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Outsourcing to Staffing Services

How Manufacturers' Use of Staffing Agencies Affects Employment and Productivity Measurement

This article is adapted from and summarizes Upjohn Institute Working Paper no. 07-132, titled "Manufacturers' Outsourcing to Employment Services," which is available at http://www.upjohninstitute.org.

The decline of manufacturing employment represents one of the most fundamental—and many believe worrisome—changes to the U.S. economy of the last decade. During the 1990s, a decade marked by high trend job growth in the economy overall, manufacturing employment actually fell: between 1989 and 2000, aggregate employment grew 22 percent, while manufacturing employment dropped 4 percent. Since 2000, the decline has been precipitous. From 2000 to 2005, the manufacturing sector lost 2.2 million jobs, or about 13 percent of its 2000 employment base.

The decline of manufacturing jobs has been widely attributed to new technology, competition from foreign companies, and the offshoring of production and service jobs by U.S. manufacturers. But a less-discussed factor is outsourcing to domestic contractors. When, for example, a U.S. manufacturer outsources janitorial work to a contract cleaning company, packing and shipping to a transportation company, IT to a computer services company, and clerical and production work to a staffing agency, manufacturing employment declines in official statistics, but the occupational structure of employment in the economy may not change. Quantifying such domestic outsourcing is important for understanding the true nature of structural changes in employment in the economy, why companies outsource, and outsourcing's implications for workers.

We examine an important component of outsourcing by manufacturers: outsourcing to staffing services—or what is called employment services in government statistics—over the 15-year period from 1989 to 2004. Our analysis highlights the occupational shift that has occurred in employment services toward production and low-skilled manual occupations, the growing share of manufacturing work in the United States being performed by employees of staffing agencies, and the implications this outsourcing has for productivity measurement in manufacturing.

By 2000, employment services accounted for 5.9 percent of all production workers and for 79 percent of the growth of production workers economy-wide from 1989 to 2000.

Employment Services Sector

The employment services sector includes three industries: temporary help services, professional employer organizations, and employment agencies—which accounted for 71 percent, 21 percent, and 8 percent, respectively, of employment in the sector in 2005. Temporary help agencies assign workers to clients on a temporary basis, though the assignment can vary considerably in length. Professional employer organizations "lease" employees back to the client company. They handle payroll, benefits, and government compliance issues for the company, and hence represent the full outsourcing of an organization's human resources function. Employment agencies, often known as "head hunters," assist in matching employers and workers.

Except in employment agencies, which account for a small minority of employment in the sector, almost all employees in the employment services sector are assigned to a client organization where they perform work. Unlike most other types of contract company workers, staffing agency workers typically work under the supervision of the client organization's management and often are employed in the client's "core" functions.

The Difficulty of Measuring Outsourcing to Employment Services

Although it is important to understand where employees of staffing agencies perform their work, this information is difficult to glean from published statistics. In the principal government household and establishment surveys, the Current Population Survey and the Current Employment Statistics program, workers in the employment services sector are counted as employees of their staffing agencies, not of the client agencies where they perform their work. The only direct information on the industries to which these workers are assigned has been collected in five Contingent Worker Supplements to the Current Population Survey conducted between 1995 and 2005, but the number of agency workers sampled in these supplements has been small.

A major innovation of our work is the construction of a panel data set from the Occupational Employment Statistics program—a large, nationally representative establishment survey—on employment by occupation by industry from 1989 to 2004. We use these panel data to document the dramatic changes in the occupational structure of the employment services sector and, in conjunction with information from the

Contingent Worker Supplements, to impute the number of staffing workers assigned to manufacturing over this 15-year period.

Occupational Trends within Employment Services

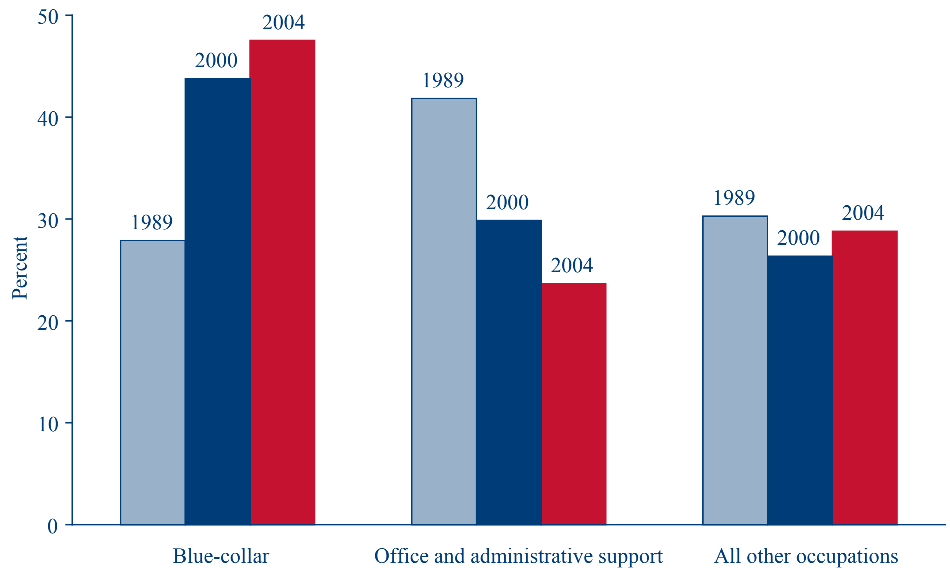
Between 1989 and 2004, the relative importance of office and administrative support occupations and blue-collar occupations within employment services reversed (see Figure 1). In 1989, office and administrative support workers comprised 42 percent of those in employment services, while blue-collar workers made up just 28 percent. By 2004, blue-collar workers accounted for 48 percent of all those in employment services, while office and administrative support workers accounted for just 24 percent.

The large majority of blue-collar workers in staffing agencies are in just one of two occupational categories: production occupations and helper, laborer, and material mover occupations. In 1989, less than 1 percent of all production workers economy-wide were employed in the staffing services. By 2000, employment services accounted for 5.9 percent of all production workers and for 79 percent of the growth of production workers economy-wide from 1989 to 2000. Employment services production workers bore a disproportionate share of the decline in production employment during the recession, but whereas employment in production occupations in the aggregate continued to decline following the end of the recession, employment of production workers within the employment services sector began to recover in 2003.

By 2004, employment services accounted for 17.6 percent of all workers in rather low-skilled manual occupations.

Employment services already accounted for a sizable share—6.3 percent—of all helpers, laborers, and hand material movers in 1989, but that share swelled to 15.8 percent by 2000. While the total number of helpers, laborers, and hand material movers declined slightly from 2000 to 2004 economy-wide, the number in employment services continued to register strong growth. By 2004, employment services accounted for 17.6 percent of all workers in these low-skilled manual occupations.

Figure 1 Occupation Shares, Employment Services, Selected Years



Outsourcing to Employment Services by Manufacturers

The strong growth in production and low-skilled manual occupations suggests that much of the growth of the employment services sector has been driven by manufacturers' outsourcing to staffing agencies. Figure 2 displays our estimates of the number of employment services workers assigned to manufacturing, along with measured manufacturing employment and manufacturing employment adjusted for use of employment services workers from 1989 to 2004.

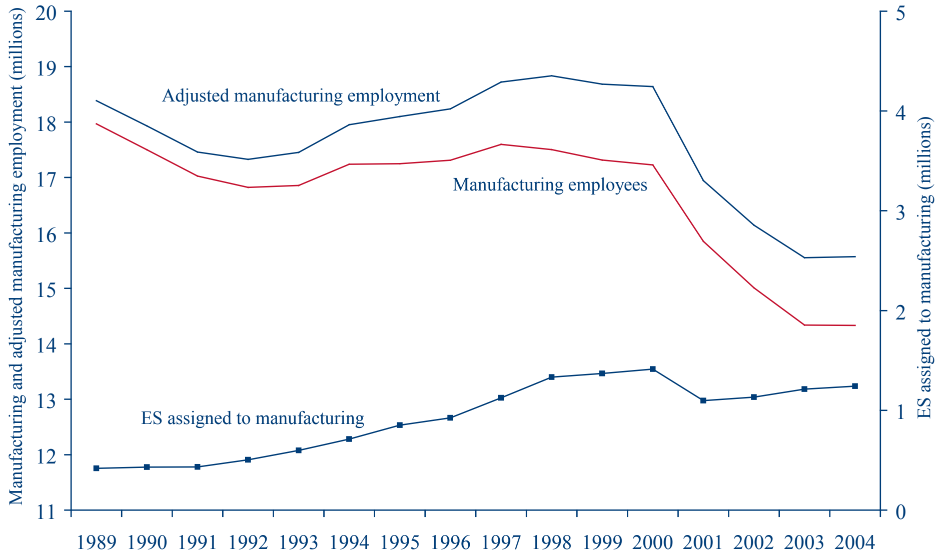
We estimate that the number of employment services workers assigned to manufacturing grew by about 1 million, from about 419,000 in 1989 to over 1.4 million in 2000. Whereas measured employment in manufacturing fell by 4.1 percent from 1989 to 2000, adjusting for employment services workers, employment in manufacturing actually grew by an estimated 1.4 percent over that period.

The number of employment services workers assigned to manufacturing dropped sharply from 2000 to 2001, as agency workers bore a disproportionate share of the adjustment during the recession. The number of employment services workers in manufacturing increased after 2001, regaining almost half of these losses by 2004, while measured employment in manufacturing continued its sharp decline. Thus, although factoring in manufacturers' use of employment services workers does not erase the large declines in manufacturing employment since 2000, a growing share of manufacturing work in the United States is being performed by employees of staffing agencies. In 2004, employment services workers added an estimated 8.7 percent to direct-hire manufacturing employment, compared to just 2.3 percent in 1989 and 8.2 percent in 2000.

Effects on Productivity Measurement in Manufacturing

Simple labor productivity statistics measure output divided by labor input. In manufacturing, output is defined as shipments in constant dollars, net of shipments between manufacturing establishments, and labor input is

Figure 2 Manufacturing Employment and Employment Service Workers Assigned to Manufacturing, 1989–2004



measured as the number of employees or hours worked by employees at manufacturing establishments. Staffing agency workers assigned to manufacturers are counted as purchased business services rather than labor input in manufacturing productivity statistics. Consequently, all else equal, the substitution of staffing agency workers for direct-hire employees will increase manufacturing labor productivity measures.

We estimate that outsourcing to employment services inflated the annual growth rate of manufacturing labor productivity by 0.5 percentage points, or 14 percent, over the 1989 to 2000 period. Because employment services workers in manufacturing bore a disproportionate share of employment adjustment to the downturn, failure to account for these workers in manufacturing depressed productivity statistics by an estimated 1.2 percentage points from 2000 to 2001. From 2001 to 2004, growth in outsourcing to employment services resumed and added a half a percentage point to labor productivity growth in manufacturing, representing 9 percent of the growth.

Implications for Future Research

Our findings illustrate the importance of taking into account outsourcing when interpreting employment and productivity trends in manufacturing. In closing, we emphasize that our study measures only one type of outsourcing, albeit an important one for manufacturers. We do not examine manufacturers' outsourcing to domestic contractors in other industries. For instance, it is possible that the growth in outsourcing to staffing services, which largely fills production, low-skilled manual, and clerical occupations, paralleled a trend to outsource to other business services industries for jobs in such areas as IT and shipping. Moreover, studies have begun to document recent growth in the foreign outsourcing of intermediate inputs and services.

Use of staffing services by manufacturers plateaued in the late 1990s, according to our estimates, and the subsequent slower growth in the staffing industry may reflect increased foreign outsourcing of production and services work, as opposed to outsourcing work to domestic contractors, a view recently expressed to us by a representative of Manpower, the country's largest staffing agency. Our findings regarding manufacturers' outsourcing to employment services, we believe, underscore the need to study the implications of other types of domestic and foreign outsourcing on employment and productivity measurement in manufacturing.

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Upcoming Conference Announced

The Upjohn Institute is planning a conference and book on U.S. labor market policy entitled "A Future of Good Jobs? America's Challenge in a Global Economy."

Conference speakers will propose solutions to the difficulties facing the U.S. labor market in sustaining low unemployment, growth in living standards, and economic security for all workers. The conference will cover six major policy areas: 1) labor skills development and the U.S. education and training system, 2) health insurance and the labor market, 3) employment problems of older Americans, 4) immigration and trade, 5) labor market problems of the disadvantaged, and 6) ways of promoting employer competitiveness.

Authors of papers include Robert Lerman, Katherine Swartz, Katharine Abraham, Lori Kletzer, Steven Raphael, and Paul Osterman. The book will be edited by Susan Houseman and Tim Bartik of the Upjohn Institute.

The conference will be held in Washington, D.C. on June 22, 2007, followed by a book in early 2008. Further announcements about the conference will be forthcoming this spring.