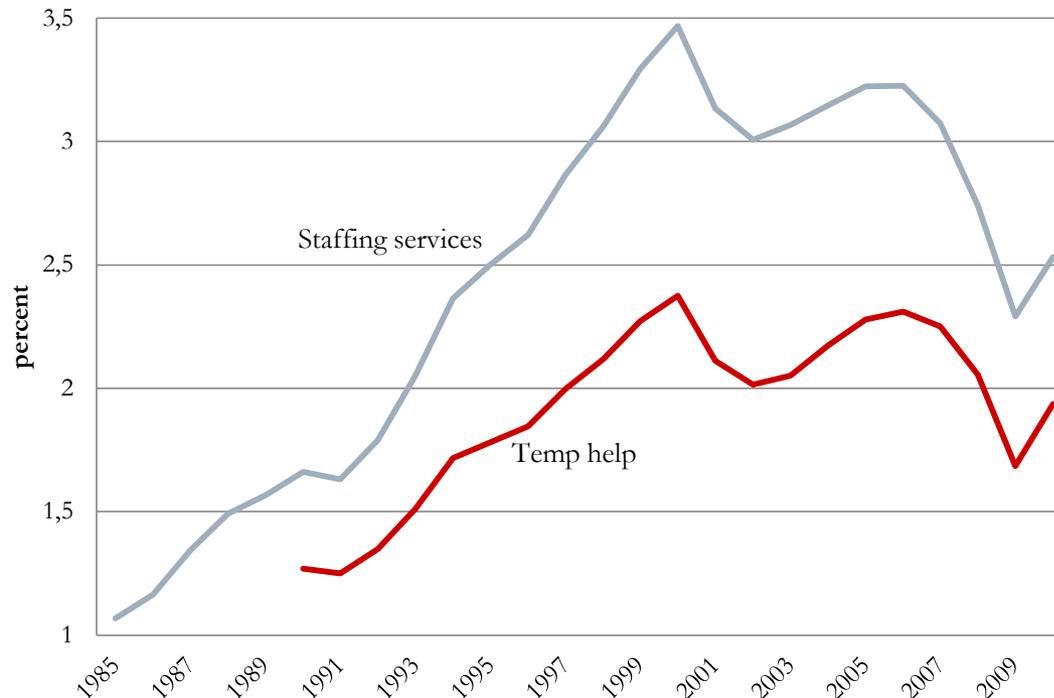


Source: OECD, Employment Outlook, 2004

- 1994 OECD Jobs Report advocates weakening EPSs & restrictions on employers' use of fixed term contracts and temporary help agencies
- Deregulation in 1980s, 1990s, 2000s primarily took form of relaxation of restrictions on use of fixed-term contracts & use of temporary help agencies.
- Temp help employment & fixed-term contracts expanded in many European countries, prompting studies of the consequences of temp employment for workers.

# Temp Help Employment & other Nonstandard Employment also Expanded in U.S.

Staffing Services and Temporary Help Employment as % of Total Private Sector



- Growth staffing services accounted for 11.7% of net job growth U.S. in 1990s—temp help 7.4%
- Other nonstandard arrangements also expanded, but not well documented in official statistics.

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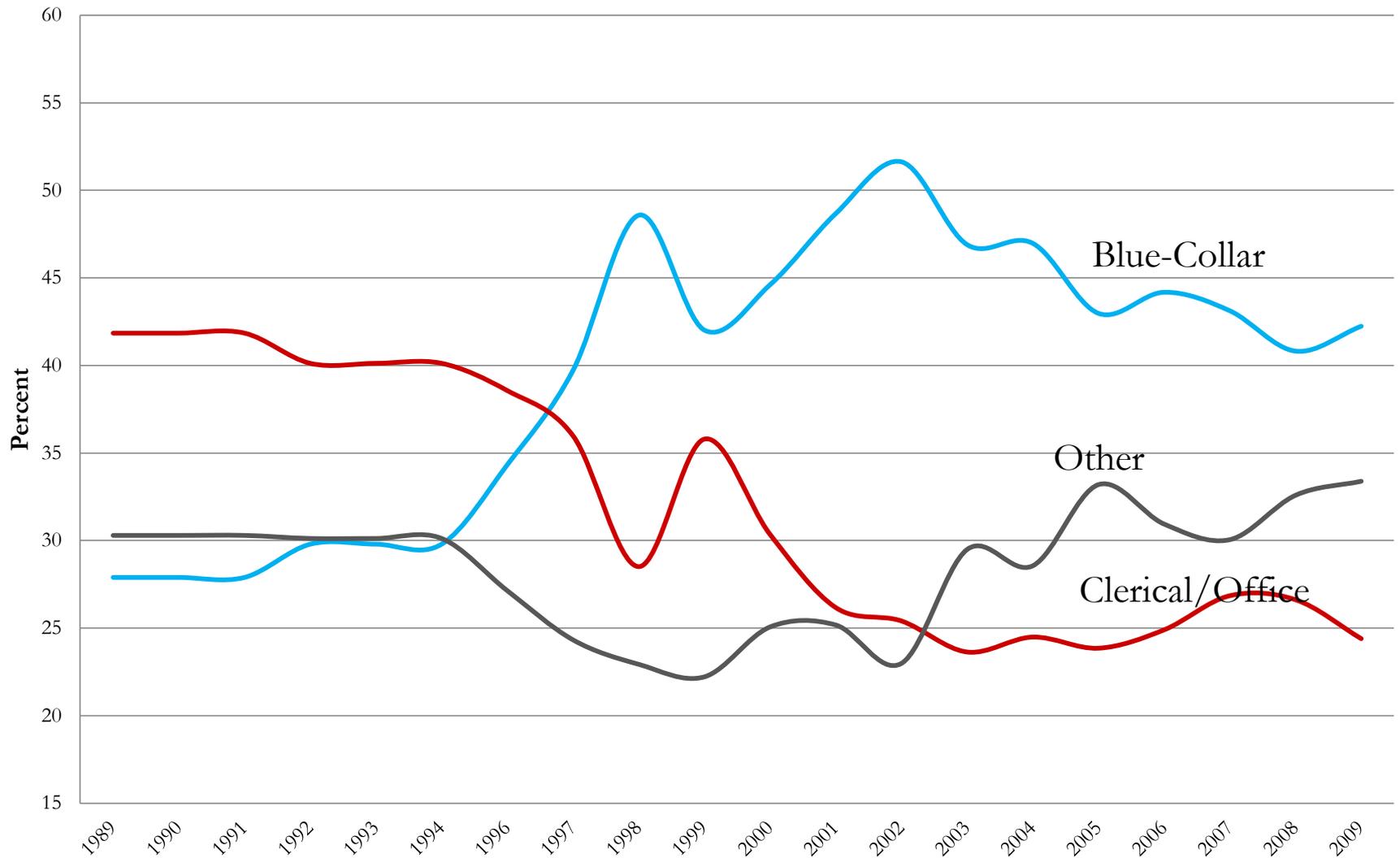
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# Characteristics of Temp Help Workers

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- **Disproportionate fraction of temporary agency workers**
  - Young—under age 35
  - Less educated—Compared to college graduates:
    - ▣ Those with high school education twice as likely to be in temp help job
    - ▣ High school drop outs 2.5 times as likely to have temp help job
  - Minority—Compared to whites:
    - ▣ African-Americans twice as likely to be in a temp help job
    - ▣ Hispanics 50% more likely to be in a temp help job
  - In low-skilled, entry-level occupations
    - ▣ Growing fraction in manual occupations—professional occupations growing, but still small share

# Occupational Distribution of Staffing Services Employment



Growth blue-collar occupations reflects use by manufacturers which behind growth of 1990s  
By 2006, temp help added 11% to manufacturing employment (Dey, Houseman, Polivka)

# Temp Help Placements in Government Supported Return to Work Programs

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- **Strikingly high incidence in this client population:**
  - Participation in government programs (e.g. WIA, welfare-to-work) in Missouri associated with 50% to 100% increase in employment in temporary-help firms (Heinrich, Mueser, Troske 2007)
  - 21% of jobs obtained by Work First participants in temporary help sector in Detroit study (Autor and Houseman 2010).
  - 15-40% of employed current or recent welfare recipients in temp help sector, according to studies in Wisconsin, Missouri, Washington State.

# Why Do U.S. Companies Use Temp Help Workers?

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- **Staff short-term needs: Why would companies pay staffing companies instead of hiring temp workers directly?**
  - Staffing companies may enjoy comparative advantage in recruiting & screening workers for temporary positions
  - Staffing companies may benefit from economies of scale—create a large pool of temp workers that can assign across companies according to staffing needs—improve staffing efficiency at companies, reduce frictional unemployment among workers
- **Screen workers for permanent positions**
  - Hire workers through temp agencies during probationary period
  - Facilitates dismissal of poor-performing workers, even when no legal barriers to dismissals
- **Lower compensation and other labor costs**
  - Typically temp workers receive fewer benefits (health & retirement)
  - Mitigate morale effects of creating two-tiered compensation system if lower (or higher) paid workers hired through 3<sup>rd</sup> party intermediary
  - Unemployment insurance & workers compensation cost savings

# Implications for Workers: Wages, Benefits, Job Security

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- **Wages**

- Evidence mixed: on average hourly wages slightly lower or about the same as comparable direct-hire workers (Segal and Sullivan 1997, Hamersma and Heinrich 2010, Autor and Houseman 2010)
- Some temp workers earn significantly more (e.g. some professionals in high demand/short supply) and some less, (e.g. blue-collar) (Houseman, Kalleberg and Erickcek 2003). Using 3<sup>rd</sup> party for hiring on the margin facilitates creation of two-tiered wage system.

- **Benefits**

- Significantly less likely than regular direct-hire employees to receive health insurance or retirement benefits from employer (temp agency)

- **Job security**

- Jobs typically short-lived
- Temp workers bear a disproportionate share of adjustment during downturns

# Implications for Workers: Stepping Stones v. Stumbling Blocks?

- **Does Temp Employment Help Low-Skilled Workers Advance?**
  - Temp help not “great” jobs—lower job security, benefits
  - Majority of workers on temporary contracts are looking for permanent employment (OECD 2003)
  - Because temp agency positions typically short-term, more relevant question is the effect on workers’ labor market trajectories.
- **Augmenting job search: ‘Stepping stone’**
  - Temporary help jobs connect low-skilled workers with potential employers, build skills, and gain work experience.
- **Prolonging instability: ‘Stumbling blocks’**
  - Offer few chances for advancement or skills development.
  - May crowd out productive job search, hamper long-term advancement.
- **Both views could be true. Relevant question:**
  - Which effect predominates in low-wage/low-skilled labor markets?

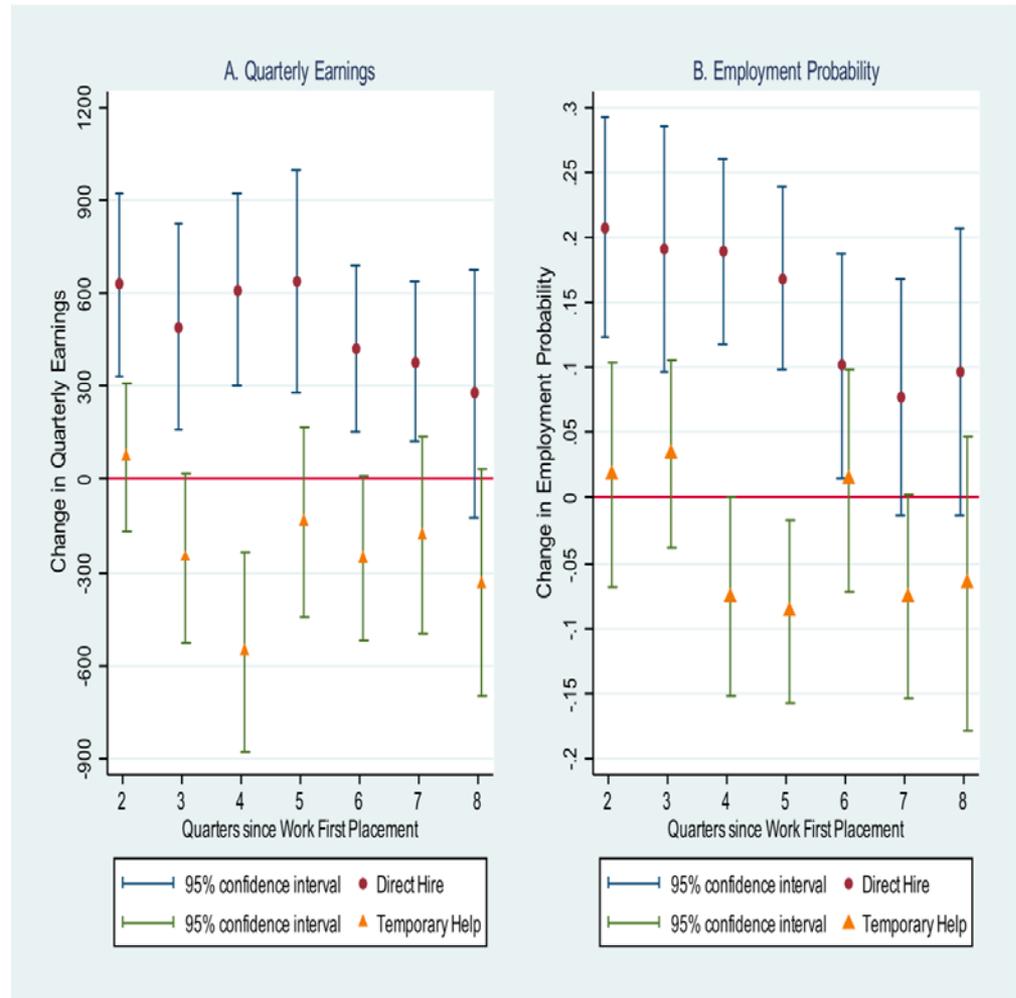
# Study of Welfare-to-Work (Work First) Program in Detroit

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- **The difficulty of answering the causal question**
  - Hard to distinguish consequences of taking a given job type from the factors that cause person to take that job initially, e.g., skills, motivation, life circumstances
- **Background on Detroit's Work First program**
  - Focus on job placements
  - Study follows individuals entering program from 1999-2003
  - 37,000+ Work First spells
- **Quasi-experimental study design (Autor & Houseman 2010):**
  - “Rotational” assignment of participants among many service providers with different propensities to place participants into temp help & direct-hire jobs
  - Work First administrative data linked to state wage records data. Employment and earnings for participants tracked for 2 years following program entry.
  - Allows identification of causal effects of temp help placements on subsequent employment & earnings – contractor assignments serve as instruments

# Evidence from Detroit Work First Study

- **Placement into direct-hire jobs ↑ employment & earnings for 2 years**
  - Raises probability of having some employment in a quarter by 15%
  - ↑ average quarterly earnings by \$500
  - Some attenuation of benefits toward end of second year
- **Placements into temp help jobs did not raise earnings & emp—worse off than those in direct-hire jobs**



Two-Stage Least Squares Estimates of the Effect of Direct-Hire and Temporary-Help Job Placements on Quarterly Earnings and Probability of Employment in Quarters 2 through 8 Following Work First Contractor Assignment. (Autor and Houseman 2010)

# Interpretation of Findings: Importance of Job Stability

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- **Finding stable employment crucial to improving employment and earnings outcomes**
- **Why do temp job placements fail to improve participants' employment outcomes?**
  - Temp jobs intrinsically short-lived,
  - Temp jobs not “scarce”—low-skilled can easily find on own
  - No evidence that on average temp assignments help low-skilled workers transition to regular employment
  - Some evidence that temp assignments lead to more temp assignments, crowd out regular employment
  - No evidence that temp employment beneficial to workers in any part of the skills distribution (Autor, Houseman and Pekkala).
- **Service providers report that maintaining employment with temp agencies often difficult for their client population:**
  - Assignments change frequently and may require new childcare and transportation arrangements
  - For-profit temp agencies oriented toward servicing business customers, not disadvantaged workers

# Direct Evidence on Incidence of Temp-to-Hire Transitions

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- **Micro data from largest U.S. staffing company shows that relatively few companies hire staffing workers assigned to them:**
  - 2.6% assignments 2007-09 result in hire by client company
  - 5.9% of non-education assignments
- **High wage workers twice as likely to be hired by client company. Excluding substitute teachers, percent hired by client company:**
  - Low-wage workers: 4.3%
  - Medium-wage workers: 4.8%
  - High wage workers: 9.0%
- **Even among staffing workers with “temp-to-perm” contracts, percent hired by client companies low:**
  - Low-wage workers: 19.5%
  - Medium-wage workers: 27.3%
  - High wage workers: 39.3%

Source: Heinrich and Houseman (2011)

# Temporary Help Employment in U.S.: Boon or Bane?

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- **Companies presumably benefit: temp help workers lower costs**
- **Workers generally do not benefit from being in temp help jobs:**
  - Lower overall compensation
  - Less job stability—bear brunt of adjustment during recessions
  - For low-skilled workers, does not facilitate transitions to permanent jobs
- **Except possibly for low-skilled, disadvantaged workers, consequences of being in temp help job—or more generally consequences of low employment protection and job security—may be small in a strong economy.**
  - Jobs openings plentiful
  - Job transitions relatively easy, unemployment low
- **Macro effects:**
  - Lack of job protections coupled with availability of flexible staffing arrangements may raise equilibrium aggregate employment
  - *But*, economies with flexible labor markets may experience greater unemployment during recessions

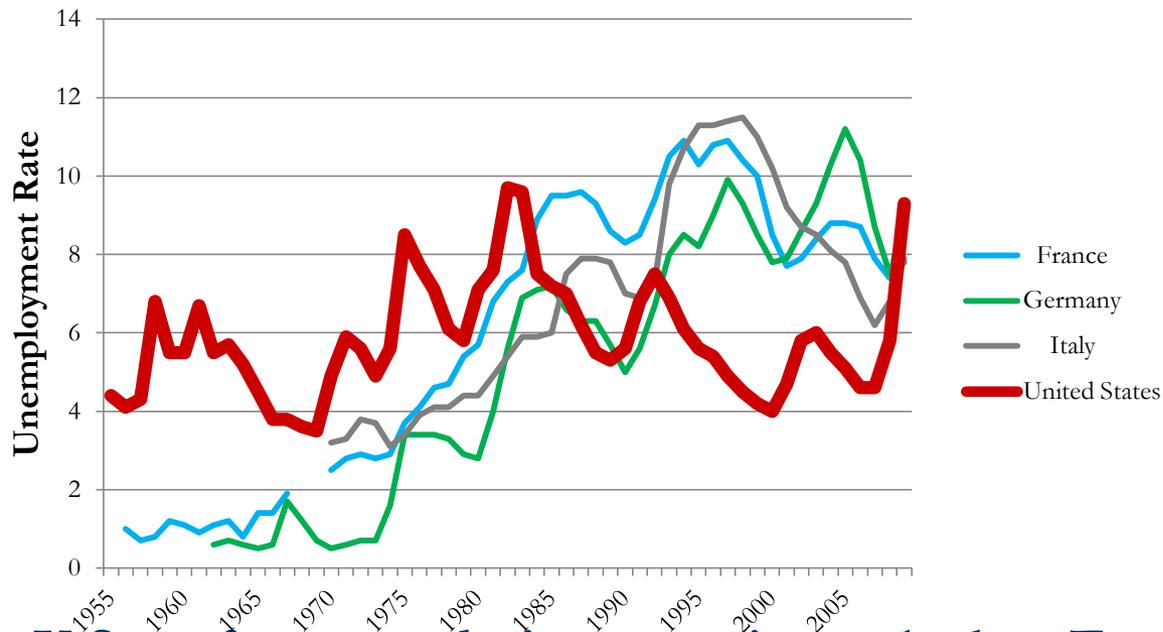
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# Policy Interest in Increasing Job Attachment during Recessions

- Severe economic recession in U.S. resulted in large-scale job loss and rise in unemployment:
  - Nonfarm employment fell by 8.4 million jobs 12/07 to 12/09; 2.5 million of these in manufacturing
  - Number of unemployed almost doubled: 7.7 m to 15.3 m



- Poor U.S. performance during recession → look to Europe & Japan for lessons.

# Recession prompted interest in programs to facilitate worksharing:

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- **At beginning of recession only about third of U.S. states offered short-time compensation (STC) as part of UI program—providing prorated UI benefits for workers whose hours have been cut due to economic conditions**
- **Historically little used,**
  - Ambiguities in federal law—legality of state STC programs in question
  - But increased use in STC states during this recession; several more states adopted program.
- **STC programs more widely available and extensively used in many other countries. Often described as accommodating EPLs.**
- **OECD (2010) estimates worksharing programs in advanced economies played a significant role in preserving jobs in recent recession.**
  - Preserved 200,000 jobs in Germany
  - Preserved 400,000 jobs in Japan

# Should work-sharing be encouraged? Arguments in favor of STC

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- **U.S. UI system w/o STC favors layoffs over worksharing**
  - Incomplete experience rating → on the margin, some companies do not bear full or any UI cost of laying off workers
  - Workers can only access UI by being laid off; many (esp those at low risk of layoff) may oppose worksharing arrangements
  - Inefficient level of separations during temporary downturns → loss of firm and individual investments in firm-specific skills.
- **Other social costs of layoffs likely not taken into account by companies**
  - Adverse spillover effects on communities associated with job loss or reduced incomes due to hours reductions.
  - Adverse impacts on individuals—health effects, persistent earnings & long-term unemployment
  - Increase in number going on long-term disability
- **More equitable: Burden of recession spread across workers**

# Should work-sharing be encouraged? Concerns about STC

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- Difficult to discriminate between temporary and structural declines at companies—STC may impede needed reallocations from declining to growing organizations
- In U.S., drawing on STC benefits will reduce eligibility for UI benefits should the workers subsequently lose their jobs.

# Characteristics of state STC programs

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- **In all STC states, employers must submit plans for approval in order for workers to collect prorated UI benefits:**
  - E.g. an employer with 50 employees and desiring to reduce hours worked by 20% may lay off 10 workers, or reduce hours by 20%--say from 5 days to 4 days per week.
  - Workers placed on short-time would be eligible for 20% of weekly benefit amount under UI
- **Worksharing plan requirements vary among states:**
  - Minimum hours reductions vary from 10% to 20%
  - Typically, maximum hours reductions vary from 6 to 12 months. Iowa permits up to 24 months on STC.
- **State administrative data show very low use of STC programs relative to regular UI in past recessions, but significant increase in recent recession.**

Take-up rates of worksharing programs in  
2009, selected countries

	All employees	Manufacturing
Austria	0.63	3.41
Belgium	5.60	16.99
Canada	0.34	na
Czech Republic	1.44	4.49
Finland	1.67	2.69
France	0.83	3.61
Germany	3.17	12.06
Ireland	1.03	1.34
Italy	3.29	9.95
Netherlands	0.75	5.01

Source: OECD, Employment Outlook, 2010

- Among other countries with STC programs, use highest in Belgium, Germany, & Italy—lowest in Canada
- Take-up rates in manufacturing significantly higher than average

Take-up Rates of Short-time  
Compensation Programs by State, 2009  
(avg. % employees covered by STC)

- Take-up rates for all private sector employees similar to those found in Canada in several states
- Higher in Rhode Island
- Available evidence indicates manufacturers disproportionately use STC
- Take-up rates among mfg production wkrs potentially high in several states

	All private sector employees	Upper-bound estimates, mfg prod wkrs
Arizona	0.11	2.01
Arkansas	0.10	0.70
California	0.25	4.55
<b>Connecticut</b>	<b>0.39</b>	<b>5.27</b>
Florida	0.03	0.91
Iowa	0.18	1.54
<b>Kansas</b>	<b>0.39</b>	<b>3.69</b>
Maryland	0.03	0.75
Massachusetts	0.18	2.95
Minnesota	0.18	2.12
Missouri	0.25	3.16
New York	0.14	2.99
Oregon	0.31	3.44
<b>Rhode Island</b>	<b>0.86</b>	<b>12.35</b>
Texas	0.06	0.86
<b>Vermont</b>	<b>0.37</b>	<b>4.01</b>
Washington	0.29	4.27
All STC states	0.17	2.74

## Average Weekly FTE Persons on STC by State, 2009

State	Number	As % Change in Private Sector Empl, 2008-09	As % Change in Manuf Production Empl, 2008-09
<b>All STC States</b>	<b>22,050</b>	<b>-0.73</b>	<b>-4.87</b>
Arizona	476	-0.26	-4.00
Arkansas	188	-0.47	-1.11
California	6,578	-0.75	-6.78
<b>Connecticut</b>	<b>1,420</b>	<b>-2.09</b>	<b>-16.34</b>
Florida	368	-0.08	-0.92
Iowa	560	-1.17	-3.05
Kansas	1,063	-2.21	-6.36
Maryland	180	-0.21	-4.36
Massachusetts	1,123	-0.96	-6.03
Minnesota	795	-0.72	-2.25
Missouri	1,425	-1.32	-5.96
New York	3,045	-1.24	-7.51
Oregon	963	-0.89	-4.41
<b>Rhode Island</b>	<b>887</b>	<b>-4.14</b>	<b>-22.88</b>
Texas	1,022	-0.3	-1.47
Vermont	198	-1.85	-5.14

- Rhode Island: relatively high use reflects strong commitment to program, outreach to businesses, small size
- If in absence of STC programs employers had used layoffs in lieu of hours reductions and if total hours adjustment the same, then FTE on STC represent potential jobs saved.

# Policy implications for STC use in U.S.

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- **STC use large enough in some states to have had measureable effect on employment adjustment in manufacturing**
- **But, overall potential jobs saved in 17 states—22,000 in 2009—small relative to overall job losses in those states**
- **Hypothetical scenarios:**
  - If all U.S. states had STC programs & use as intensive as in Rhode Island, FTE on STC would have been about 10 times greater—220,000
  - If all U.S. states used STC programs as intensively as in Germany and Italy, FTE on STC in 2009 would have approached 1 million (or about one in 8 jobs lost during recession).
- **More research needed on**
  - Effectiveness of STC programs in reducing job loss during recessions
  - Role of STC (like regular UI) as an automatic stabilizer for the macro economy during severe recessions

# Labor Market Flexibility in U.S.: Boon or Bane?

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- **Do gains from labor market flexibility outweigh the costs?**
- **In recessions, probably no: Lack of job protections or policies to promote job attachments → too many layoffs. Long-term adverse labor market consequences:**
  - Prolonged spells of unemployment lead to loss of human capital,
  - Increase in numbers on long-term disability
  - Adoption of modest STC programs that would primarily be used in recessions feasible
- **Many studies address partial equilibrium question: workers in flexible staffing arrangements worse off than comparable workers in regular arrangements.**
- **What are general equilibrium effects?**
  - Assume employers benefit from low employment regulations, flexible labor markets?
  - If so, in global economy, can strong employment protection laws/inflexible labor markets exist without incurring unacceptable levels of unemployment?

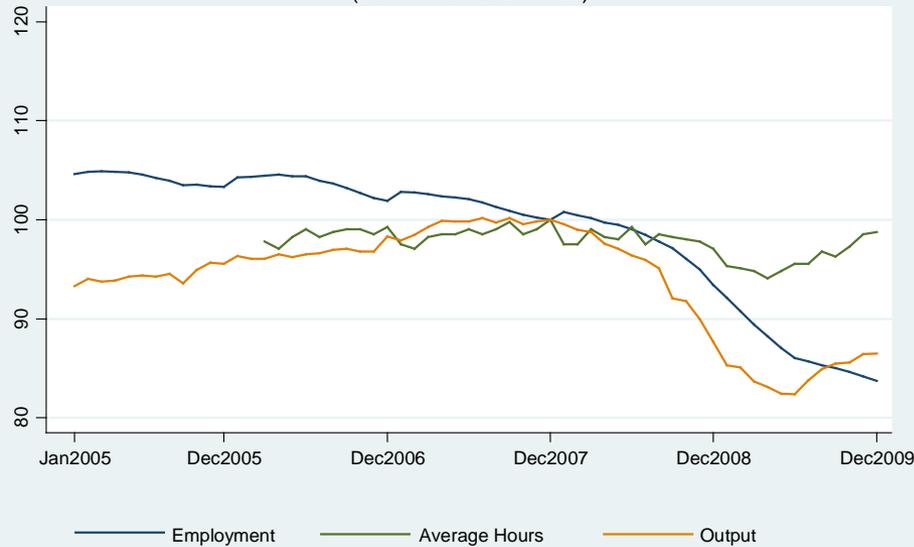


# Background on STC programs in U.S.

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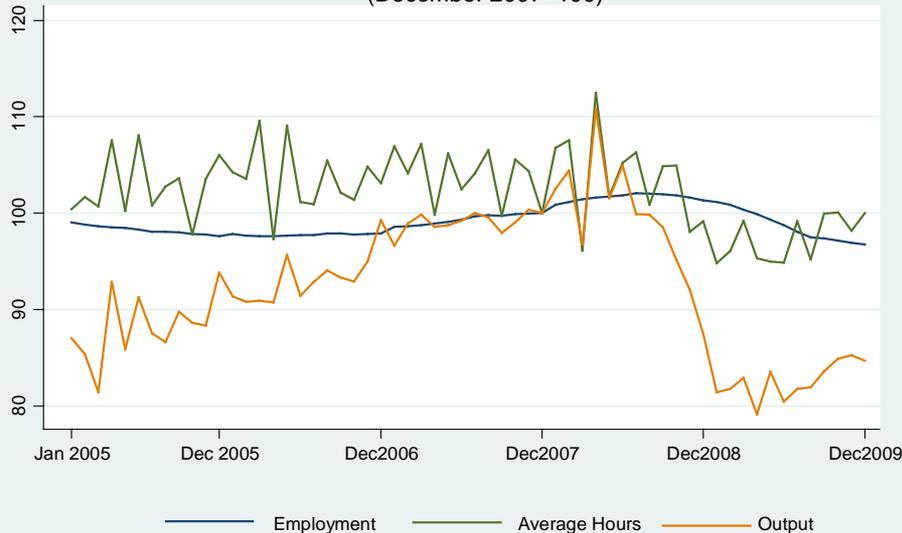
- **Worksharing common in U.S. in early economy history**
  - Fell into disfavor during 1930s (Nemirow 1984)
  - Further declined with introduction of UI
- **Interest in worksharing revived in U.S. during 1974-75 recession**
  - California first state to pass STC in 1978, and another 18 implemented plans between 1978 and 1994, though 2 rescinded them.
  - From 1994 to 2009, no other states adopted STC. Balducci & Wandner (2008) attribute stalemate to ambiguities in federal law and lack of leadership at federal level
  - At start of recent recession, 17 states had STC programs; 3 more states introduced STC in 2010; legislation pending in several other states.

U.S. Manufacturing Output, Hours and Employment Indexes, 2005-2009  
(December 2007=100)



U.S. mfg primarily adjusted labor input through employment reductions rather than hours reductions during recession.

Germany Manufacturing Output, Hours and Employment Indexes, 2005-2009  
(December 2007=100)



German mfg had similar output reductions during recent recession. Adjusted employment levels relatively little.