Temporary employment agencies as labour market intermediaries – new ways of working in an open economy

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This paper draws on a discussion paper prepared for the Recruitment and Consulting Services Association. The discussion paper was commissioned by the RCSA to offer a broader review of and promote a debate about available policy options in relation to new working arrangements. The views expressed are those of the author and do not represent RCSA policy.
Temporary work agencies should have their place in a modern labour market as new intermediaries that can support flexibility and mobility of firms and of workers, while offering security for workers in the form of improved job opportunities and high employment standards, including in terms of pay, working time and training opportunities.¹

Key role of labour market intermediaries

European governments established a high-level Employment Taskforce ‘in response to concerns that Europe was failing to tackle effectively the significant employment challenges it faces’. Headed by a former Dutch Prime Minister, Kim Kok, the Taskforce has called for regulators to make it easier for employers and employees to have access to a range of more appropriate employment arrangements in order to stimulate job creation.²

The EU’s European Employment Taskforce report points to the positive role employment services agencies play in the labour market. The report recommends that governments seek to utilise better the potential of temporary work agencies by providing a more flexible framework through which they can operate more effectively. The Taskforce report also challenges the employment services providers themselves to become more actively involved in supporting the training and other needs of their employees:

Temporary agency work can be an effective stepping stone for new entrants into the labour market and hence contribute to increased job creation, for example by facilitating recruitment instead of overtime. Acting as human capital managers – rather than mere manpower suppliers – these agencies can also play the role of new intermediaries in the recruitment and management of both qualified and unqualified staff, offering employers an attractive alternative to traditional recruitment channels.³

The EU Employment Taskforce urges that better use be made of temporary agency work ‘to allow enterprises to have some flexibility to increase or decrease the size of their workforces, while ensuring sufficient security for the workers concerned’⁴

Why Australia seeks some types of flexibility and not others

Open, liberal market economies, such as Australia’s, tend to have production systems that produce standardised products and services, using general skills. These economies rely more on numerical, temporal and pay flexibility to achieve competitive advantage. This is because market forces in these economies are given freer reign to use these forms of

² Ibid, p 28
⁴ Ibid, p 29.
flexibility than they are in coordinated market economies such as Germany, Japan, the Nordic countries and the Netherlands.\(^5\)

The latter tend to emphasise industry and enterprise specific skills and put in place mechanisms to protect employees who have invested in acquiring these more narrowly-based skills.\(^6\) This different approach to skills formation and skills use helps explain why employment protection laws in the liberal market economies of the USA, the UK, Australia, Canada, New Zealand and Ireland are less severe than those of the coordinated market economies of continental Europe.

However, in Australia’s case, scope for pay flexibility is more limited than in other liberal market economies as a high proportion of the workforce is covered by legal minimum wage rates specified in industrial awards. Indeed, many RCSA members note that their on-hired employee services are paid the same or better pay wage rates compared with the employees of the client enterprise. This leaves numerical and temporal flexibility as major sources of comparative advantage for the Australian economy. Options considered below need to clearly address how employment services firms can continue to offer solutions that enhance numerical and temporal flexibility.

**Employment services firms as labour market intermediaries**

Recent published research provides insights into the reasons for the rapid growth in the use of employment services agencies and on-hired employees in both European and United States economies.\(^7\) The use of temporary work agencies has grown in OECD countries not merely as a means of avoiding termination costs, although there is some evidence that this may be the case in the USA.\(^8\)

More important reasons are the efficiencies these agencies offer in placing employees in client firms. Economies of scale are achieved when a specialist third party manages key aspects of the employment relationship such as recruitment and undertaking other functions of a personnel department. In turn, the client firm achieves efficiencies and lower transaction costs due to the better matching of people to what is required.\(^9\)

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\(^6\) Ibid


Why the greater use of intermediaries?

The need for a greater role for labour market intermediaries in the modern labour market stems from a number of factors. These include the much more competitive environment many enterprises now have to operate in. This competitive environment is a product of lower tariff barriers and exposure to world markets for those enterprises in the tradeable goods and services sector. In other instances, competitive pressures come from changes in competition law which have abolished the monopoly position of a range of service providers such as utilities and public transport. New technologies and organisational changes such as just-in time inventory, team work and outsourcing of non-core activities have also created a new set of pressures.

Benefits to enterprises

The demands on enterprises operating in highly competitive markets means that hiring someone who does not have the right skills or work attitudes can be a costly exercise. The protections offered ‘permanent’ employees mean that the transaction costs of dismissing an employee can be high, especially if a legal challenge is mounted.

Many enterprises now use on-hired employee services for two broad sets of reasons. One set of factors relate to achieving greater short-term numerical flexibility due to fluctuations in workload or staff absences. The demands of more comprehensive service delivery such as round-the-clock availability make staff absences more difficult to manage. Uncertainties caused by combinations of service-related and staff-related factors can only be met by resort to a specialised facility to provide appropriately skilled labour if and when required.

The other set of factors explaining the greater use of on-hired employees relate to strategic reasons. These focus on improving enterprise competitiveness in the longer term. Many enterprises now operate with a small core workforce. The capacity to expand and contract according to the demands of the business cycle is a key feature of a competitive strategy in world markets. This means that enterprises now require a buffer workforce that sits between its core workforce and their need for short-term temporary staff for meeting ad hoc or seasonal demands.

This buffer workforce needs to be highly skilled so it can work productively with the core workforce. It also needs access to the same working conditions in terms of OH&S training and support. However, this buffer workforce in most instances cannot be engaged in the same way as an enterprise's core workforce due to unpredictability of the business cycles.

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Enterprises operating in competitive markets, therefore, require both the capacity for numerical flexibility, should it be needed, and a labour force with the right skills and attitudes. These twin objectives of numerical flexibility and a skilled workforce push in opposite directions. The former requires of those providing their services little commitment while the latter requires a high level of commitment and hence a degree of security. This has been termed an important paradox in the modern labour market – the need for enterprises to have numerical flexibility alongside a workforce with the right skills to deliver high quality work within a safe working environment.

**Australian evidence**

An Australian survey in 2003 showed that just over half the main reasons cited by firms using on-hired employees are concerned with meeting short term contingencies. However, another 42 per cent of the main reasons given by enterprises related to the perceived long-term benefits to the enterprise. These longer term benefits included: outsourcing the administrative burden, ensuring a thorough recruitment process and overcoming skill shortages.

In keeping with this short-term or strategic focus, enterprises are in most cases not seeking to lower costs through lower wages by using on-hired employee services. A survey of RCSA members in NSW (N=99) in March 2004 found that nearly 4 in 5 on hired employees receive rates of pay that are equivalent to or better than those paid by the client organisation. Similarly, other survey results show that 85 per cent of firms using on-hired employees do not believe that they treat them differently to their own direct employees. Only 3 per cent of firms surveyed in 2003 wanted ‘to reduce staffing costs by paying less’ as a main reason for using agency employees.

**Benefits to job seekers**

As noted above, the transaction costs involved in recruiting and training a new employee are important reasons for employers seeking to find other ways to minimise their risks. One response by employers to reducing risk is to seek to recruit people who are seen as ‘low risk’, such as employees already working for other enterprises. This results in an ‘adverse selection’ effect for the unemployed who are placed at the back of hiring queue, especially those who cannot show recent relevant work experience.

Access to temporary work through on-hired employee services can provide the opportunity for disadvantaged job seekers to gain a foothold in a client enterprise by

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13 Osterman, P, 2003, p 162.
15 Ibid
16 Ibid
17 Brennan, L; Valos, M and Hindle, K; 2003, pp18-19
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giving them a chance to prove their worth in realistic work situations in firms where they might otherwise have been discriminated against.\textsuperscript{19} This applies to qualified school leavers without relevant job experience, young people trapped in a cycle of intermittent part-time work and unemployment, women re-entering the labour market and older employees who have ‘voluntarily’ or ‘involuntarily’ left their previous job.

In the USA, workforce intermediaries act as an alternative to informal and haphazard hiring networks. They can operate as first and second chance employment and training opportunities where the job ready are linked to employers, and employers are helped to define jobs and identify appropriate job qualifications.\textsuperscript{20}

Australian evidence offers support for this stepping stone role of on-hired employee services agencies for many on-hired employees as shown by the fact that most on-hired employees are using more than one agency to find a work assignment. The RCSA member survey in NSW shows that over half (55 per cent) are registered with more than one agency. Nearly a quarter (23 per cent) achieved a ‘temp to perm’ placement. Others use agency work to put together the number of work hours they are seeking, with 21 per cent working regularly at more than one client firm in a week or other regular working cycle. Only 44 per cent of on-hired employees with one agency are in a regular cycle of back-to-back assignments.

\textit{Benefits to the economy}

Employment services firms as labour market intermediaries also play a macro economic role in lowering frictional or seasonal unemployment.\textsuperscript{21} It is reasonable to claim that the lower unemployment rate of recent years in Australia, as well as the USA, UK and the Netherlands is at least partly explained by the greater facilitative role played by employment services firms.

\textbf{How important are temporary employment firms in Australia?}

Enterprises providing employment services, including on-hired employee services, have grown significantly between 1998-99 and 2001-02.\textsuperscript{22} Total income generated by employment services increased by 31 per cent over these 3 years. At the same time, the total number of enterprises providing employment services increased by 29 per cent. This growth in employment services has taken place during a period of good employment growth in the Australian economy. This suggests that the growth in employment services has promoted and not hindered employment growth more generally.

How important are temporary employment agencies in Australia compared with other countries? The ABS estimates that 290,115 employees were on-hired through agencies in

\textsuperscript{19} Storrie 2002, p 70  
\textsuperscript{21} Neugart and Storrie, 2002  
\textsuperscript{22} ABS 2003, Employment Services, Australia. Cat. 8558.0
the year to June 2002. This represents 3.1 per cent of total employment at that time. Using similar time periods, countries with a higher use of temporary employment agencies than Australia are the Netherlands, France, USA and the UK. In nearly every Member State of the European Union, temporary agency work has at least doubled during the 1990s, and in Scandinavia, Spain, Italy and Austria, it has increased at least five-fold.23

**Characteristics of on-hired employees in Australia**

Who in terms of age and gender are employed by employment services firms? The following profile is based on data available from the industry’s superannuation fund – RecruitmentSuper. Women account for 58 per cent of all contributors. Women and men in the 25 to 34 years age group are the largest age and gender groupings (27 and 18 per cent respectively) (see Table 1 below). Women in the 35 to 44 years and up to 24 years age groups are the next largest groupings (11 and 10 per cent respectively), followed by males in the up to 24 years age group and 25 to 44 years groups (both 8 per cent).

**Table 1: Age and Gender profile of current contributors to RecruitmentSuper**

<table>
<thead>
<tr>
<th></th>
<th>Up to 24 yrs</th>
<th>25 to 34 yrs</th>
<th>35 to 44 yrs</th>
<th>45 to 54 yrs</th>
<th>55 yrs &amp; over</th>
<th>Unknown</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Male</td>
<td>18,671</td>
<td>40,048</td>
<td>17,528</td>
<td>9,425</td>
<td>4,199</td>
<td>4,494</td>
<td>94,320</td>
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<tr>
<td></td>
<td>8.4</td>
<td>18.0</td>
<td>7.9</td>
<td>4.2</td>
<td>1.9</td>
<td>2.0</td>
<td>42.4</td>
</tr>
<tr>
<td>Female</td>
<td>21,150</td>
<td>58,945</td>
<td>23,999</td>
<td>14,048</td>
<td>4,386</td>
<td>5,821</td>
<td>128,349</td>
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<tr>
<td></td>
<td>9.5</td>
<td>26.5</td>
<td>10.8</td>
<td>6.3</td>
<td>2.0</td>
<td>2.6</td>
<td>57.6</td>
</tr>
<tr>
<td>Total</td>
<td>39,821</td>
<td>98,993</td>
<td>41,527</td>
<td>23,473</td>
<td>8,585</td>
<td>10,270</td>
<td>222,669</td>
</tr>
<tr>
<td></td>
<td>17.9</td>
<td>44.5</td>
<td>18.6</td>
<td>10.5</td>
<td>3.9</td>
<td>4.6</td>
<td>100.0</td>
</tr>
</tbody>
</table>

Source: RecruitmentSuper, personal communication 27 Sept, 2004

Another notable feature of this profile only becomes obvious when it is compared with the age and gender profile of the total employed population, using May 2004 data. This comparison shows that employment services firms are twice as likely to employ people in the 25 to 34 age group than this age group is represented in the employed population at large (45 per cent compared with 23 per cent). This applies particularly to women in this age group who are more than 2.5 times likely to be employed in this sector compared with their share of total employment (27 per cent compared with 10 per cent). These data show that young people to age 35 years in particular benefit from the jobs provided through employment services firms, with women in the 25 to 34 age group benefiting the most.

23 Storrie, D; 2002, Temporary Agency Work in the European Union, European Foundation for the Improvement of Living and Working Conditions, Dublin