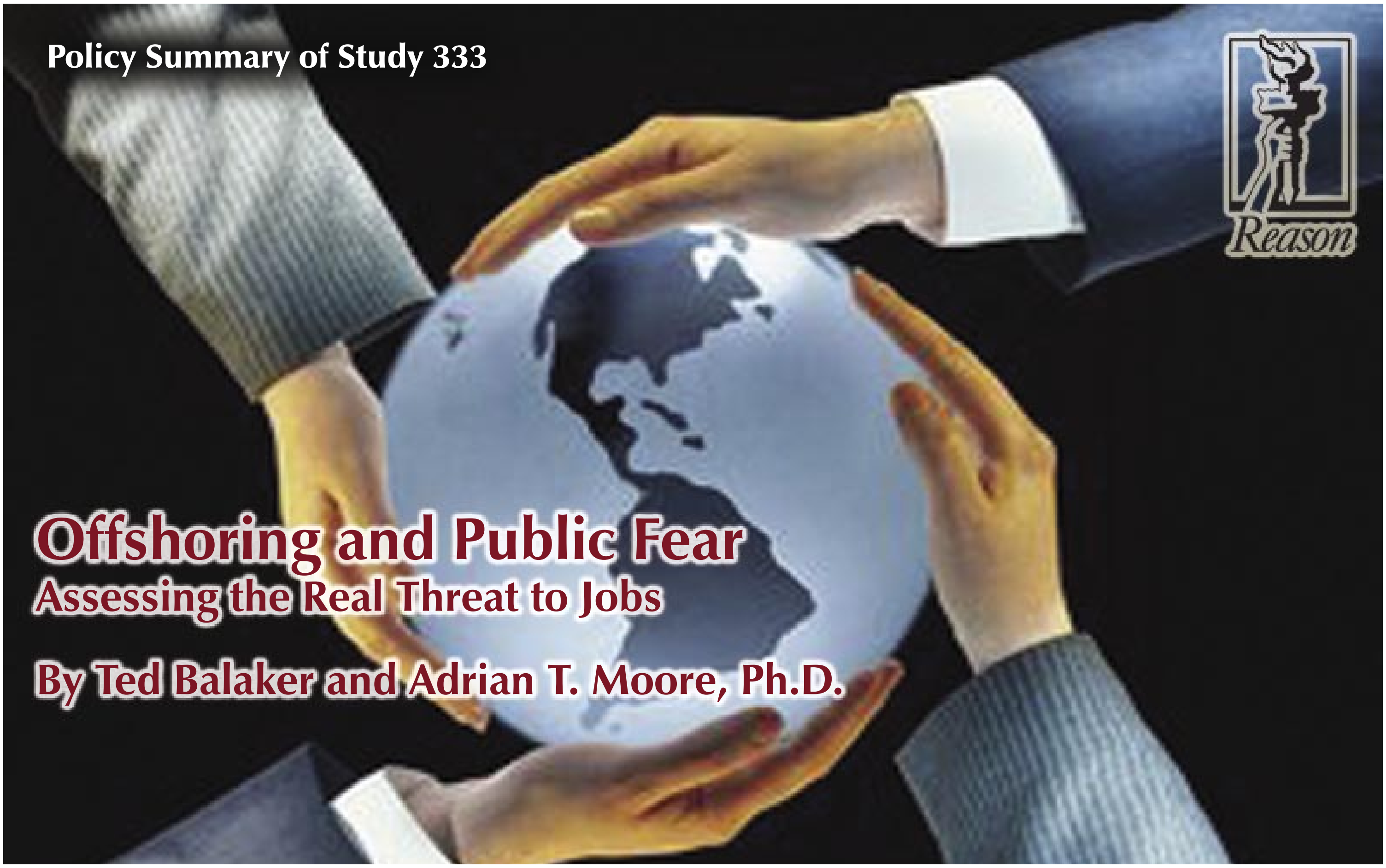


Policy Summary of Study 333

Offshoring and Public Fear

Assessing the Real Threat to Jobs

By Ted Balaker and Adrian T. Moore, Ph.D.

Has offshore outsourcing come out of nowhere? Suddenly news reports ask, "Will your job go overseas?" The American worker considers the question and trembles. Often, anxiety turns to calls for political action.

During the 2004 presidential campaign, pollsters found widespread public support for measures designed to impede outsourcing. State and federal lawmakers paid attention, and quickly penned over 200 anti-outsourcing proposals. Now that election year has passed, one might have expected anti-outsourcing momentum to slow. Yet the opposite has happened—legislators are now crafting anti-outsourcing bills at an even faster pace.

Policymakers must step back and separate the outsourcing's mythology from its reality. Contrary to hyperbolic stump speeches, workers have little to fear from outsourcing. Greater threats may come from shortsighted attempts to stymie outsourcing, and from allowing outsourcing to distract lawmakers from addressing lingering problems.

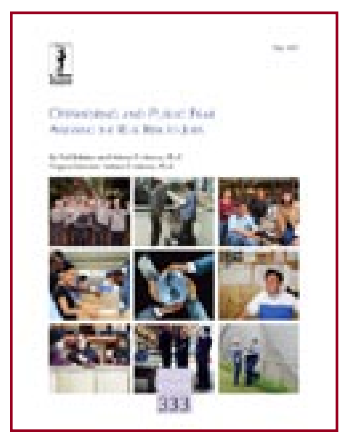
Outsourcing is not a newly created threat to jobs. It is merely a version of trade, and like previous versions of trade it brings some pain—but it brings even more promise.

The public debate about offshore outsourcing suffers from many misconceptions:

1 Misconception: Everyone is offshoring. Reality: Few companies offshore.

Offshoring is less prevalent than most people realize. For example, a Chief Executive magazine survey of over 300 companies found that only 25 percent of high tech companies practice offshore outsourcing. The survey discovered that other kinds of companies use offshore outsourcing even less often.

This is a summary of *Offshoring and Public Fear: Assessing the Real Threat to Jobs*, by Ted Balaker and Adrian T. Moore, www.rppi.org/ps333.pdf



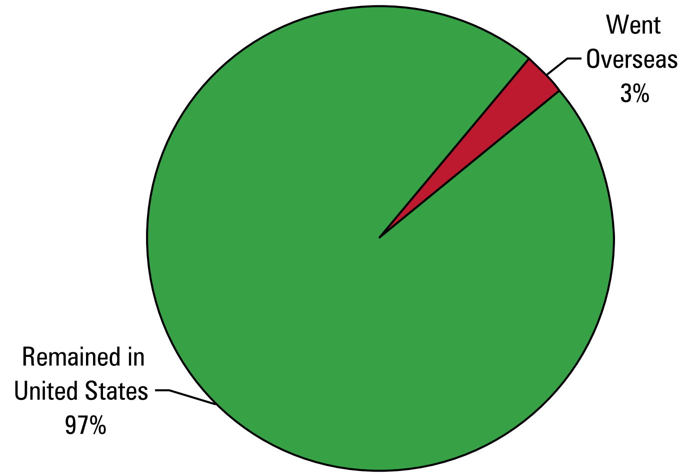
2 Misconception: Foreign workers are taking American jobs. Reality: Most American jobs are lost to other Americans or absorbed by new technology.

While the federal government has only recently begun to track offshore outsourcing, the figures that are available suggest that most outsourced jobs never leave American soil. The Bureau of Labor Statistics notes that, in 2004, only between 1.7 and 3 percent of mass layoffs involved overseas location (see pie chart).

The report suggests that fears over losing American jobs to cheap foreign competition are overblown. In most cases, outsourcing had nothing to do with mass layoffs, and when jobs were lost from relocation, 69 percent stayed within the United States.

Take a longer view and job loss from overseas location continues to represent a tiny portion of total job loss. Of all the mass-layoff job losses reported between 1996-2003, overseas relocation accounted for only 0.9 percent. Note that this period contains data for 2002, the peak year for overseas relocation.

Where did the jobs go? Extended Mass Layoffs 2004



Source: Bureau of Labor Statistics

3 Misconception: Outsourcing destroys jobs. Reality: Job loss from outsourcing has been grossly overstated.

As of 2003 roughly 400,000 American jobs had been outsourced to overseas providers. While this figure may seem large, it represents less than 1 percent of the civilian workforce.

Since this figure only accounts for layoffs borne by companies with 50 or more employees, it likely understates the number of offshored jobs. But even if the actual figure is somewhat higher, a less threatening picture still emerges: Offshoring affects only a fraction of America's workforce.

4 Misconception: The American worker has nothing to gain from outsourcing. Reality: Outsourcing is a form of trade, and trade creates more jobs than it destroys.

Outsourcing helps create jobs. Like any innovation that improves efficiency, outsourcing allows a business to do more with less. As costs fall, a business can expand by doing more of what it was doing already, or it can expand into related areas, by providing new goods and services. In either case, outsourcing encourages expansion, and expansion leads to new job openings.

Take the case of Delta Airlines. Delta outsourced 1,000 call-center jobs to India, saved $25 million in the process and then hired 1,200 Americans for higher paying reservation and sales positions. Notably, the company outsourced without laying off any employees.

Offshore outsouring also helped Donaldson Co. Inc., a Minnestota-based technology components company. Facing competition from overseas manufacturers with much lower prices, Donaldson shifted production to China. The design work stayed with its American team of engineers, chemists, and designers. Offshoring production helped increase Donaldson's U.S.-based employment by 400 employees since 1990. What if the company had refused to go offshore? "We'd be out of business," says an executive.

5 Misconception: Outsourcing destroys high-end jobs. Reality: Few high-end jobs are at risk, and outsourcing will help create more high-paying jobs than it destroys.

Certain technology professions have experienced job losses in recent years. But these losses came after the dot com burst, the Y2K technology job build up, and after a decade-long expansion of technology employment.

Just as was the case with past innovations, some jobs are lost, but more and better jobs are created. Since 1999, 70,000 computer programmers have lost their jobs, yet, at the same time, companies created 115,000 higher paying jobs in software engineering.

High-paying jobs are more plentiful than ever. From 1983 to 2002, management and professional specialty jobs have increased by 80 percent. These kinds of jobs account for nearly a third of total employment, a substantial jump from two decades ago when they comprised about a quarter of all jobs.

6 Misconception: Outsourcing is a one-way street. Reality: Millions of Americans have jobs thanks to "insourcing."

The debate about offshore outsourcing has focused on jobs leaving the United States. By definition offshore outsourcing does, in fact, address only the outflow aspect of trade. But we should not define ourselves into a corner. Let us not forget that offshore outsourcing is merely one component of the larger process of trade.

Insourcing represents an often-overlooked aspect of trade that creates jobs at home. Outsourcing goes both ways: U.S. companies send jobs to foreign nations and foreign companies send jobs to the United States.

Between 1990 and 2002 the United States received $800 billion in service-sector foreign investment, more than the next two largest recipients combined. According to the Organization for International Investment, U.S. subsidiaries of foreign companies employ 6.4 million Americans, a figure that has grown dramatically during the past 15 years.

7 Misconception: Companies could simply refuse to go offshore. Reality: Refusing to offshore can mean foregoing expansion or worse.

A business owner's decision may not be a question of outsourcing or not. It may be a choice between outsourcing or foregoing expansion, or even, outsourcing or going bankrupt.

Outsourcing can even save American jobs. For example, ValiCert avoided bankruptcy by outsourcing jobs to India. The cost savings allowed the hi-tech company to stay in business, and eventually hire more Americans at higher-level positions. Said the CEO, "Without India I don't know if we'd be around today.

8 Misconception: Outsourcing is driven by businesses looking for cheap labor. Reality: Where a company decides to do business is determined by many factors.

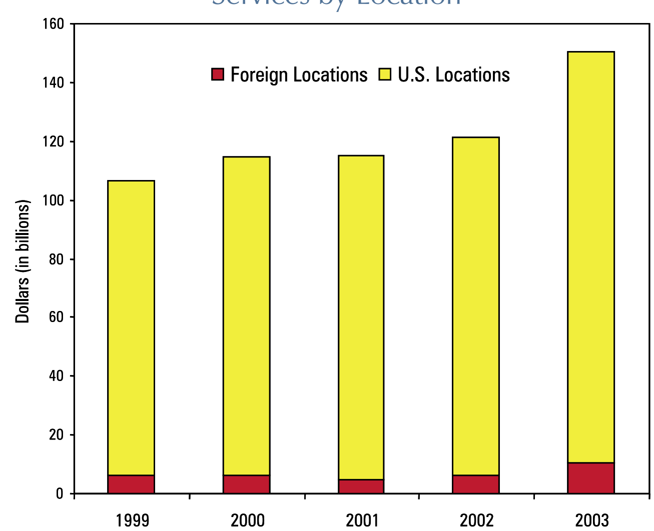
If businesses were interested only in cheap labor, third world nations would be flooded with foreign investment. Yet during recent years, while India was making headlines, U.S. investment actually increased faster in Ireland. In fact, the United States invests more in Ireland than in China, the Philippines and India combined.

Focus directly on outsourcing and the pattern remains the same. Although outsourcing destinations like India are growing in popularity, U.S. multinationals are much more likely to outsource to Canada and the United Kingdom where labor costs are comparatively high.

9 Misconception: Government-sector offshore outsourcing is widespread. Reality: Government-sector offshore outsourcing is especially rare.

Offshore outsourcing remains a small portion (about 6 percent) of total federal government outsourcing. It is even more difficult to assign a dollar figure to the amount of offshore outsourcing done by state governments, largely because the practice is so uncommon.

Is Government Work Going Overseas? Dollar Value of Federal Government Procurement of Services by Location



Source: United States Government Accountability Office, "International Trade: Current Government Data Provide Limited Insight into Offshoring of Services," GAO-04-932, September 2004.

10 Misconception: Only Republicans defend offshore outsourcing. Reality: Many well-respected voices across the political spectrum have defended offshore outsourcing.

Many nonpartisan and non-Republican voices have criticized the way the outsourcing debate has been framed.

Former Clinton Administration Labor Secretary Robert Reich argues:

> *There is no sense for us to try to protect or preserve high-tech jobs in America or block efforts by American companies to outsource. Our economic future is wedded to technological change, and most of the jobs of the future are still ours to invent.*

The Progressive Policy Institute asserts the "offshoring panic ... has triggered a spate of ill-conceived legislation." *The Los Angeles Times* editorial staff called a slate of state-level anti-outsourcing bills "wrongheaded."

FIGHT THE REAL THREAT—OUTFORCING

Some jobs leave town because the natural evolution of the market allows them to be done somewhere else; others get chased out by costly policy decisions, that is, they are outforced.

In the United States federal, state and local tax policies, convoluted labor laws and policies, outdated licensing and permitting requirements, unduly burdensome land use and environmental regulations and many other layers of the regulatory apparatus have driven up the costs of doing business, and thus creating jobs, making other nations more competitive at producing some goods and services. Increasingly this suite of policies raises costs to the point of outforcing jobs to other nations.

And like outsourcing, outforcing is mostly a domestic phenomenon. Some jobs get forced overseas, but even more get pushed from city to city and from state to state.

Outsourcing absorbs much negative publicity, but actually does more good than harm. Outforcing, on the other hand, is not the source of national outrage even though it makes more mischief. Policy should not fight outsourcing, it should fight the real threat—outforcing.

WHAT WOULD ANTI-OUTSOURCING LEGISLATION ACCOMPLISH?

There are many reasons why lawmakers should not support anti-outsourcing legislation.

1. Since offshore outsourcing is difficult to define, laws that target it would invite unintended consequences.
2. Anti-outsourcing legislation would make government more burdensome for taxpayers.
3. Anti-outsourcing legislation could push jobs to different states.
4. Anti-outsourcing legislation could prompt retaliation from other nations, resulting in the loss of American jobs.
5. Immigration restrictions could slow job growth.
6. Anti-outsourcing laws are not necessary to protect privacy or boost security.
7. Trying to curtail outsourcing likely would be futile and counterproductive.

POLICY RECOMMENDATIONS

To fight outforcing and address concerns about offshore outsourcing, lawmakers should:

1. Resist anti-outsourcing legislation.
2. Encourage workers and companies to prepare for employment transition.

3. Make benefits portable.
4. Improve math and science education.
5. Reassert America's position as the land of opportunity.
6. Relax land use regulations.
7. Support telecommuting or "homesourcing."
8. Outsource more government services.

CONCLUSION

Policymakers can choose to continue to target the wrong culprit by pushing anti-outsourcing legislation or they can pursue the real threat to jobs—outforcing. The future vigor of our labor market depends on our ability to learn from the past and realize that innovations like outsourcing stir anxiety, but ultimately bring a better world.

ABOUT THE AUTHORS

Ted Balaker is the Jacobs Fellow at Reason Foundation where he researches a variety of issues, including offshore outsourcing, privatization, transportation, and urban policy. Mr. Balaker has contributed to a wide range of print outlets, including the *Investor's Business Daily, Lithuanian Papers, Los Angeles Business Journal, Los Angeles Daily News, Orange County Register, Reason* magazine and the *San Francisco Chronicle*. He has appeared on many television and radio programs, including CBS Evening News, CNNfn's "Money and Markets," and various National Public Radio programs.

Mr. Balaker edits *Privatization Watch*, which analyzes the latest developments in privatization, outsourcing, and government reform. *Privatization Watch* provides lawmakers nationwide with tools to improve their communities and has been described as "energizing," "subversive," and "highly relevant" by the Institute of Economic Affairs. Prior to joining Reason, Mr. Balaker spent five years with ABC Network News producing pieces on issues ranging from regulation and economic development to addiction, self-esteem, free speech, and the environment.

Mr. Balaker graduated Phi Beta Kappa from the University of California, Irvine with degrees in political science and English. He lives in Los Angeles with his wife.

Adrian Moore is the vice-president of Reason Foundation, where he oversees all policy research. That research includes a focus on issues pertaining to education and child welfare, transportation, urban land use and economic development, environmental quality, and privatization. His own research focuses on privatization, government reform, and infrastructure. In 2002, he received a "World Outsourcing Achievement Award" for outstanding achievement in outsourcing research and communication by PricewaterhouseCoopers and Michael F. Corbett & Associates Ltd.

Dr. Moore is co-author of *Curb Rights: A Foundation for Free Enterprise in Urban Transit*, published in 1997 by the Brookings Institution Press, as well as Reason Foundation policy studies on regulatory reform and privatization of prisons and utilities. His articles have appeared in many publications such as *The American Enterprise, The Independent Review, Economic Affairs, and Public Policy and Management, Consumer Affairs,* and *Regulation*. He has also published op/eds in newspapers nationwide including the *Los Angeles Times, Boston Globe, Houston Chronicle, and the Atlanta Journal* and *Constitution*.

Dr. Moore applies this research to real-world problems through advisory roles with state and local government commissions on privatization and government reform throughout the nation, including Kansas, Oklahoma, Arizona, Virginia, San Diego County, South Charlotte, and Washington, D.C.

Adrian Moore graduated with a Master's in history from California State University, Chico and a Master's in economics from the University of California, Irvine, specializing in public choice, urban, and transportation economics. He holds a Ph.D. in economics from the University of California, Irvine.

RELATED STUDIES

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- To promote the use of economic reasoning to understand a world of scarcity and trade-offs;
- To show that government intervention is inappropriate and inefficient for solving social problems;
- To reframe debates in terms of control versus choice;
- To show the importance of a culture of responsibility that respects innovation, creativity, risk, failure, and diversity.