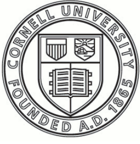

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IWS Issue Brief - Where in the World Is Your Job Going?

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IWS Issue Brief - Where in the World Is Your Job Going?

Abstract

Let's say you have a job processing credit card receipts, answering calls to a customer hotline, reading X-rays, or writing software code. Then one day the boss announces the facility is closing and you, along with all your co-workers, will be laid off. Shortly after, you learn from a news report in the local paper that workers in India are now performing the tasks that used to be handled in your office. In the article the company explained its decision to "offshore" jobs by noting the sizeable gap between the wages earned by its former employees in America and those earned by workers in that far away country.

Keywords

job, labor, worker, America, economic, trade, goods, services, skill, federal, government, offshoring, pay, export, foreign, wage

Comments

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IWS Issue Briefs

Where in the World Is Your Job Going?

Let's say you have a job processing credit card receipts, answering calls to a customer hotline, reading X-rays, or writing software code. Then one day the boss announces the facility is closing and you, along with all your co-workers, will be laid off. Shortly after, you learn from a news report in the local paper that workers in India are now performing the tasks that used to be handled in your office. In the article the company explained its decision to "offshore" jobs by noting the sizeable gap between the wages earned by its former employees in America and those earned by workers in that far away country.

From the employer's point of view, sending high-priced, labor-intensive jobs overseas is an irrefutably good deal. Lower labor costs open up a range of strategic opportunities, from holding down price increases to buying more equipment, investing in new lines of business, or boosting bottom line profitability. If other companies pursue a similar cost-saving path, the overall effect on the economy would be positively buoyant. Economic resources (capital and labor) would drain away from industries that can be mounted and managed at lower cost elsewhere and flow to those where the United States has a comparative advantage. These growth sectors would hire more workers and trade would ensure consumers could choose from a variety of moderately-priced options. Meanwhile, the countries sending us goods and services would become wealthier and begin demanding more of our goods and services.

From the laid-off worker's point of view, the benefits of offshoring might not be so obvious. Losing a job is hard enough, but when the industry you work in shrinks because jobs are moving abroad, your chances of finding comparable work at comparable pay diminish sharply. Your employer-sponsored health insurance and retirement plan disappear along with your good job, and unemployment insurance carries you only so far. When you finally realize you will need to retrain by retooling your skills, you are stymied. You have no idea which industries are expanding and will offer the job security or life style to which you were accustomed. And for a variety of reasons too arcane to fathom, you don't qualify for any of the limited training and education programs offered by the federal government that are intended to help displaced workers.

This, then, is the crux of the problem: Economic theory tells us – and data support the premise – that trade in goods and services enlarges the size of the economic pie, making a generalized "all of us" winners in the long run. What sometimes gets overlooked, though, is that trade, helped along by technological advances, changes the relative size of the slices consumed by each specific "one of us." This means some industries and some individuals (e.g., investors, managers, and workers) grow fatter while those whose jobs migrate offshore are left to feed off the crumbs. In other words, the macro gains that are disbursed generally across the economy over a period of time impose heavy short-run costs on particular workers whose skill sets and experience hold little value in the new order. That we as a nation have not yet determined who, if anyone, is responsible for easing the burdens of offshoring has made the practice a contentious political issue.

Jobs Move Abroad Because…

The export of jobs to lower-cost foreign producers is hardly a new phenomenon. American manufacturers began sending work abroad in headline-grabbing numbers more than 20 years ago, extending to Mexico, Asia, and Eastern Europe a parallel intra-country migration of jobs from the industrial north to the rural south and Midwest, where specialized contractors paid lower wages, provided fewer benefits, and boasted financial structures that kept costs to a minimum. Americans have since grudgingly adjusted to the shrinking number of blue-collar jobs, a process that reflects expanding international trade as well as continuous gains in productivity.

Over the past year or so, offshoring has drawn renewed attention because it is now affecting white-collar service and technical occupations, as well. Once thought immune to foreign trade, the "output" of workers in computing, finance, telecommunications, telemarketing, medical services, research and development, and even illustration is increasingly part of the import-export stew. The global exchange of goods and services has become so pervasive that America now imports the work product of customer sales representatives, accountants, architectural draftsmen, doctors, engineers, and research scientists along with the more tangible output of seamstresses, tool and die makers, machine operators, and other blue-collar workers. Well-educated and middle-income Americans who long reveled in a wide assortment of affordable consumables, courtesy of robust international trade and rapid technological advances, are beginning to understand that sustaining this level of affluence means their once-secure white-collar jobs could be traded away.

Indeed, public opinion regarding unconstrained international trade has shifted in recent years. According to an article in *Finance & Development*, a quarterly magazine published by the International Monetary Fund, a study by the University of Maryland found support for free trade among individuals earning more than $100,000 a year had slipped to 28% by early 2004 from 57% in 1999. Growing doubts about trade were probably fueled by the 2001 recession and the weak recovery, with its lackluster job creation, that followed. Not surprisingly, trade-related anxieties seeped into the 2004 elections, when presidential and Congressional candidates, along with assorted interest groups, took stands for, against, or somewhere in-between the linked issues of offshoring and trade.

In a world where competitive pressures continue to multiply, geographic distances are quickly traversed, new technology facilitates voice and data communication, and foreign exchange rates can put U.S. companies at a disadvantage, the allure of exporting labor-intensive white-collar work is hard to ignore. Customer support, telemarketing, data processing, computer coding, and other types of standardized, repetitive, and easily codified tasks were the first to go offshore, starting in the 1990s. Early adopters of the offshore strategy for service and technology jobs, such as American Express and General Electric, were soon joined by Bank of America, Honeywell, Daimler-Chrysler, and other companies both large and small. During the past few years, the offshoring wave has been cresting ever higher on the skill ladder.

The decision to offshore technical and white-collar work becomes increasingly favorable over time. The countries importing these jobs, notably India and China, are upgrading their educational systems, improving their economic infrastructures, and loosening restraints on trade and foreign investment. Another critical selling point is the sizeable pool of potential employees conversant in English who are eager to work for wages that are high by local standards but far below the compensation earned by their American counterparts. According to IBM, as reported last November in *Barron's*, Chinese computer programmers with three to five years experience earn about $12.50 an hour compared to $56 an hour in the U.S. The article also noted that American companies operating in Bangalore, India pay software engineers approximately $30,000 a year while the rate in Silicon Valley tops $180,000 a year. A survey of information technology (IT) managers cited in *Economic Review*, a publication of the Federal Reserve Bank of Kansas City, found that 44% of respondents said reducing or controlling costs was the primary incentive for offshoring.

The Impact

Just how much offshoring actually saves American companies is a matter of some debate. McKinsey Global Institute, a think tank within its parent consulting company, figures the difference in compensation cuts employers' net cost by 45%-55%. But such gains are not realized without risk. Academics and consultants caution that differences in culture, laws, and language can inhibit the smooth flow of services and lead to expensive misunderstandings. In addition, concerns about firm-level management issues, such as product quality, intellectual property, customer privacy, data security, and the possible loss of control over key facets of a company's operations, can reduce the quantifiable gains from offshoring. Critics also note that many of the receiving countries have repressive political systems, tolerate labor practices that do not meet international standards, and subsidize the export sectors of their economies. Taken as a whole, the critics contend, these social and political factors may exact incalculable costs by raising questions about the values underlying America's economic system, not to mention the very real costs imposed on workers ousted by lopsided rules of play.

These risks notwithstanding, employment analysts and corporate executives readily agree that offshoring is here to stay. There is no consensus, however, about the number of white-collar jobs that have already vanished and how many more are destined to go. In the absence of verifiable data – the federal government does not produce any regular statistical series on offshoring – consultants and academics have proffered a variety of estimates and predictions. One widely cited report released by Forrester Research says 3.4 million white-collar jobs will disappear by 2015, taking $136 billion in wages out of the economy. Analysts at Goldman Sachs figure approximately 500,000 service sector jobs moved offshore between 2000 and 2003 and further suggest that six million could be eliminated by 2015. Deloitte Research says the 100 largest financial services firms will export $356 billion in operations, including two million jobs, by 2009. And economists at the University of California, Berkeley say 14 million jobs are at risk of being moved offshore because of specific job characteristics favorable to offshoring.

These numbers may seem alarming, but close scrutiny reveals a more nuanced reality. First, even if a total of four million white-collar jobs are dispatched to foreign shores over the next 10 years (the equivalent of 400,000 jobs a year), that's a small fraction of a U.S. labor force that will soon surpass 160 million people. Moreover, many of the job loss estimates were derived by using 2000 as the base year – a moment when employment in the technology sector was at its peak – and may thus overstate the case. The ensuing dot-com bust, coupled by the recession of 2001, make it nearly impossible to tease out which employees were laid off due to white-collar offshoring.

Then too, job loss predictions often fail to account for new job creation, projected to exceed 20 million by the end of this decade. The Bureau of Labor Statistics, for example, reckons the number of IT-related jobs will have increased 43% by 2010. This normal course of job growth and economic expansion is sustained, in part, by offshoring. Some companies that send jobs abroad discover that the cost-reducing, efficiency-enhancing side effects enable them to grow their businesses; IBM, Microsoft, and Oracle, have been, and are, making net additions to their stateside payrolls. Other companies, in turn, reap the benefits of such activity and likewise enlarge their operations, and on and on. A study by the economic forecasting firm Global Insight, as reported in *National Review*, found that offshoring added $34 billion to the 2003 U.S. gross domestic product (GDP) and facilitated the creation of 90,000 new jobs. In 2008, the study continued, offshoring is expected to generate a net GDP gain of $124 billion and 317,000 more jobs.

The upsurge in economic activity that follows in the wake of swelling trade buoys the chances for laid-off professionals seeking new work. The Congressional Research Service recently reported that three-quarters of the workers displaced by foreign trade between 1999 and 2000 had found work by the end of 2001. White-collar workers were more successful in their job searches than were laid-off blue-collar workers, and half were earning at least as much as they had in their former employ. The lesson here: education, experience, and specialized knowledge may not insulate against the negative micro (individualized) effects of foreign trade, but these attributes can help cushion the blow.

So, what's the bottom line? The global economy is a fact of life; the international exchange of products and services will continue to expand. In its generalized impact, trade enhances the common good. Analysts at McKinsey estimate that for each dollar spent to offshore a service activity, the U.S. economy gets back $1.14. The biggest winners, who take home 62 cents of the total returns, are shareholders in the companies doing the outsourcing and the consumers who buy those companies' goods and services; reemployed workers get 47 cents and the economy's export sector gets five cents. Whether people perceive this outcome as a boon to their economic wellbeing largely depends on whether they identify as a reemployed worker, a shareholder, or a consumer.

The breakdown provided by McKinsey shows that reemployed workers receive the fewest gains from trade and says nothing about those who remain unemployed. Although trade does, in fact, harm particular workers, a caveat is warranted here: current tax and monetary policies, combined with ongoing labor-saving innovations, have been hard on

wage earners in general. Using data from the *2004 Economic Report of the President*, analysts from The Brookings Institution have observed that pre-tax corporate profits exploded in the post-2001 recovery while compensation paid to labor fell sharply. The competition from offshoring and the slow pace of new job creation during the past few years only exacerbate the dilemma facing blue- and white-collar workers alike.

Mitigating the Effect

One superficially appealing way to keep jobs in America would be to restrict the global exchange of goods and services. Helping workers cope with the downsides of offshoring by constraining trade, however, is not an optimal strategy. The long-term cost of protectionist measures is probably way higher than most Americans would be willing to pay. President Bush's decision in 2002 to protect steelmakers by imposing tariffs on foreign imports failed miserably. The price of domestically-produced steel shot up, forcing customers to raise their own prices; these products then became less competitive and sales fell. Citing data first reported by the Institute for International Economics, an article in *Foreign Affairs* reports that 45,000-70,000 workers in companies that used steel as a material input were laid off. The article also notes that quotas on sugar imports have made U.S. sugar prices 350% higher than the world market price, prompting candy makers to relocate offshore, with 7,500-10,000 jobs wiped out as a result.

Although free trade and its offshoring byproduct benefit many sectors of the economy and many individuals, some industries and some individuals lose out. People on the losing end are not happy: some are unemployed, some earn less than they once did, and some fret about how much longer they can hold on. And some, including those who may not be personally wounded by the effects of foreign trade, wonder how the richest industrialized nation can and should respond when friends, as well as strangers, are penalized by economic forces beyond their control.

Even staunch proponents of unfettered trade argue that the federal government should weave a safety net for displaced workers. Think tanks, academics, and politicians who are dissatisfied with current administration policies have crafted a range of alternatives, such as opening up existing assistance programs to service sector workers (and simultaneously relaxing rigid restrictions that disqualify many manufacturing workers), providing more funds for on-the-job training, and creating a wage insurance program that would reward workers for accepting a new job at lower pay by subsidizing part of their wage loss for a limited period. Fiscal analysts say provisions in the tax code that encourage offshoring could be revised, and employment specialists say American schools should place more emphasis on the knowledge and skills required by a high-tech economy.

In the end, our country's willingness and ability to mitigate the inequities induced by foreign trade and exacerbated by the economy's overall dynamism has more to do with politics than with economics. Trade exacts a short-term price on some individuals that is hard to bear. Government intervention, far more than patience, is needed until the promised long-term gains of trade can be shared by all.

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