The rise and fall of internalised employment systems?

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Internalized labour market systems became more widespread during the 1960s and 1970s. In the United States, salaried and industrial internal labour markets, first developed during the 1920s and 1930s, became increasingly widespread in large corporations during the 1960s and 1970s. Internal labour markets also began to develop more widely in the UK, despite the continued importance of occupational labour markets. Long-term employment and opportunities for internal promotion had been characteristic of the civil service, local government, banking and certain sections of retailing for many years.

However, a number of studies also found evidence of salaried internal labour markets for professional engineers and professional chemists (Mace, 1979; Creedy and Whitfield, 1986) and more restricted versions of industrial internal labour markets for skilled and semi-skilled workers in engineering (George and Shorey, 1985). Moreover, even though fully developed internal labour markets were far from universal in the UK, the salaried internal labour market was an important influence on the development of ideas concerning personnel management and human resource management during the 1970s and 1980s.

Increasingly, internalisation of employment came to be seen as best practice (Boxall and Purcell, 2003; Nolan and Slater, 2003). Corporations such as IBM, with highly developed salaried internal labour markets, were held up as examples of sophisticated personnel management and pioneers of human resource management.

Factors contributing to the internalisation of employment in the 1960s and 1970s

Employers' labour requirements

Increasingly, managers designed jobs on the basis of firm-specific skills. This was partly the result of differences in the ways firms made use of technologies of production. It was also partly a response to features of the labour market. This was a time of full employment, which meant that workers could move easily between jobs in search of higher pay or better conditions. This encouraged employers to develop ways of retaining workers and reducing labour turnover.

In some countries such as the USA, UK and France, the absence of a training system that produced an adequate supply of workers with transferable skills meant that firms increasingly designed shopfloor jobs to require limited firm-specific skills and trained their workers internally. In some other countries, notably Germany, the presence of highly effective apprentice training maintained a stronger basis for skilled occupational labour markets.

Organisational constraints

Steady economic growth during the 1950s and 1960s provided a foundation for increasingly large-scale enterprises geared to producing for stable mass markets. As firms grew in size and complexity they needed more supervisory and administrative staff. This in turn created more layers of hierarchy, which extended job ladders and opened up career paths. At the same time, stable long-term growth made it rational for firms to commit themselves to developing long-term career paths for more of their employees. Large enterprises also had the financial and managerial resources to develop internal systems of training and promotion and set up formal internal pay structures.

Employee pressure and influence

Trade union membership and influence rose during the 1960s and 1970s. In Britain, unions extended their membership and representation among white-collar workers during the 1970s, contributing to the development of salaried internal labour markets. In representing their more traditional constituency among manual workers they were also able to establish ‘seniority’ rules with respect to redundancy dismissals and restrict management’s freedom to hire and fire.

In a number of European countries, workers’ ability to influence employment systems was encouraged to varying degrees by legally supported structures of collective bargaining and co-determination, as in West Germany and Sweden, or the ability of unions to influence government legislation, as in France. In West Germany an elaborate system of collective bargaining and employee co-determination was established after the Second World War, supported and regulated by law.

German workers, through their representatives, were empowered to influence not only wages and hours but also procedures for ‘layoffs, promotion criteria, changes in working conditions, the use of overtime and of “short time”, and the introduction of new technologies’ (Osterman, 1988: 119). This resulted in management providing a high degree of employment security for incumbent workers in return for their acceptance of flexible working practices, i.e. broadly defined job roles and ‘willingness to learn new skills’ (Osterman, 1988: 123).

In France, new developments in collective bargaining after the political unrest among workers and students in 1968 led to enhanced ‘job security, vocational training, [and] salaried status for manual workers’ (Goetschy and Rozenblatt, 1992). In the United States, even though trade union membership peaked in the mid-1950s and declined thereafter, unions were increasingly successful in pushing up wages in unionised firms. This gave firms an increasing incentive to avoid unionisation.

Therefore, during the 1960s and 1970s, more employers began to introduce personnel policies that combined long-term employment security, training linked to internal promotion, high wages and employee involvement in an attempt to buy workers’ loyalty and avoid or weaken unionisation (Kochan et al., 1986).

The labour market environment

The growth in trade union influence in most countries was supported by developments in the labour market. Unemployment was low throughout the 1950s and 1960s. This enhanced unions’ bargaining power and influence. However, the labour market retained long-established structural features. One of the most important of these was the gendered division of labour, leading to gendered patterns of labour market segmentation. Women continued to be regarded as secondary income earners.

The concept of the man as the main ‘breadwinner’ remained dominant. Consequently, long-term jobs and careers were developed for men rather than women. The fact that household income depended on male earnings shaped trade union demands, which were for better pay, greater job security and better prospects for wage progression for men. During the 1960s and 1970s there was also a growth of legislative protection for workers in many countries, e.g. restricting employers’ freedom to make workers redundant, and laws protecting workers from unfair dismissal.

The wider institutional environment

Developments in the wider institutional environment affected labour market policy and trade union influence. The development of social democracy in Europe after the Second World War involved the fuller recognition of the place of workers and their organizations within the nation-state. This was reflected in a commitment by governments to maintain full employment and create and support welfare states. These commitments reduced, although by no means eliminated, the inequality of power in the employment relationship and thus gave workers greater power to influence their terms and conditions of employment.

The social democratic spirit also led to a greater degree of political legitimacy and support for trade unions, reflected in the development of 'tripartite' institutions of economic management. These involved trade unions, together with government and employer representatives, in decisions concerning economic and social policy. In addition, as shown above, the 1970s saw legal extensions of workers' rights to participate in decision-making at workplace level in countries such as West Germany, Sweden and France.

Restructuring employment since the 1980s: the externalisation of employment?

Since the 1980s, large corporations, particularly in Britain and the United States but also in Europe, have undertaken processes of 'restructuring', aimed at reducing costs and improving responsiveness to more rapidly changing, intensely competitive and less predictable markets. Job cuts on a large scale have been a central feature of the process, as have new patterns of work organisation and changes to employment structures. The effect has been to weaken internal labour market structures (Cappelli et al., 1997; Boxall and Purcell, 2003: 121):

First, employers in Britain, the USA and a number of European countries have made greater use of part-time and temporary labour and in a minority of cases, highly casualised forms of employment such as zero hours contracts (Cappelli et al., 1997; Cully et al., 1999; Millward et al., 2000). During the 1990s, although the total number of jobs grew, there was a net reduction in the number of full-time jobs in Britain. All of the growth in employment was accounted for by a growth of part-time employment. This trend was replicated across the European Union, where the share of part-time jobs in total employment rose from 12.7 per cent to 17.9 per cent and that of fixedterm- contract jobs from 8.4 per cent to 13.4 per cent between 1985 and 2001 (European Commission, 2002: 173).Second, a number of companies have transferred some of their workers from employed to self-employed status by dismissing them and then offering them a contract to perform their job as self-employed workers.Third, employers have reduced their commitment to providing long-term employment security for 'permanent' employees. Increasingly, employers and employers' organisations in Britain and the USA have claimed that workers should take greater responsibility for their own careers and 'employability' and be less reliant on employers to provide long-term employment security and career paths. The risk of job loss increased significantly for managers during the late 1980s and 1990s as restructuring usually involved changes in management organisation. It also increased for workers in occupations previously regarded as offering jobs for life, such as public administration, banking and education (Cappelli et al., 1997; Heery and Salmon, 2000).Fourth, senior managers have 'downsized' and 'delayered' their organisations. This has not only resulted in job cuts. It has also reduced the number of job levels. The result is that workers have fewer opportunities to gain access to internal promotion ladders. This has been noticeable in the banking and finance sector and in supermarkets, where jobs that used to provide stepping stones from junior to more senior grades have largely been eliminated (Cappelli et al., 1997; Grimshaw et al. 2001; Hudson, 2002).Fifth, a growing number of organisations no longer employ their own staff to perform jobs that are not 'core' functions of the business, e.g. cleaning, catering, security, payroll administration, but buy these services in from outside companies instead. In the UK this has been widespread in public administration, the public utilities sector, i.e. electricity, gas

and water, and the financial services sector (Cappelli et al., 1997; Cully et al., 1999).Finally, employers have increased the variability of pay by linking elements of pay to measures of individual, team or organisational performance. This has undermined the principle of the 'rate for the job' which has been an important feature of internal labour markets. It has meant that in some organisations there is no longer a clear pay structure that links to different job levels so as to provide a path to promotion and higher pay (Cappelli et al., 1997; Grimshaw et al., 2001).
We can use the analytical framework developed in the previous section of this chapter to explain these developments.

Changes in employers' labour requirements

The effects of sectoral change – the shift from manufacturing to services The proportion of workers employed in manufacturing has declined in the USA and all the major European Union economies since the 1970s. At the same time there has been absolute and relative growth in the number of people employed in the service sector. The decline of employment in manufacturing and the growth of the service sector have altered the nature of skills required by employers.

Manufacturing is more likely to make use of idiosyncratic technologies and to require firm-specific skills. The growth of service sector employment has been concentrated at two poles – high-level professional and managerial skills at one pole, and low-skilled jobs at the other. High-level professional skills are largely acquired through formal training leading to nationally or internationally recognised qualifications. These skills are predominantly transferable, so there is no strong incentive for employers to develop internal labour markets for these workers, as they can easily move between firms in search of higher rewards.

Under-performers can be dismissed and replaced with new hires from the external (occupational) labour market. At the low-skilled end of the labour market there are even fewer incentives for employers to develop internal labour markets. Even where certain behaviours are needed in order to ensure satisfactory levels of customer service, these are usually fairly rudimentary, easily learnt and transferable. Therefore there is only limited training investment and consequently little need to retain workers in order to protect long-term investments in training. Consequently, it can be argued that the shift away from manufacturing to service employment means that fewer employers have strong incentives to develop internal labour markets.

The effects of increased competition – cost reduction and labour flexibility Since the 1970s, organisations have been subject to increasingly intense pressure from three main sources. First, markets have become increasingly competitive as a result of the emergence of new low-cost areas of production in China, South-East Asia and the Pacific Rim and, recently, Central and Eastern Europe. International competition has been encouraged by tariff reductions and freer trade between countries as a result of long-term projects such as the European Union and the World Trade Organisation.

Within individual countries, government policies of privatisation and deregulation have encouraged domestic competition by enabling more firms to enter certain areas of economic activity, such as mail services, gas, electricity and water supply, telecommunications and transport. Competition has put pressure on producers to reduce costs as well as improve the quality of their products. Secondly, markets for goods and services have become more volatile. Customers are more demanding than they used to be and products become obsolete much more quickly.

As a result of these changes, organisations have to be more innovative and responsive to change. Furthermore, the level of market demand is subject to sharper and more frequent variations than used to be the case, which means that organisations also have to be able to adjust the level of their labour inputs in line with changes in demand for their output.

Organisational restructuringhas been the widespread response to these pressures. Efforts at organisational restructuring have focused on decentralisation of hitherto large, centralised corporations and reductions in headcount in an attempt to eliminate unnecessary labour costs. Increasingly, organisations have sought to cut costs by reducing the number of employees who are not contributing directly to production or service delivery. This restructuring of organisations consists of four main elements:

Downsizing, i.e. reducing the size of the workforce while reorganising the production process and intensifying work so that production can be achieved with fewer workers.Externalisation of those activities that are required by the organisation but are not central to the production process by 'contracting out' or 'outsourcing'. Outsourcing enables firms to reduce the number of workers they employ directly, together with the associated costs, by transferring responsibility for provision to specialist external organisations. Examples of such activities include cleaning and catering, security and maintenance, and some administrative services such as payroll administration.Delayering, i.e. stripping out layers of supervision and management. This cuts employment costs and also, in theory, increases the speed of communication and decision-making by 'flattening' the organisation, i.e. reducing the number of levels in the hierarchy.Devolution of responsibility for decision-making and problem-solving to more junior managers and production workers. This is a necessary consequence of delayering. The result of restructuring is a 'lean' organisation that uses fewer employees to produce the same or a higher level of output. As part of organisational restructuring, employers and governments have come to insist on the need for greater labour flexibility in order to reduce costs and improve quality and competitiveness. From the employer's standpoint labour flexibility refers to the ability of managers to:Vary the size of the workforce in line with demand for output. This aspect of flexible labour utilisation is known as numerical flexibility. This is partly in response to the increased volatility of markets and the consequent unpredictability of demand. Firms cannot afford to carry workers who are surplus to requirements. At the same time they need to be able to respond rapidly to rising demand if they are to retain their shares of the market. Therefore they need to be able to reduce or increase labour inputs in line with changes in demand. Numerical flexibility can be achieved in various ways, i.e. by employing more workers on part-time, temporary, or fixed-term contracts of employment and by substituting outside contractors and self-employed workers for direct employees.Move away from fixed hours of work, such as the 9 to 5 working day. This means making more use of shift-working and part-time working to maximise the utilization of plant and equipment or ensure that customer expectations are met while matching labour inputs to peaks and troughs in demand. This aspect of labour flexibility is known as temporal flexibility.Redeploy workers across tasks and jobs. Employers need to be able to ask workers to perform a wider range of tasks than before. There are various reasons for this. One is that organisational downsizing means smaller workforces. These have to be more productive. This has led managers to reorganise and intensify work in order to raise labour productivity by introducing multi-tasking and multi-skilling to ensure that when workers are not occupied with one task they transfer to another. Another reason is to enable organisations to make effective use of new technology. This creates a need for highly trained workers with a broad range of skills. This aspect of labour flexibility is known as functional flexibility.Control wage and salary costs by linking pay to various measures of performance such as individual performance, team performance or organisational performance, and to local labour market conditions. This is referred to as financial flexibility. Employers' search for labour flexibility has led to an attack on 'rigidities' associated with internal labour markets and structured occupational labour markets. Both the narrowly defined jobs of the industrial internal labour market and the demarcation lines between jobs in structured occupational labour markets are claimed to be incompatible with the need for functional flexibility of labour. Narrowly designed jobs that are separated from each other by clear boundaries do not allow management to make full use of new technology and new methods of work organisation, which require broader skills and more versatile, adaptable workers. Pay scales that set a uniform rate of pay for the job, as in both variants of internal labour markets and in structured occupational labour markets, are seen by managers to be incompatible with their desire to link pay to team or individual performance. Finally, the guarantees of long-term employment and career progression associated with salaried internal labour markets restrict management's ability to adjust the size of the workforce in response to changes in market demand.Organisational constraints Increased international competition, combined with financial deregulation and the mobility of capital, has reinforced pressures on British and US firms to maximise shortterm profits to meet the demands of shareholders and introduced them to countries where they used to be relatively absent, such as Sweden and Germany. These pressures make it harder for senior managers to commit themselves to long-term investment in workers' training and provisions for long-term employment security and career progression. Furthermore, the successive rounds of job cuts that were made during the 1980s and 1990s as corporate restructuring aimed to create 'lean organisations' meant that many firms reduced or ended their commitment to long-term job security for employees. In addition, externalisation, decentralisation and delayering have also meant that organizations are smaller and more fragmented and have fewer hierarchical levels. This has broken up the internal promotion ladders that underpinned salaried internal labour markets in previously large, centralised corporations (Hudson, 2002). Employee pressure and influence Changes in the labour market environment and the wider institutional environment have weakened workers' bargaining power and their ability to influence employment systems. High unemployment in the main European economies during the 1980s and 1990s weakened trade union membership and bargaining power. The impact of unemployment was reinforced by government policies that were aimed at reinvigorating European capitalism by encouraging competition and restricting the power of organised labour. In Britain the decline in trade union membership and power was dramatic, leading to the erosion of the trade union-based industrial relations system that had developed after the Second World War. This reflected the collapse of employment in manufacturing during the 1980s together with anti-union policies and legislation that were implemented by Conservative governments under Margaret Thatcher and John Major during the 1980s and 1990s and have largely continued under Tony Blair's Labour government since 1997. In other countries such as Sweden, France and Germany, although unemployment rose significantly, public policy did not shift powerfully against the unions as it did in Britain. Thus while union membership has declined in relation to the employed workforce and unions have been forced to make concessions to employers in order to reduce costs, maintain competitiveness and save jobs, unions have not lost their influence in employment matters to the same extent they have in Britain. Thus it is to varying extents that employers have a freer hand to restructure employment systems in line with their own needs and constraints and with less regard to pressure from employees. The labour market environment The 1970s in Europe saw a slowing down in the rate of economic growth, increasing inflationary pressures and rising unemployment. Unemployment increased more rapidly during the 1980s and 1990s.

For example, unemployment across the 12 member states of the European Union (excluding East Germany) rose from 3.7 per cent in 1975 to 9.9 per cent in 1985 and was still 8.1 per cent in 1991. In 2001 the unemployment rate across the 15 member states was 7.4 per cent (European Commission, 1996, 2002). On the supply side of the labour market there has been a significant increase in the proportion of women in employment. Across the European Union the proportion of women aged 15–64 in employment rose from 45.1 per cent in 1985 to 54.9 per cent in 2001 (European Commission, 1996, 2002).

In the UK and the USA there has also been a significant increase in the number of young people in part-time employment. This reflects the growth in the number of young people in further and higher education, for whom part-time or temporary work is a convenient way of supplementing their income. In terms of Rubery's analysis outlined earlier, these groups have swollen the secondary segment of the labour market, providing a pool of cheap yet compliant labour from which employers can draw and so avoid having to invest in positive incentives to obtain desired levels of behaviour at work.

Policies that are currently aimed at increasing labour market participation among ethnic minorities, women and older people may add to the disadvantaged segments of the labour market unless they are linked to improvements in educational and training opportunities and forms of regulation that deter employers from adopting 'cheap labour' policies. However, high unemployment and low rates of job creation have led to growing criticism of labour market regulation in many EU member states. It has been argued increasingly that high levels of protection against dismissal and restrictions on employers' freedom to employ people on part-time and temporary contracts deter employers from creating new jobs.

The proposed remedy has been to increase labour market flexibility by reducing these protections and restrictions and in some cases by legislating to reduce the bargaining power of trade unions. Nevertheless, the European Union has not followed a simple course of labour market deregulation. Instead it has tried to encourage increased labour market flexibility within a reformed framework of regulation. While this has meant relaxing a number of regulations limiting, for example, the employment of workers on temporary and fixed-term contracts, there is a commitment to ensuring that such 'non-standard' workers enjoy the same employment rights as full-time, permanent workers (European Commission, 1999).

The European Commission has also espoused the principle that in a more flexible, decentralized labour market, workers should have enhanced rights of representation and participation in decision-making (Gill et al., 1999). This is linked to the Commission's continued emphasis on the importance of Europe competing internationally on the basis of highly skilled, adaptable workforces (see Chapter 16 for further discussion). The most radical policy shift in the direction of labour market flexibility has occurred in the UK, where trade unions and collective bargaining, rather than government legislation, were traditionally the main curbs on unilateral management action.

The decline of trade union membership and collective bargaining coverage that resulted from economic policy and anti-union legislation during the 1980s and 1990s, together with the determination to minimise statutory protection for workers as far as possible, means that the British labour market is now the least regulated in Europe. Originally a Conservative government project, labour market flexibility has continued to be a priority for the Labour government since 1997.

The introduction of a national minimum wage, the strengthening of workers' protection against unfair dismissal and legislation providing trade unions with a legal right to claim recognition from employers can be seen as a partial reversal of some aspects of Conservative policy. However, the level of the minimum wage is low, workers in Britain continue to have weaker employment rights than their counterparts in Europe and British trade unions continue to be subject to the most restrictive laws in the European Union.

The current government claims that labour market flexibility has enabled Britain to reduce unemployment far more successfully than the more highly regulated economies in Europe such as Germany and France. However, Britain has a higher incidence of low-paid employment than other major European economies and the most unequal earnings distribution (Rubery and Edwards, 2003). To varying degrees therefore, changes in the labour market emvironment have given employers greater freedom to restructure employment systems in line with their changing labour requirements and organisational constraints.

The wider institutional environment

These policy shifts have been closely linked to radical changes in economic institutions. Financial markets have been deregulated, allowing capital to flow freely from one financial centre to another in search of the best possible short-term profits. This, together with advances in information and communications technology, has helped stimulate the growth of multinational corporations, which began during the 1970s. Furthermore, increasing pressures for free trade in goods and services, embodied in the formation of the Single European Market, the North American Free Trade Agreement and the World Trade Organisation, have given further stimulus to international competition and the internationalisation of production.

This has in turn intensified the pressures on governments to pursue economic policies that are acceptable to international investors, such as promoting labour market flexibility, and on firms to offer consumers better value for money by reducing costs and prices while improving the quality of products and services. These pressures have also been transmitted to workers and their unions. They are increasingly aware that the continuation of jobs depends on maintaining the competitiveness of their workplaces.

This competition is not confined to competition between companies. Multinational companies scrutinise the performance of their plants in different countries, comparing cost and productivity levels and concentrating investment in those that are deemed to be most efficient. This means that workers employed in different plants of the same company are in increasingly direct competition with each other. The consequence is that workers and their unions are less able to influence terms and conditions of employment or resist managerial initiatives aimed at weakening internal labour markets.

This is true even in economies such as Germany, where public policy has not shifted as radically in favour of labour market flexibility as in the UK (Katz and Darbishire, 2000; Whittall, 2001).