NAYSAYERS, BEHOLD! OUTSOURCING IS BENEFICIAL TO THE UNITED STATES

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ASBSTRACT

One obvious result of World Trade Organization (WTO) and the subsequent North American Free Trade Agreement (NAFTA) is the migration of a large number of manufacturing jobs in the United States (US) to Mexico and other developing countries with plenty of cheap labor. As a result of rapid progress in information technology, many companies in the US are now outsourcing many jobs even in the white-collar services sector to India, China and other countries to take advantage of their low cost and highly skilled work force. About three million service jobs are expected to be outsourced from the U. S. mostly to Bangalore, India by the year 2015. Many state and local governments are also beginning to outsource jobs in information technology to foreign countries. Outsourcing has become a crucial economic and political issue in the presidential election campaign. Many politicians are threatening to bring legislation to levy taxes on companies that outsource jobs. But few realize the fact that outsourcing is not harmful but beneficial to the U. S. economy in the long run. People in every region of the world would be able to obtain the best goods and services at the lowest prices.

INTRODUCTION

One obvious result of WTO and NAFTA is the migration of a large number of manufacturing jobs to Mexico and other developing countries with plenty of cheap labor. Rapid progress in information technology brought in another unexpected phenomenon. Many companies in the United States (US) are now exporting many jobs even in the services sector to India, China and other countries to take advantage of their low cost and highly skilled work force. About three million service jobs are expected to be outsourced from the US mostly to Bangalore, India by the year 2015. This phenomenon is not limited to private sector alone. Many state and local governments, starving for cash, are beginning to outsource jobs in information technology to foreign countries. Outsourcing is hitting even skilled jobs that were once thought to be safe across a wide range of white-collar work force. The main reason for the speed and size of this shift is the nature of service work. Unlike manufacturing jobs which need years of time and billions of dollars to erect plants overseas, service jobs need only a desk, a computer and Net access. The recent trend of jobs migrating from the United States to India and China has created an economic and political storm in the US. Many supporters of liberalization of world trade are now worried that the migration and outsourcing of jobs to the developing countries could jeopardize the free trade movement. Outsourcing has become a crucial economic and political issue in the presidential election campaign. Several legislators in the US Congress are threatening to bring legislation to levy taxes on companies that outsource jobs. Some state governments are also planning to follow suit. To many people, outsourcing means eliminating jobs in the US and exporting them to poor countries such as India and China. There is no dearth of naysayers who are loudly claiming that this present advent of wholesale outsourcing would spell permanent loss of jobs and economic doom to the US. But few realize the fact that outsourcing is not harmful but beneficial to the US economy in the long run. Many well known economists are of opinion that outsourcing is closely related to global trade and is beneficial to all concerned parties. They assert that people in every region of the world would be able to obtain the best quality goods at the lowest prices. However, the fierce debate on outsourcing continues unabated.

FUROR ON OUTSOURCING

The term outsourcing is defined as the work done for a company by people other than the company's full-time employees (*www.Outsource2india.com*, 2004). According to Pfannenstein (2004), the most common definition nowadays includes turning over a firm's computer operations, network operations software development, or other functions to a provider for a specific time. Another related term, off-shoring, is used in the US to specifically refer to outsourcing to another country, mainly to India, Ireland, China, and other countries. But, in the present furor about outsourcing, the two terms are being used as synonyms. Gnuschke (2004) states that outsourcing occurs when an organization transfers some of its tasks to outside suppliers and that offshore outsourcing occurs when these tasks are transferred to other countries.

Riegle (2004) identifies four major socio-economic epochs (ages) in the history civilization, classified by the primary activity engaged by human beings in each age.

SOCIO-ECONOMIC EPOCHS

Age	Dates	Primary Human Activity
Stone	1,000,000 B.C. - 6,000 B.C.	Hunting and Gathering Food
Agricultural	6,000 B.C. - 1750 A.D.	Farming
Industrial	1750 A.D. - 1975 A.D.	Working in Factories
Information	1975 A.D. - the present	Acquiring, Analyzing, and Communicating Information

Source: Rod Riegle: Education in the Information. www.coe.ilstu.edu/rpriegle

According to Riegle (2004), the Information Age differs from the Industrial Age as follows:

The Information Age is characterized by the value of information, rather than raw materials and physical labor. For example, one of the main products of the

Industrial Age is the automobile. Sixty percent of the cost of an automobile is due to the raw materials (e.g., steel) and physical labor needed to produce it. This is in sharp contrast to one of the main products of the Information Age - the computer. Only two percent of the cost of a computer is due to the raw materials and labor. Over 98% of the price we are paying is for the information (software and patents) necessary to produce it. In the Information Age, information - not raw materials and physical labor - is power (Riegle, 2004)

Riegle (2004) gives a list of some startling facts about what it means to us:

1. More information was produced in the last 20 years than the previous 5,000.
2. Information is doubling every 4 years.
3. A typical weekday edition of *The New York Times* contains more information than a person would encounter in a lifetime in the 17th century.
4. 80% of new jobs require sophisticated information handling skills.
5. Jobs that involve the Internet pay about 50% more than jobs that do not.
6. Artificial intelligence is expected to affect 60-90% of all jobs in organizations; augmenting, displacing, or eliminating workers.
7. In the next five years, 80% of workers will be doing jobs differently from the way they have done them over the past 50 years.

Thus, to survive, individuals, organizations, and nations must acquire, analyze, and communicate information more quickly than their competitors (Riegle, 2004).

As Kirchhoefer (2004) observes, outsourcing is the logical extension of the evolutionary process that began with contract manufacturing and continued into corporate services. Lou Dobbs, one of the most vociferous critics of outsourcing, stated that, “for the first time in this country’s history, we are shipping jobs overseas to provide products and services for export back into this country” (Cocheo, 2004). Dobbs equated outsourcing to “exporting America” and suggested that CEOs of the outsourcing companies should be censured or out right fired. Some economists in India called the growing political backlash in the US against outsourcing, “the Lou Dobbs Effect” (Angwin, 2004). Commenting on the outsourcing debate, Kirkpatrick (2004) observed that,”seldom have so many had such strong opinions about something they understood so poorly.”

IN 2004, outsourcing took on a different meaning. “It now refers to a specific segment of the growing international trade in services,” (Bhagwati, 2004). Typical examples of the present outsourcing are, phone call centers staffed in Bangalore, India to serve customers in New York, x-rays transmitted digitally from Boston to be read in Bombay, or with direct purchases by individuals who hire an offshore firm to provide design plans. The members of President Bush’s Council of Economic Advisors (CEA) also recognized that,” outsourcing of professional services is a prominent example of a new type of trade” (Mankiw et al, 2004). Tumulty et al (2004) state that the topic of “outsourcing packs a powerful new wallop … because it hits middle and upper income workers – software engineers, X-ray readers, financial analysts – who thought they were immune to the great job exodus to Mexico and China that has decimated blue collars over the past 25 years.”

Mankiw, the chair of the CEA, made a similar point in a press interview when he said, “I think outsourcing is a growing phenomenon, but it is something that we should realize is probably a plus for the economy in the long run” (Andrew, 2004). Mankiw’s comments added a lot fuel to the fiery debate. As Abelson (2004) stated, many Democrats considered Mankiw’s observation as a, “flagrant proof of the Bush administration’s stone-hearted response to the wholesale and growing export of jobs to cheap labor locales. Edgy Republicans, themselves hardly unmindful of November (elections), pecked at poor Mankiw, as well." As for the comment about outsourcing being the long run plus for the economy, Abelson (2004) sarcastically opined that, "Mr. Mankiw is a scholar and he views economic trends with a generous time frame, as evidenced by his careful qualification that benefits from outsourcing would accrue over 'the long pull.' Of course, as a somewhat more celebrated economist, John Maynard Keynes, pointed out decades ago and has yet to be definitively proved wrong, in the long pull, we're all dead."

THE NUMBERS ON OUTSOURCING

The actual situation of statistics regarding the number of jobs involved in outsourcing is as follows. The best known projection is done by McCarthy (2002) at the Forrester Research, an information technology consulting firm. According to his estimate, more than 3.3 million jobs are projected to leave the country by 2015. According to Drezner (2004), the predictions of job losses in the millions are driving the current outsourcing hysteria. He cautions that it is crucial to note that these estimates are gross, not net, losses. No one much worried about job outsourcing during the 1990s because more jobs were being created in the US economy than the ones leaving. The predictions would not seem as ominous once they are analyzed closely. Outsourcing overseas is not an available option for about 90 percent of the total jobs in the US. These jobs include service areas such as retail, restaurants, marketing, personal care etc., which require geographical proximity between producers and consumers. About 10 to 11 percent of the jobs have been identified as at risk of being sent abroad. These include any service jobs that can be sent through fiber optic wires, jobs such as telephone call centers, computer data entry operators, business and financial support, paralegal and legal assistants, accounting, bookkeeping, payroll etc. (McCarthy, 2002).

Even if the most frightening forecasts of job outsourcing prove to be accurate, the net impact of such outsourcing on the US economy would be negligible. The Estimate of 3.3 million jobs lost is for a period of 15 years. That amounts to about 220,000 jobs lost per year. The number may sound considerable until one realizes that the total employment in the US now is approximately 130 million. As Drezner (2004) points out, about 22 million new jobs are expected to be added by 2010, reducing the outsourcing effect to less than 0.2 percent of total employed Americans.

THE NAYSAYERS TO OUTSOURCING

The panic over outsourcing presents a powerful motivation to politicians to take recourse toward protectionism. The prevailing panic over offshore outsourcing has driven several law makers to call for legislative measures to curtail the process. A recent white-paper from US Senator Liebermann's office (Liebermann, 2004) lists no less than 13 different proposals for US federal legislation for limiting the scope of offshore outsourcing. 33 US states also have introduced similar measures of legislation since May 2003 (Kirkegaard, 2004). Such attempts toward restricting free trade would be dysfunctional to both providers and consumers. Zaremberg (2004) warns that protectionist legislation that blocks a business from using outsourcing to control costs is certain to cause a net loss of jobs in the industries covered by the restriction and lead to retaliation by our trading partners. The present phenomenon of outsourcing is part of an inevitable evolutionary process. Ezrati (2004) provides a list of such naysayers of the past:

1960: John Kennedy, in his presidential campaign, spoke of foreign competition carrying “the dark menace of industrial dislocation, increasing unemployment, and deepening poverty.”

1970: Prominent financier, Felix Rohatyn, bemoaning over the threat from Japan, talked about, “de-industrialization and the prospect of America becoming a nation of short-order cooks and saleswomen.”

1975: Senator Lloyd Bentsen (D-TX) expressed his worries that, “American workers will end up like the people in the biblical village who were condemned to be hewers of wood and drawers of water.”

1996: Walter Mondale, while serving as US ambassador to Japan, suggested that Americans would soon be fit only to sweep the floors in the Japanese factories.

1985: When Japan began to go into stagnation and the foreign threat shifted to Mexico, the then presidential candidate H. Ross Perot could hear the “giant sucking sound” of lost jobs to Mexico.

1990: On the edge of the great technological leap of the 1990s, a Pulitzer prize went to two journalists, Donald Bartlett and James Steele for their book on America’s decline: What Went Wrong.

2004: Even the eminent economist, Paul Samuelson, argues recently that the loss of our competitive advantage to low-wage countries such as China and India would be permanent (Samuelson, 2004)

At almost all the above junctures, there were demands for protectionist measures. Ezrati (2004) noted that, fortunately, the nation has so far resisted this misguided solution. Instead, the US coped with each situation by applying its genius for productivity enhancement, technological innovation and product development.

RAPID RISE IN OFFSHORE OUTSOURCING

Kirkegaard (2004) and others identify four factors that significantly contributed to the recent rapid rise in offshore outsourcing.

1. Technological Innovation: Rapid progress in innovation has enabled large price decreases and the consequent diffusion of information technology (IT). Since the late 1990s, it also paved the way for rapid decline in the prices of telecommunication connections. Because of India’s recent investment boom on undersea fiber optic cables, the country’s capacity to exchange electronic data worldwide would sky-rocket, boosting India’s enormous cost advantage. The cost of transmitting work offshore to India is expected to drop by at least 60 percent next year (Baker, 2004).

2. Free Trade: Deregulation of the service industries and trade liberalization by both developed and developing countries largely contributed to the growth of international trade in services. The outsourcing sector has been free of any regulatory barriers so far. The growth has been entirely market oriented. As Nilekani (2004) observes, the US has all along been pushing the nations like India to free up their markets and now we are seeing the results.

3. Cost Savings: Lower production costs in foreign countries such as India and China are a major cause of service-sector offshoring (Garner, 2004). Ezrati (2004) holds that low foreign wages pose a great challenge to US work force.

4. Access to a Large English-Speaking, Skilled Labor Pool: Several countries, such as India and the Philippines, have large pools of highly skilled, English-speaking labor. The ability to speak English is crucial in facilitating smooth and continuous interaction between business units from different countries (Ezrati, 2004). These countries also have a large workforce highly educated in technological areas. For example, In India, the number of college graduates each year is only about double the number of graduates in the US. However, the number graduating in India with degrees in mathematics, science and engineering is from five to ten times greater (Challenger, August 2004).

BENEFITS OF OUTSOURCING

Most of the participants in the raging debate on outsourcing are of a firm opinion that outsourcing is beneficial to the US economy and also to all the providers and consumers involved in the process. The principal benefits are listed below:

Cost Savings: Companies are outsourcing jobs and importing services to cut cost, increase productivity, and meet customers' demands for low-price, high-quality goods and services (Challenger, December 2004).

Boost for the US Revenues: As a result of outsourcing, US firms save money and become more profitable, benefiting shareholders and increasing returns on investment. For example, a recent report released by McKinsey Global Institute concluded that for every dollar spent on business process that is outsourced to India, the US economy gains at least $1.14**. A** large portion of that amount, nearly 58 cents, goes back to the original employer. Additionally, 30 percent of Indian offshoring is performed by US companies in India, thus enabling them to bring more monies home as earnings (Kirkpatrick, 2004).

Higher Productivity: There is an enormous power in globalization and outsourcing to reduce prices and thus help spread the benefits of new technology throughout the economy. For instance, outsourcing of production offshores during the 1990s was responsible for 10 – 30 percent of fall in hardware prices. These lower prices led to higher US productivity growth and added nearly $230 billion of extra GDP between 1995 and 2002 (Mann, 2003).

24/7 Service: There are also other benefits that US customers receive from 24 hours a day call centers that became more efficient because of offshore support in other time zones.

Redeployment of Labor: US labor can be redeployed to more competitive, better-paying jobs by sending lower level jobs overseas and enabling the American workforce to move into higher-paying jobs (Marks, 2004). Contrary to the common belief that US is importing massive amounts of services from low-wage countries

(Lou Dobbs, 2004), in 2002, the US generated a surplus of $64.8 billion in services (Drezner, 2004).

Non-Monetary Benefits: Many developing countries have reduced their trade barriers at the instance of the US and it is in the interests of the US that these countries are rewarded. Some of the countries in which the US has set up outsourcing facilities, including India, Philippines and Poland are staunch supporters of the US in the war on terrorism. The US gains heavily from the political stability spurred by economic growth in these countries as result of outsourcing (Drezner, 2004).

Insourcing: Peter Drucker (2004) points out that very few people in this debate seem to realize that the US imports twice as many jobs as are exported. For instance, Bureau of Economic Analysis data show that, "between 1991 and 2001 for 2,500 multi national companies, for every job outsourced abroad, multinationals created nearly two jobs in the US," (Challenger, December 2004).

SUMMARY AND CONCLUSIONS

The number of jobs lost due to offshoring in the service sector is very small compared to the total US employment. It is likely to increase rapidly in future because of sweeping progress in IT and fiber optic technology and the availability of very low-cost , highly educated and skilled English –speaking workforce in India, China and other countries. Outsourcing displaces some of the US workers but it is not expected to permanently lower the US employment or its production superiority. It is expected to bring global prosperity and benefit both the providers and the consumers of the outsourced services alike. As Thottam, et al (2004) point out, the present phenomenon of outsourcing is part of an inevitable evolutionary process. Some jobs will be lost but some other jobs will be created.

Structural changes like this in our economic environment are inevitable and recurring. Every transition can be painful. The US government has so far resisted the temptation for legislating trade barriers against outsourcing. Such measures would further complicate global trade negotiations and are not likely to save many jobs at home. The temporary discomfort due to dislocation in jobs has to be met with greater unemployment support and continuous education and retraining for our workforce. Our educational system has to be modified to encourage and facilitate present and future generations of students in high schools and colleges to study and excel in mathematics, science and engineering related fields to fill the thousands of jobs that are expected to be created through innovations in new sectors such as biotechnology and nanotechnology.

As Murray (2004) observes, the US is the strongest and the most competitive economy on the face of the earth, with no others coming even close. It is the most flexible economy in the whole world. It is easy to lose a job in the US but it is also easy to find a new job. As a result, we have a constantly churning and rejuvenating economy. Outsourcing is not a symptom of America's decline. It is part of a process that prevents decline. As Humphrey (2004) recognizes, many economists are of opinion that innovation, and its offspring, offshore outsourcing, are beneficial for the overall American economy and promise to create more jobs in the long run than they destroy in the short.

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