Research Note
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Kinship Pressure and Firm-Worker Matching Distortions

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Many small businesses in low-income countries hire employees from their kinship networks. This fact is often attributed to hiring from the kinship network reducing contracting frictions or informational asymmetries. In this paper, I test for the possibility that some of this hiring is due to redistributive pressure: i.e. that firm owners face a social cost when they do not choose a relative employee for a job. I run a field experiment with small firms in Zambia to test this hypothesis, and find that firms are less likely to hire their relatives when they are offered plausible deniability for not doing so.

Introduction

Firms are considered to be an engine of growth for the developing world, yet the vast majority of firms in these economies have few employees, and are relatively unproductive (Hsieh and Klenow 2009; Hsieh and Olken 2014; McKenzie 2017). Labour market frictions are posited as a possible constraint to firm growth (Hardy and McCasland 2015): few businesses hire and when businesses hire employees, "the vast majority of microenterprises have no employees outside the owner's family'' (Jayachandran 2020). The available data corroborates this (De Mel et al. 2008). This propensity to hire relatives is often attributed to contracting frictions and missing information markets, implying that the optimal policy response is to create policies designed to alleviate adverse selection or moral hazard that might lead to better firm-employee matches.

The hypothesis of this project is that redistributive pressures and insurance arrangements may be an important reason that some businesses hire relatives as employees. Specifically, I hypothesise that hiring kin might crowd out the hiring of more productive non-kin, and that this matching may result from social pressure or social norms. A substantial literature in anthropology suggests that firms hire relatives not as the optimal response to contracting frictions, but rather as a result of kinship pressure or mutual insurance arrangements (Akyeampong et al. 2014). In these accounts firms are often reluctant to hire relatives, who are often worse employees than non-relatives due to negative selection (less able relatives request jobs) and greater moral hazard (firm owners find it difficult to levy sanctions on their relatives). This interpretation is consistent with the cross-sectional evidence that exists, showing negative returns to hiring relatives (Fafchamps and Minten 2002) as well as the literature on family firms in developed economies, which has proposed that family firms may exist for cultural as much as efficiency reasons (Bertrand and Schoar 2006). If this hypothesis is correct, the result might have important lessons for policy: rather than attempting to remedy contracting or information markets when firms operate as a mechanism to provide insurance to kin, policy may fix insurance markets to better promote firm growth.

Context and Methodology

To test for the role of redistributive pressure shaping firms' hiring decisions, I conduct a field experiment with owners and managers of micro, small and medium enterprises in Chipata, Eastern Province, Zambia. The enumerators randomly sampled businesses from all markets in town. Our sample comprised all businesses in which: i) the owner had working age relatives nearby they were able to hire, ii) the business operator said they had authority to make hiring decisions, and iii) they were willing to hire an employee if offered a subsidised wage. In total, firms that met this condition made up 60% of all sampled businesses. Around 50% of eligible businesses are in the retail sector, 10% in manufacturing, and 10% in agricultural processing, while the remainder are distributed across other sectors. The proportions of retail and manufacturing businesses are similar to the proportions found in the 2023 census of Lusaka, Zambia used by Ashraf and coauthors (2023). 60% of eligible businesses have an employee – a proportion that is slightly higher than Ashraf et al 2023. However only 40% of these businesses classify their worker as full time, with the majority of the remainder classifying their employee as part time.

Consistent with the prior literature, relatives do appear to be more likely to be hired for particular jobs. Consistent with Bloom et al 2013, they are 12 percentage points more likely to be hired for a job in management, 30 percentage points more likely to be hired for jobs involving money, and they become increasingly likely to be hired as employers rank the job as requiring more trust. However, relatives are also hired around 30% of the time for jobs that do not involve management, money and lower levels of trust, suggesting that other channels might also explain the reasons such individuals are hired.

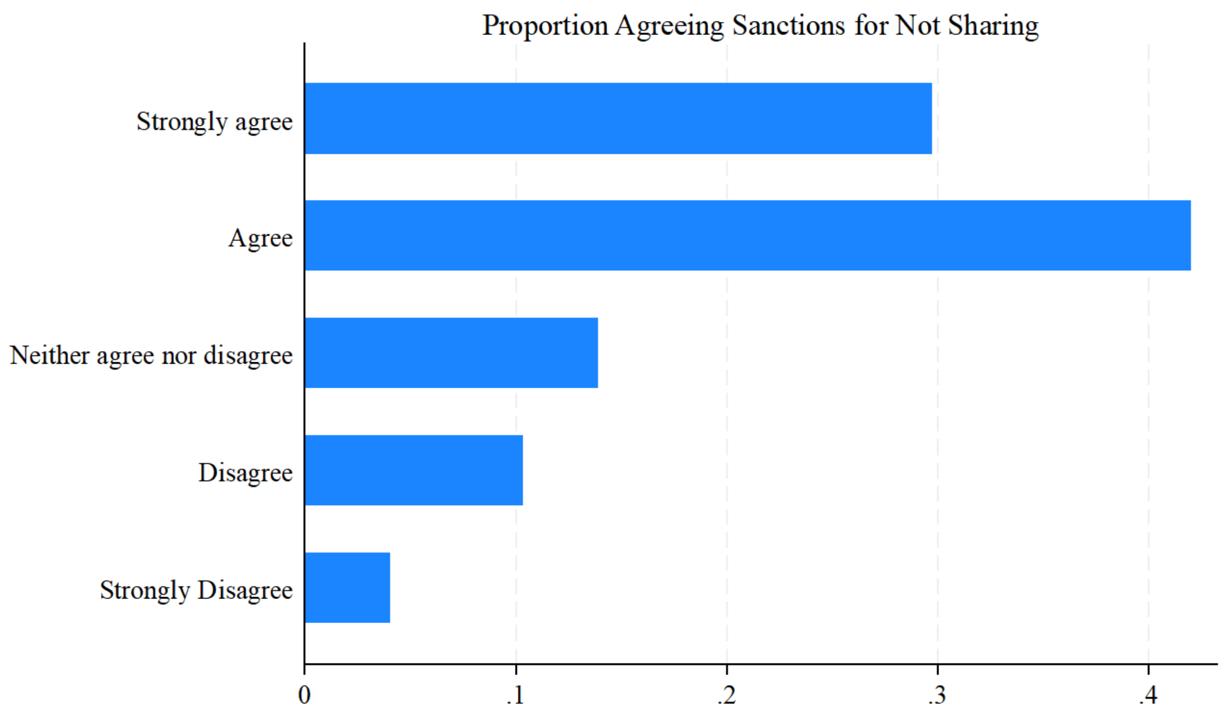
To test for the role of pressure as a hiring determinant, I conduct a field experiment that offers business owners the opportunity to hire an additional employee at a subsidised wage, and then examines whom businesses choose to hire for the position. Importantly, before making the hiring decision, employers are offered one of two posters: 1) a control poster, 2) a treatment poster that states that the person hired for the position might not have been the first choice of the employer themselves. This latter poster offers employers some plausible deniability – in the event that someone comes and complains that they were not selected for the position, the business owner can point to the poster and state that they did not have control over the hiring decision. This poster was designed based on focus group interviews that suggested that business owners face sanctions for choosing to hire someone unrelated when there is someone related who would be interested in the job. Therefore, comparing who businesses choose to hire in control and treatment conditions offers a test of how different expectations of social pressure change hiring choices.

To operationalise the experiment, in a baseline survey the enumerators explained to employers the characteristics of the subsidy, and asked to identify a relative and non-relative candidate they would be interested in hiring for the position. In a second visit, after identifying the candidates, employers are informed that they will be randomly assigned to receive a subsidy for the relative candidate, the non-relative candidate, or for their "choice" of the two. Finally, before knowing which group they will be assigned to, firms are randomly assigned to one of the two poster groups, and are asked to make their choice of who to hire if they are in the choice group. Finally, at the end of the experiment, employers are randomly assigned to one of the groups, and their choices are implemented probabilistically.

Main Findings

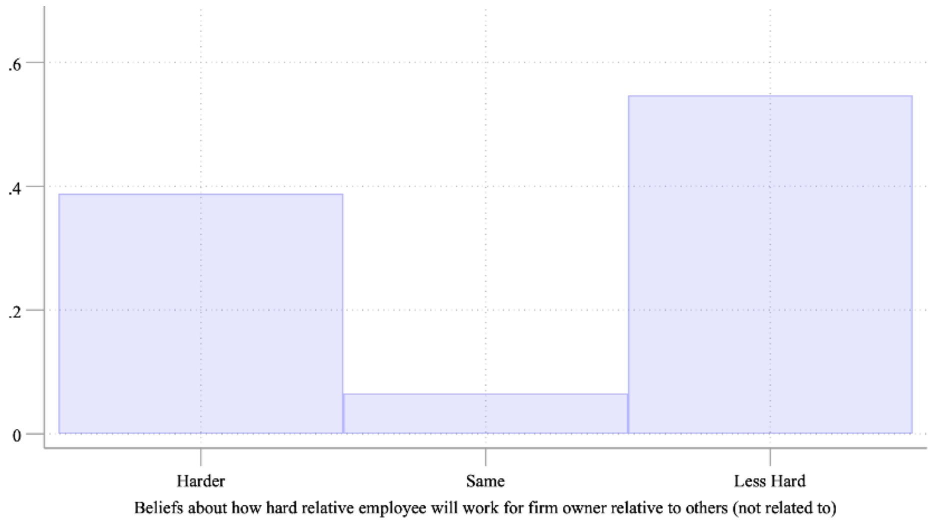
The experiment has several main results. First, there is high agreement at baseline among microenterprises that they can face social costs for not sharing with their kinship network. Figure 1 shows that more than 70% of firms Agree or Strongly Agree with the statement that there can be social costs for not sharing with one's kinship network.

Figure 1: Responses of firm owners to whether they would face sanctions if they were asked to share with their relatives and did not.



Second, baseline results also indicated that some hiring of relative employees may be undesirable from a productivity perspective. Consistent with the existing literature (see e.g. Falco et al 2022) there is heterogeneity in firm owner's expectations regarding whether employees who are related to the firm owner will work harder, or less hard, for them as compared to unrelated employers. While almost 40% of employers expect their relative to work harder for them, more than half expect their relative to work less hard. This appears to be related to the fact that employers expect it to be difficult to sanction employees who they are related, with many stating that it would be difficult to sanction related employees who do not perform well.

Figure 2: Responses of firm owners to how hard they expect a relative employee to work for them, as compared to another business owner they are not related to.



Third, pressure appears to contribute to the tendency to hire related employees and particularly those that are not desirable employees from the firm's perspective. Firms who receive the treatment poster reduce the likelihood of hiring a related employee by 15 percentage points. Moreover, this pressure appears to be concentrated among less desirable employees: treatment effects are larger for employers who state that their relative is likely to work less hard for them as compared to another employer they are unrelated to.

Additional tests in the paper suggest that firms' hiring choices are driven by the perceived costs of not choosing to hire one's relative, rather than the perceived benefits. They also suggest that the effects are not driven by the selection of employees brought to the experiment. Altogether – the results indicate a role for social norms in determining firms' hiring choices.

Policy Implications and Future Research

This project suggests that at least some hiring in small businesses may be driven by redistributive pressures. This project may partly explain why existing literature in development economics has generally found only muted impacts for programmes designed to reduce search costs or contracting frictions in labour markets.

However, policies that seek to reduce social pressure may not be optimal. A long literature in economics has studied informal insurance arrangements and these likely have important welfare benefits for their members, which make the associated hiring costs worthwhile. Therefore, an important direction for future research is to better understand the micro-foundations of these redistributive arrangements, as well as their interlinkages with hiring decisions. Moreover, it may be interesting to explore whether hiring decisions and pressure are reduced when formal welfare systems expand.

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