

Labor Shortages, Needs, and Related Issues in Small and Large Businesses

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Purpose

Currently, small businesses are ranking labor shortages above taxes and government regulations as their biggest burden. This report quantifies the extent of the labor shortage, measures the impacts from survey data, and examines how small businesses are coping.

The labor shortage has large implications for the economy at large, because it would be both inflationary and unprofitable if small firms raised wages without increasing productivity. In addition, if small businesses are facing a labor shortage, their output growth could slow or stagnate, thus braking the overall output growth of the U.S. economy. In theory, small businesses would be more affected by a labor shortage as they are more labor intensive and less able than large businesses to substitute labor for capital.

The report also examines the possibility that contingent workers (such as temporary and contract workers) might be a solution for small businesses that are facing labor shortages. Subcontracting for another firm's labor can fill positions that small businesses might not otherwise be able to fill.

Scope and Methodology

The researchers used private and public data to evaluate labor shortages. They used data from the Current Population Survey (CPS), a joint venture of the Bureau of the Census and the Bureau of Labor Statistics, to study contingent workers. They also

analyzed data collected in the Skills Deficit Survey conducted by the National Federation of Independent Business (NFIB) to study the labor shortage. The CPS sampled businesses with fewer than 500 employees and the Skills Deficit Survey sampled businesses from Dun and Bradstreet's data base with fewer than 100 employees.

Highlights

The report is broken into two sections: part A, "Labor Shortages in Small Firms," and part B, "Contingent Workers in Small and Large Firms."

Concerning labor shortages, the researchers found:

- In late 1998, about half of all small firms (those with 1 to 100 employees) were looking to hire, with about two-thirds of those reporting trouble hiring. Thus, about a third of all small firms had trouble hiring.
- The percentage of firms reporting difficulties filling job openings right away was at the highest level since such records were first kept in 1974. In 1998, the percentage was almost twice as high as the low point reached in 1991, and about three times as high as the all-time low reported in 1982.
- About half of the companies looking to hire someone eventually hired someone less qualified than they were originally looking for. Slightly more than a third of firms that had hiring difficulties increased the time allotted for training the new hires.
- About half of the small firms that had trouble

hiring raised the wages they were originally offering, and about a quarter raised benefits. This translated into about 15 percent of all small firms raising wages because of hiring difficulties.

- It is unclear if firms that raised wages raised them above standard levels or originally offered a wage that was too low. However, about 90 percent of the firms that had trouble hiring felt their wage and salary policies were at or above the market. This figure was 95 percent for firms that had no trouble hiring.

- According to the survey, hiring difficulties had their biggest impact on employee morale and productivity. Many firms reported multiple impacts: in addition to morale and productivity, profitability, hours of operation, and growth were also affected.

- Slightly more firms that were having hiring troubles compared to firms without hiring troubles upgraded their technology substantially. This suggests that a few small firms were substituting capital (or technology) for labor.

- Firms were generally trying to fill entry-level jobs. Of the firms that were having trouble hiring, about three-fourths were seeking someone with one to two years of experience, and a little less than three-fourths were seeking someone with a high school diploma.

- About 60 percent of the firms with hiring difficulties felt that finding workers without a history of poor work habits and substance abuse problems was the cause of their hiring difficulties.

- A little more than a third of firms that had trouble hiring were seeking someone with computer skills. About a third were seeking someone with a bachelor's degree or greater education.

- Almost all firms that had hiring troubles used word of mouth to recruit. About two-thirds used local newspapers, and about a quarter used the Internet. The latter method was more prevalent among the larger of the small firms. As expected, recruiting efforts increased when hiring difficulties occurred.

- The pattern of hiring difficulties did not seem to differ much in the different size categories of small firms (such as firms with 1 to 4 employees, 5 to 9 employees, etc.).

Concerning contingent workers, the researchers found:

- Contingent workers (broadly defined as workers who expect to lose their job in the future) comprise a little less than 5 percent of the work force.

- Small firms (those with fewer than 500 employees) employ about 45 percent of the contingent worker force. Small firms are less likely than large firms to hire contingent workers, but are nevertheless a very significant employer of contingent workers.

- Small firms are more likely than large firms to use contingent workers in blue-collar occupations. The small firms that use contingent workers are more likely to be in goods-producing than service-producing industries.

- While small firms in goods, trade, and service industries all reported labor shortages (in part A of the report), goods-producing industries are more likely to use contingent workers as a solution (according to part B of the report).

Conclusions

The labor shortage reported by small businesses is at an all-time high. Employee morale, employee productivity, and small business profits are suffering as a result. Most of the shortage appears to be at the entry level. Small firms are hiring individuals less qualified than they were originally looking for, raising wages, increasing recruiting, increasing their investments in technology, and hiring temporary workers. Although these measures may have the effect of bringing more people into the labor force, the labor shortage being experienced by small businesses shows no sign of abating.

Ordering Information

The full text of this report, along with summaries of other studies performed under contract to the U.S. Small Business Administration's Office of Advocacy, is available on the Internet at www.sba.gov/advo/research.

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