
Beyond Borders In a Global Economy.

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This paper attempts to explore the issues facing the U.S. services industry in a global economy – in particular the influence that outsourcing has with respect to the concept held by many that outsourcing is one of the key factors that help the economy by stimulating innovation.

This paper will attempt to not only provide background into the arguments for and against such a practice but will also try and reflect the cyclical trend of outsourcing. Data from interviews and research of articles and reports will be used to attempt to analyze the current trend, forecast an outcome of continued practice and provide an answer to the current situation.

Introduction

Before we can begin to examine outsourcing in the services industry, it would be prudent to explore how outsourcing has evolved especially in light of the context of this paper vis-à-vis a global economy. We also need to understand exactly what outsourcing or offshoring is in order to come to any conclusions in the arguments for or against this increasingly popular business practice. Research for this paper includes interviews and responses of IT professionals, developers and managers, and academics in the IT field.

Outsourcing or Offshoring?

Current references to any form of outsourcing in a global market are often termed offshoring.

Word IQ¹ attributes the concept of outsourcing to Ross Perot, founder of Electronic Data Systems, who would tell a prospective client, "You are familiar with designing, manufacturing and selling furniture, but we're familiar with managing information technology. We can sell you the information technology you need, and you pay us monthly for the service with a minimum commitment of two to ten years."

- Outsourcing is the transfer of the operation and day-to-day management of a business process to an external service provider. The customer receives a service that performs a distinct business function that fits into the customer's overall business operation.²
- Outsourcing is an arrangement by which one company provides services for another company that could also be, or previously had been, provided in-house.³
- Offshoring can be contrasted with outsourcing and offshore outsourcing which implies that a third party service provider takes over the business process and runs them based on service level agreements.⁴
- Business Process Outsourcing (BPO) refers to outsourcing arrangements when entire business functions (such as IT, Customer Service, etc) are outsourced.

Then there are the "transnationals" – businesses placing top executives and core corporate functions in different countries to gain a competitive edge through the availability of talent, capital, low costs, or proximity to their most important customers – take for example Wipro Ltd. with their sales division based in the US, near clients, and their engineering group in India⁵. Companies can therefore close down a service unit in one country and open an office in another country. When companies fragment this way, they are no longer limited to the strengths, or hobbled by the weaknesses, of their native lands. Is this outsourcing, offshoring or business process outsourcing? Maybe not in the traditional sense but the concept is there – the relocation of an in-house business function.

These definitions reflect the broad concept of "outsourcing". The question then arises, "If the concept is that ambiguous, on what fundamental business principles do corporations outsource?"

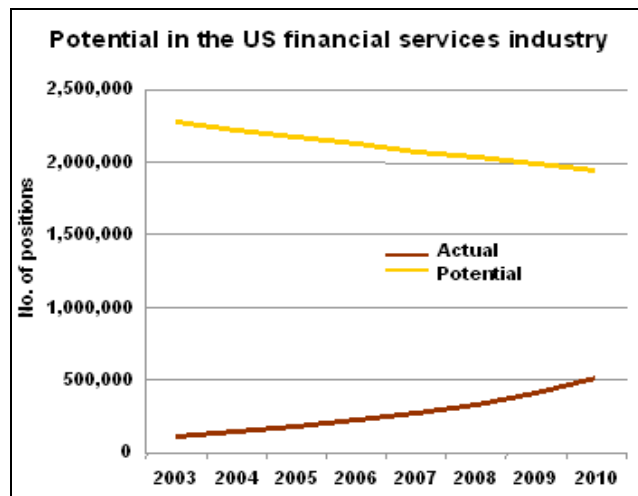
Two common types of outsourcing are Information Technology (IT) outsourcing and Business Process Outsourcing (BPO). BPO includes outsourcing related to accounting, HR, benefits, payroll, and finance functions and activities.

The Growth Of Offshoring Services

Reliable and affordable communication infrastructure and the digitization of many services has made it possible to shift the actual delivery location of services to low cost locations.

Average Salaries of Programmers ⁶	
Country	Salary Range
Poland and Hungary	\$4,800 to \$8,000
India	\$5,880 to \$11,000
Philippines	\$6,564
Malaysia	\$7,200
Russian Federation	\$5,000 to \$7,500
China	\$8,952
Ireland	\$23,000 to \$34,000
Israel	\$15,000 to \$38,000
USA	\$60,000 to \$80,000

Almost one third of the world's top financial institutions have sent work to facilities in countries other than where the work is currently taking place. These institutions are expected to significantly increase their reliance on offshoring over the next decade, and new institutions are incorporating offshoring into their business plans.⁷



India benefited from the trend as it has a large pool of English speaking and technically qualified manpower.

India's offshoring industry took root in IT functions in the 90s, and has since moved to back-office processes such as Call Centers and Transaction Processing as well as high-end jobs such as Research & Development, Equity Analysis, etc. Other offshoring destinations are the Philippines, Ireland and Eastern European countries.

Thus began the debate between what many developers in the US believe to be the demise of the IT industry as they had come to know it, and the strategic and competitive positioning that many companies in the service industry adopted. In addition, economists began to promote their theory that innovation, enhanced by competition, will increase demand for opportunities in the local job market.

The Economics

Many believe that the attributing factor for a jobless US economic recovery is due to the spread of outsourcing. Studies from the University of California at Berkeley show that the country lost more than 1 million white-collar jobs in the 1990s and "hundreds of thousands more since the turn of the century." Ashok Deo Bardhan, a researcher for the study believes that there is some correlation between jobs lost in the US and jobs created in India.⁸ Wipro chairman, Raman Roy who helped start the Indian call center boom in the '90s, believes that companies can save between 30 and 50 percent by outsourcing services to India.⁹

On the other hand, a study by the Information Technology Association of America estimated "that global outsourcing would save US technology companies some \$21 billion a year by 2008; as those savings ripple through the economy, productivity and wages would rise, creating more than 317,000 jobs in 2008." The study went on to conclude that only three percent of lost technology jobs could be attributed to outsourcing.¹⁰

Haseeb Ahmed, an economist at Economy.com, stated that offshore outsourcing is good for the U.S. for the same reasons that free trade is beneficial for a vibrant economy. "Arguing that outsourcing hurts is arguing that free trade hurts."¹¹

In another study, McKinsey Global Institute claims that for every dollar spent on a business process that is outsourced to India, the US economy gains at least \$1.12 with 58 cents going back to the original employer. The study also claims that even though the US had lost about 2 million jobs due to global trade over the past 20 years, 35 million new jobs have been added in the past 10 years. The point of this study was to show that offshore

outsourcing is not the cause of lost technical jobs in the US but because of improved efficiencies and business automation.¹²

Hillary Rodham Clinton, believes that the US has the potential to be far more competitive than employers believe as many, when considering outsourcing, neglect to factor in costs related to planning, offshore transition, vendor selection, technology, communications, off-shore management, travel and security. Her assertion is that when employers add in these costs, a call-center worker costing \$5 in wages offshore has an actual cost of \$17.¹³

Chief Technical Officer of PCI Corp based in Boston, Massachusetts, Jamil Azhur, says otherwise. Their decision to outsource was based on good contacts, familiarity with their outsourcing partners and their ability to control the vendor situation. PCI's experience is that outsourcing must be seen as a long-term venture thereby enabling the learning curve costs to diminish over time. For their outsourcing vendor to become familiar with PCI's products took anywhere from 6 months to 2 years, depending on the complexity of the product.¹⁴

White Collar Job Migration

Shifting of jobs¹⁵

While there are signs of a slow economic recovery, many claim this event as a "Jobless Recovery" with much of the blame laid at the door of those corporations implementing Cross Border Business Process Outsourcing, the practice of outsourcing business functions to subsidiaries or vendors in other countries. Researchers predict that at least 3.3m white-collar jobs, translating to wages of \$136b, will leave the US by 2015.¹⁶

In May 2004 Bank of America, who recently acquired FleetBoston Bank, announced that it will hire 1,500 people at its subsidiary, Continuum Solutions¹⁷, which plans to open in southern India in the town of Hyderabad. This was 500 more than previously predicted in 2003. On June 5, 2004, Bank of America announced that it would lay-off 12,500 jobs as part of its FleetBoston takeover but stressed that Continuum only accounted for one percent of its workforce. Bank of America has relied on software firms in India for its software development, testing and modernizing since 2002.

Companies such as Dish Network Satellite TV of Littleton, Colo., Dell Computer Corp., Procter & Gamble Co., American Express Corp., and Citibank employ

workers in the Philippines to answer their phones. The Philippine government predicts that call center jobs will double over the next year.

Filipinos also are competing for high-tech jobs like software development and engineering, the kind of work US firms have been sending to India, Ireland, Russia, China and Ghana. But in a country as poor as the Philippines, outsourcing is seen as a move towards the economic growth that was enjoyed by Taiwan and Singapore. Of the 84 million people, there is a sizable middle class with an average household income in 2000 of \$2,600. However a third of all households earned less than \$1,000 a year.



Part of the attraction by US-based companies to this part of the world is confidence in the workers - with a literacy rate of over 90 percent, universities producing 350,000 graduates a year, (50,000 engineers) and most who speak English, the Philippines offer an almost limitless resource of skilled workers - of course at lower cost. In addition, thanks to its close geographical proximity to Asia and Australia, the country has superb telecommunications links via a network of undersea fiber-optic cables that provide low cost voice and data communications. The network links the Philippines, North America, Africa, Asia and Europe.

Most outsourcing jobs in the Philippines are not directed toward software engineers but to lower-skilled technology work like medical transcription. Manila company, eData Services, provides an 800 phone number in the United States for doctors to dial in and dictate medical information which is then typed up by eData workers. These workers all hold a degree in medical care, usually in nursing or physical therapy. Doctors, working part-time for eData, provide editing and accuracy checks and once verified, the transcripts are e-mailed back to doctors' offices in the United States.

Forrester Research of Cambridge projects the number of US business service and software jobs migrating to India and other countries increasing from 315,000 in 2003 to 588,000 in 2004. The number of outsourced jobs is expected to increase to 830,000 in 2005. In India, approximately 60 percent of the revenues of the overall IT software and services market were accounted for by exports that jumped from \$9.5b in 2002/3 to an estimated \$12.2b in 2003/04.

Chances are, if a call is made to the technical support for Delta Airlines, American Express, Sprint, Citibank, IBM or Hewlett Packard, it will be routed to India. Outsourcing of services include debt collection, technical calls (Dell and AOL), email response for Amazon.com, stock analysts for JP Morgan Chase, radiology processing for

Massachusetts General Hospital in Boston, and the completion of tax returns for at least 150 US accounting firms, 20 of which are in the top 100.¹⁸

Wired Magazine, February 2004	
	United States GDP per capita \$35,060 Unemployment rate 5.8% Labor force 141.8 million Population below the poverty line 13% Typical salary for a programmer \$70,000
	India GDP per capita \$480 Unemployment rate 8.8% Labor force 406 million Population below the poverty line 25% Typical salary for a programmer \$8,000
Top 5 US Employers in India	
General Electric	17,800 employees
Hewlett-Packard	11,000 employees
IBM	6,000 employees
American Express	4,000 employees
Dell	3,800 employees

Azhur, of PCI Corp, disagrees with those wanting to restrict the movement of outsourcing. “From an Asian prospective ... it is a very interesting one-sided, short-sighted kind of argument to say that we will not allow global trade of goods and services whenever it hurts us. If you are a consumer standing in the streets of Shanghai, Dhaka or Bombay and drinking Coke, where do you think those profits are going?” “It is very interesting to say that China should open its markets (and) should have no tariffs, that India should open its markets, that Japan should withdraw subsidies on rice and allow unrestricted tariffs on imports of US and European tariffs – that they will buy all of “Western stuff” but the West will not buy anything from them.” Azhur feels that if the US continues to impose tariffs and restrictions when it comes to free trade but at the same time wants to taking advantage of a global economy, “it won’t work”.¹⁹

Positions in the Debate

The Economists²⁰

Economists predict that lost jobs will be absorbed as the economic expansion lengthens and as baby boomers retire but the UC study reports that unless displaced workers are employed in new high-wage industries created by US economy pioneers, the future of these workers will be one of lower pay and a reduced standard of living.

Other economists say that over time, Americans will benefit from the higher corporate profits that come from outsourcing. Low-level work will be performed in low-wage countries, saving US employees for more demanding, higher-paying tasks.

Treasury Secretary John W. Snow, in an interview with the Cincinnati Enquirer stated that outsourcing “*is a part of trade . . . and there can't be any doubt about the fact that trade makes the economy stronger...*” Federal Reserve chairman, Alan Greenspan advocates the concept of outsourcing which encourages competition saying that “*competition leads to the type of innovations that drive the US economy forward and ultimately create far more jobs than are lost.*” This sentiment was echoed by N. Gregory Mankiw, chairman of the Council of Economic Advisers, and Stephen Friedman, director of the National Economic Council, two of President Bush’s top economic advisors, an indication that the Bush government fully intends to defend free trade.²¹

Diana Farrell, an economist at the McKinsey Global Institute, is convinced that the current situation is a “global-wealth-creation story over all”. Farrell believes that while other countries are benefiting, it is “ultimately a global wealth story for ourselves”. The basis of her statement is that huge savings can be redeployed in positive ways and that labor can be redeployed to more productive and higher output use. “This is a win-win game.”²²

Framing the debate in economic terms can be tricky because while economic theory offers tidy equations that lead to win-win situations, there are losers in the real world. Workers who see their jobs shipped overseas are hurt while companies and the economy as a whole may see benefits such as lower prices for consumers. Haseeb Ahmed of Economy.com believes that the economic advantages of offshoring are problematic since the pain is felt quickly and prominently while benefits are spread out over time and hard to quantify. The complexity of this debate is one that is dividing many economists as the May 10, 2004, report “Offshore Face-Off” by Timothy Aepfel, a Staff Reporter for The Wall Street Journal indicates.²³

The Employers

In a global economy, US companies say they have no choice since they must stay competitive with companies that operate in lower-cost countries: therefore that if one does, everybody has to - just to keep alive.

“The reason was money”, said Jim Daley, co-founder of PCI Corporation. PCI began outsourcing work to Dhaka, Bangladesh in 1997, long before the concept of

outsourcing became popular. Daley went on to say that the company also had the confidence that their service providers would perform and that it helped that Bangladesh was a former English colony. PCI also outsource some work to Armenia.²⁴

PCI's Chief Technology Officer, Jamil Azhur sees their outsourcing initiative slightly different to Daley. Initially, as startup, outsourcing was not a factor in their business process but as the company grew from a start-up to a more mature business, outsourcing became a crucial factor in PCI's ability to be competitive. Senior executives identified the need for more resources, flexibility and focus to meet business objectives. According to Azhur, outsourcing first and foremost allows PCI to focus on core competencies – part of QA and development is currently outsourced. His belief is that certain functionalities are simply more efficient and effectively done if they are outsourced. Secondly, outsourcing provides on-demand services and the flexibility of scalability and availability of resources. Azhur admits that cost, while an important contributing factor, was not the core motivator for outsourcing.²⁵

"Clearly, US companies have looked offshore because they have to reduce their operating costs in order to survive," said Rita Cruz, a partner at the consulting firm Accenture which employs 2,000 Filipino software developers. Con-Way Transportation Services, a major trucking firm in Ann Arbor, Mich., has had its older software maintained by Software Ventures, based in the Philippines, since 2001. "It frees our people up to do more cutting-edge stuff," said Con-Way's marketing director, Joe DeLuca.²⁶

Even though bandwidth and language still poses problems, Daley believes that the company is "still ahead" with respect to overheads although return on investment is not quite what it is made out to be since there are other hidden costs that need to be accounted for when considering offshore services. Looking long-term, Daley believes that outsourcing costs in Bangladesh will not increase that significantly for him to look at outsourcing work to another country. The company does not plan to expand their number of current outsourcing providers because of the economy of scale.

Founder of Patni Computer²⁷, Indian-born MIT graduate Narendra K. Patni and who has development offices in India, England, Germany, and 11 locations across America, points out that the lost work represents a small fraction of US gross domestic product. He contends that the flow of low-wage jobs overseas, in fields such as customer call centers, brings savings to the US economy

and enables it to invest in higher-value activities such as biomedical research.²⁸

The Workers

The following are extracts from responses to a survey sent to a number of IT professionals.²⁹

How do you feel about outsourcing of services to other countries as an IT professional working in the US?

- "Outsourcing services to foreign countries may be a cost reduction strategy that makes sense from a corporate fiscal point of view. I am not opposed to such actions as long as the concern for the social well being of the local US workforce is not negatively impacted and the outsourced services do not take unfair advantage of foreign workers. Services can be rendered in foreign places at a lower cost due to lower living cost and lower wages. It is important to me that the wage/living costs are proportional so that workers are competitively paid and can meet their financial needs. To escape from losing one's job to outsourcing lies in specialization and further education of US based staff."
- "I'm certainly not happy about it, because it would be hard for me, or my wife, to make a transition to another type of job with similar benefits. The possible negative impact is very immediate to us, with few or no direct benefits for us. The argument that creating jobs in other countries increases the market for our products seems to fall flat, since it seems to me that the goods sold to workers in other countries might very well be made outside of the US, even if the company behind the product is a US company. Ultimately, it looks to me like shareholders and corporate executives might benefit from ramping up the economies of other countries, but that I will not benefit much."
- "Troubled. Typically functions regarded as cost centers (customer service, technical support) were prime candidates for offshore outsourcing. Specialized functions such as software development, which are now being outsourced, require much greater management resources, a need now increased by the geographic distances between the decision makers and implementers. I have seen companies become extremely "top-heavy" with multiple layers of upper and middle management becoming more and more involved in processes that used to be managed on a more local level. I can easily see such organizations becoming institutionalized to the point of ineffectiveness."

- “I feel the same way as I do about other professions and trades being exported. I think work that originates in this country should be performed in this country. It makes no sense to me that the money paid for offshore workers is allowed to undermine the economy of the American middle class. The only beneficiaries of this arrangement are the owners/stockholders of the companies involved. American companies should be employing American workers whenever and wherever possible.”

Do you agree that the US in earlier years benefited from participating in a global economy and now has to endure the results of a sluggish US economy? If not, why?

- “I agree that the US has benefited in earlier years from the global economy. There is envy towards foreign countries that prosper while the domestic economy only recovers slowly from the events following September 2001. While 9/11 can be seen as a milestone that precipitated a further economic decline it is not the underlying cause. All depends on the viewpoint also - the economy deteriorated for lower and middle class Americans, while the current administration took care of the upper class and large corporations with tax cuts and large government contracts. Especially heavy industry and military oriented industries benefited despite an overall economic decline. US Oil dependency was turned into a cash cow by almost 100% increase in gas prices, while smaller corporations and "consumers" suffers, the oil lobby rakes in the benefits.”
- “First is the matter of whether the US benefited from participating in a global economy in earlier years. I assume the years implied by "earlier" refer to the boom during the Clinton administration, for which I say yes, I believe that is the case. Certainly corporate profits increased, and the GDP increased, and manufacturing productivity increased even as manufacturing jobs were moved to other countries. However, it's worth pointing out that while there were more jobs in the US, many of them were part-time jobs or jobs that had low compensation (including a relative lack of benefits such as health care). In many cases one person needed to work as many as three of these new jobs in order to "get ahead". So, while embracing the global marketplace increased U.S. wealth generally, it often came at the expense of the physical and social health of workers and their families.”
- “I think the global economy has contributed to the recent sluggish US economy. Certainly, US states that relied heavily on manufacturing have

experienced a recession that is deeper than average for the nation, and it seems obvious that many of those manufacturing jobs were eliminated during the boom years in order to relocate the jobs outside of the US. Tech jobs accounted for many of the job losses, but I think it's worth pointing out here that while the tech boom was in part due to optimism during the US expansion into the global marketplace, the "burst bubble" in the tech sector was partly the result of irresponsible capital investment and unrealistic expectations -- in other words, that it was preventable. It's worth noting those attitudes are not intrinsic to the global economy.

Job losses in those two areas (manufacturing and tech) probably added to problems in other parts of the economy. That is, with consumer confidence and spending relatively low due in part to a sense of job insecurity, retail jobs have suffered too.”

- “The U.S. benefits from the international economy but has no consequent responsibility to "contribute" jobs to the rest of the world. There is no quid pro quo here. Economies are demand based, and if the needs for U.S. goods and services comes from the rest of the world, then that is just a good indication that we are competitive. We lose this competitive edge when the goods and services we provide aren't even produced here.”

What do you foresee as the future of the service industry in the US?

- “I think it's important to look for solutions that do not alienate our economic partners, as tariffs and other protective measures can do. While NAFTA has some deep flaws, it's not morally right and not economically wise for our long-term prospects to seek short-term economic relief at the expense of our trading partners. Any changes to our trade agreements should be negotiated with our partners.”
- “Service industry in the US will only be able to survive if the services are of outstanding quality, cost effective, and readily available. Customized services will be a key for survival. IT service industry is again different than let's say food service - which requires domestic workers, even though they may be immigrants. All consulting services are likely to vanish to foreign countries as long as they don't require physical presence or interaction.”

- “Because I do not think low-tech manufacturing jobs will expand greatly in the future, I think the future of the service industry is directly linked to the health of highly specialized manufacturing and high-tech services in the US. But even so, the service industry can expect to occupy the less desirable position resulting from the increasing division between the wealthy and the rest of the nation. If the US can continue as a leader and innovator in the sciences--growing jobs in technology, medical research, etc.--then the service industry will maintain relative stable even as the divide between its workers and the wealth increases. On the other hand, if people with specialized and advanced skills can't find jobs and are competing with those who have lost manufacturing jobs for less desirable service jobs, there will be little chance for increased compensation in the service industry even if jobs grow in that area.”
- “Increased outsourcing of services, and beyond that, redefinition of what a "service" is. Software companies continue to search for realistic ways to turn their products into services. I see other industries following suit, turning their products into services and outsourcing non-core business units to other companies. The only service which I see remaining in the U.S. indefinitely is education, but without a domestic population of students and alumni to support them I imagine they too will eventually suffer foreign competition.”
- “The future of the U.S. service industry is uncertain to me. Although entrepreneurs will always find new markets, technologies, and services, the ability to provide labor and talent in this country will remain dependent upon whether or not our work force is superlative to that of other countries. Once again, success is demand-driven. You go to the best place for the best resources. The reason that America experienced such a technology boom was that we were positioned to deliver the goods and services required.”
- standard and cost will affect those locations eventually.”
- “It's certainly occurring in Ireland. The Irish economy benefited greatly from the United States' economic prosperity in the latter years of the 20th century, so much so that it was referred to as the "Celtic Tiger". The tiger is no more, largely because of the dip in the U.S. economy, but also because the services provided are now available elsewhere at a lower cost. Ireland had offered greater and greater incentives to foreign companies to bring their business to Ireland (in the form of tax breaks, deferments, etc.). These inducements increased to compete with cheaper countries, but have now reached the point where it is no longer viable to do so. The jobs are going elsewhere, and the tiger is more of a large cat. Meow.”
- “Disagree. India to the best of my knowledge is just become more efficient. Bangalore has more PhDs and qualified IT graduates than Silicon Valley. The best brains from all over the world are being recruited to Bangalore. Their salaries are still 1/3 of the US salaries. They go to India for variety of reasons. But due to this the quality of the IT sector has risen tremendously.”
- “Once again, demand is the issue. The labor rates in these countries are bound to rise, but not nearly to American levels because of the differing standards of living. There will always be a search for the cheapest ports of production, but the real issue is what America has lost and not what these developing nations have gained. We really do not stand to benefit from a rise of the standard of living in India or Malaysia, and certainly not to any proportion of benefit that we stand to enjoy as the provider of the goods and services being shipped offshore.”

Please provide comment on claims that countries currently providing services to the US, such as India, Ireland, Singapore and Malaysia, are becoming less cost effective and that focus is now shifting to countries where such services can be outsourced more cheaply?

- “The rising living standard and associated cost raises the need for better pay. International computer networks will allow moving the outsourced ventures into cheaper regions. However, that will stay a temporary solution also, as the same raising living

In light of the current economic situation in the US, please comment on the following excerpt taken on 3/31/2004 from the Boston Globe titled, "Treasury chief calls outsourcing a plus for US": "Treasury Secretary John W. Snow, in the latest sign that the Bush administration intends to directly defend free trade despite the loss of American jobs overseas, argued in an interview published yesterday that outsourcing ultimately helps the US economy. Snow told The Cincinnati Enquirer that outsourcing "is a part of trade . . . and there can't be any doubt about the fact that trade makes the economy stronger.... Many economists, including the Federal Reserve chairman, Alan Greenspan, say the competition leads to the type of innovations that drive the

US economy forward and ultimately create far more jobs than are lost."

- “Exporting jobs and competition are inherently different things as the outsourcing of jobs into foreign countries makes it impossible for domestic companies to compete. The basic costs in offering services based in the US are much higher than in the countries that are targeted for outsourcing. Quoting Greenspan is fine, however, completely out of context. The claim that trading jobs is creating viable competition is in my opinion false. The statements seem to be made from a corporate point of view, with most concerns for corporate profits and cost cutting.

It is important to identify who is the main beneficiary of the "trade" that the US engages in - under the current administration obviously it is corporations. I believe that the corporate well-being has taken over interest in the well-being of the American people. If the American population benefits it is only secondary but not the primary interest. It will be a challenge to restore a broad based economical concept that defines economy as a means to benefit not only the American population but also the global population without being driven by corporate greed only.”

- “I think Snow's position is somewhat disingenuous. I don't doubt that creating jobs overseas can help the profits of many US companies, but I don't think this trickles down to increased wealth for the average American unless the transition is gradual, with US employment remaining high.

Mr. Snow points to history and theory without acknowledging that the nature of the shift towards outsourcing is fundamentally different than anything we've experience in our history. To say trade makes the economy stronger is **not** necessarily to say that outsourcing results in trade that makes the economy stronger -- that remains to be seen. Who's to say that the goods and services consumed by the countries we've outsourced to will be made or provided by American workers? Why would they be, if it were cheaper for those jobs to be outsourced? In other words, US companies might be very effective selling to new middle classes they've created worldwide, but **what** they sell and provide very well might not be made or provided by US workers. Perhaps that means the US will transition towards making even more specialized goods and high-tech products, but that remains to be seen.

I don't think the US suffers from an innovation deficit, as evidenced by our ability to increase the productivity of the average worker in recent years,

and even by our flexibility in moving towards outsourcing. Mr. Snow's comments indicating that outsourcing will spark innovation translates to me as a statement saying that the innovation will be based not on opportunity backed by strength, but rather by the challenges posed by a less advantageous climate -- something akin to desperation. And yet the US is always innovative wherever there is opportunity -- desperation is not our only motivation for invention.

Snow's comment makes me wonder the following question: If a company's manufacturing workers are not in the US, and many of its service needs (such as aspects of accounting, for instance) have been outsourced, and its shareholders are distributed among many countries, what exactly makes it a US company? The fact that its executives are in the US - and that the incorporation papers are filed here? That's rather unsatisfying.”

- “While I might agree that outsourcing drives the economy forward, I certainly don't see any evidence that it creates jobs in a sustainable manner in the United States. Even if it were true that the immediate, perhaps short-term, effects of such a practice yielded domestic employment opportunities, the idea that this could continue indefinitely is ridiculous to this layman, and smacks of a ponzi scheme. The only provable result of a strong economy is that it benefits people who own stock. I know over a dozen people who have lost their jobs in the last four years at all levels (management, IT professionals, service industry), and not a single one has found a "better" job after they were laid off.”
- “SYCAMORE president Deshpande agrees with the above notion. He believes that money saved by outsourcing is being used in the USA to research new products and introduce new products. I believe what he is saying is that if you have no money your business will come to a grinding halt and thanks to outsourcing many companies are at least able to provide salaries to those employed in the USA.”
- “My comment here is that we need to focus on strengthening and maintaining our national economy by preserving job and manufacturing opportunities on our own soil, where ALL the investment (i.e. infrastructure, taxes, wages, profits) remain within our domestic economy. Offshoring is simply a method of avoiding the cost of doing business in America in the name of maximizing profits.”

Is There A Place For Any Mainstream Service Worker?

Jamil Azhur, of PCI, believes that, "... all change is painful to some at all times throughout time – transformation is never easy..." He goes on to say that the US economy will have to remain vibrant, dynamic and ready to take the opportunities that arise from any situation, from any place, in today's globe and grow – even if it's hard for some people. "(innovation is) 'what America was built on'". During his interview, Azhur uses the IT industry as an example saying that no large numbers of IT workers existed in 1979, that Microsoft had a small number of employees when it first started yet now has a large number of employees. He goes on to say that history proves that the concept is not unique - that the change in the service industry is more of a transformation and an effect of innovation. Azhur refers to the IT transformation as still "very young", saying it will cause "massive unemployment" – even in developing countries, as computers replace workers. "It will inevitably cause some pain but in the end ... no-one would want to go back to (the way of doing things in) 1985 today."³⁰ Azhur recommends that the US worker today has to have some competitive advantage over a worker overseas otherwise it would be impossible for that person to retain their job.³¹ A report by the Meta Group of Stamford, Conn. seems to substantiate Azhur's theory saying that offshore outsourcing has had little impact on the salaries of those with critical skill sets such as senior network architects or senior database management staff while those with standardized skills are seeing salaries flatten out.³²

Exporting of manufacturing jobs over the last three decades have seen changes to the American economy. Unlike Azhur however, authors Stuart Yagur and Ernie Nounou, of the Drum Major Institute for Public Policy, claim that there is a definite difference between the outsourcing of manufacturing jobs in the seventies and those of IT jobs today. Their claim is based on the fact that IT jobs are "qualitatively different than the jobs that left earlier" and because "there are no natural barriers to limit the extent by which American jobs will be exported due to cross-border BPO".³³

"As the workplace became increasingly more high-tech, the American worker was promised greater rewards in higher skill, higher value, higher paying jobs, if they continued to work hard, learn the new skills required of them to adapt to the needs of an information economy, and accept greater job insecurity and longer working hours. American workers responded to that call by changing their lifestyles and re-entering the American educational infrastructure, which had quickly adapted to

help American workers remain occupationally relevant. A wealth of private classes sprung up in short time, and courses offered in community colleges were touted as a bridge to the information economy. In the end, however, the bridge was too short, and the promise of high paying jobs on the other side of the tech wave was not kept."

"Despite the price paid by the American worker to participate in the information economy, many have never had the opportunity to do so. While the job preparation infrastructure still performs its key function, the kinds of jobs that it is readying people for are increasingly being exported overseas."³⁴

Global Insight Inc., who conducted research for the Information Technology Association of America, predicts that more IT jobs will be created offshore than onshore over the next five years, but the overall U.S. economy will get a boost from the cost savings that offshore outsourcing yields. It must be noted that the ITAA is a high-tech trade group that is lobbying Congress in favor of offshoring. The membership includes companies such as Accenture, Amazon, Dell, EDS, Hewlett-Packard, IBM, Microsoft, Siebel and Sun to name but a few.³⁵ The report also notes that while wages and jobs will increase in the economy overall, the outlook for IT workers may be less positive. "Some workers may have to take a job that pays less than their [current jobs]," and some IT workers will face "wage compression" as a result of overseas competition, said Nariman Behraves, chief economist at Global Insight.³⁶

Mike Gildea, executive director of the Department for Professional Employees of the AFL-CIO, which represents 4 million white-collar workers, does not believe the explanation that Americans will do better in the long run referring to the report as "a load of.... This is exactly what we were told about manufacturing jobs 15 years ago."³⁷ While US companies reap the benefits of outsourcing, Ron Hira, chair of IEEE- USA's Career & Workforce Policy Committee, responded to the report by saying that there was no clear indication that the US economy would benefit from this since there was little evidence that displaced workers were being redeployed to equal or better jobs despite predictions by economists.

Daniel H. Pink of Wired Magazine believes that it is the speed at which outsourcing has transformed the IT industry that is causing the greatest shock. "Agriculture jobs provided decent livelihoods for at least 80 years before the rules changed and working in the factory became the norm. Those industrial jobs endured for some 40 years before the twin pressures of cheap competition overseas and laborsaving automation at home rewrote the rules again. IT jobs - the kind of high-

skill knowledge work that was supposed to be our future - are facing the same sort of realignment after only 20 years or so. The upheaval is occurring not across generations, but within individual careers. The rules are being rewritten while people are still playing the game. And that seems unjust."³⁸

There appears to be no allegiance to any one country when it comes to the need to satisfy corporate profit and its shareholders. Outsourcing, in whatever form, appears to be cyclical and the fall-out in the US caused by outsourcing is very likely to be seen in India as happened in Ireland. Patni Computer, a company with 7,000 employees worldwide, is India's sixth-largest information technology services company. It is but one of a handful of global outsourcing companies now facing competition from lower-wage markets such as China and Southeast Asia, as well as from US outsourcing giants like Accenture Ltd. and IBM Corp who have set up operations in India.

Aparna Jairam of Mumbai, is under no illusion that her own IT job would face the danger of being replaced by a worker in another country. Her own philosophy is to move with the times and not be cocooned in her own world for "that's the way life is".³⁹

As demand for offshore services drives up pay rates in India, there have been questions about the long-term benefits of outsourcing work to that country. IT workers in India, according to recent research, reported double-digit salary growth in 2003. Although salaries in India are still lower than those in the US, the narrowing wage gap and other unforeseen factors are leading some US companies to reevaluate the cost savings to be had by sending work offshore as previous savings of around 50% are now realizing about 20%. Some Indian companies such as Tata Consultancy Services have even begun offshoring their own work to China. One of the four largest exporters of software in India, Tata plans to have 15% of their global work force based in China by 2005.⁴⁰

No country appears to be unaffected by the outsourcing phenomena as call center workers in Dakar, Senegal, field calls from France 3700 miles away. Senegal's fiber optic cable from France gives the country a telecommunications infrastructure as good as any in Europe. Add political stability, young educated employees and French as one of its national languages, one can see why low-cost African outsourcing is luring investors and jobs. Although minimal, a mere 2% of French jobs are outsourced, outsourcing is becoming a huge industry in West Africa and is becoming a concern for French workers. Affiliated Computer Services of Texas has become one of the largest private employers in

Ghana employing over 1,700 employees who process American health insurance claims.⁴¹

Already, consultants are eyeing skilled workforce in countries such as Nepal claiming that India is beginning to be less cost-effective. As developing countries improve infrastructure and education, they will become the next harvesting ground in global outsourcing. Recognizing this trend, Patni believes that the implications of global sourcing will extend beyond information technology. In the future, "wherever I live," said Patni, "my doctor might be in Boston, my secretary in Bangalore, my accountant might be in Bermuda."⁴² Azhur of PCI believes that the future of IT work in Bangladesh will eventually face the same predicament as the US as more countries enter the outsourcing market. "Yes, some Bangladesh workers will be displaced by a lower cost, just as Irish workers are now being displaced - that's the nature of international business as long as you have a non-protectionist system which the WTO promises."

In a move that seem to indicate that some companies are responding to the pressure of criticism of their offshoring practices, employers such as IBM have adopted new internal-transfer policies that are aimed at filling more open positions with employees who would otherwise have lost their jobs due to offshoring. This gesture only came after internal documents revealed plans to send nearly 5,000 jobs to India, Brazil and other developing countries over two years to save on labor costs. IBM Vice President of Learning, Ted Hoff, would not confirm the impact that this would have on the number of jobs that would be lost. IBM says it expects the new policy will save money overall by reducing costs associated with hiring and firing. A spokesman said that moving an IBM worker would be 20% to 30% cheaper in the first year than hiring an outsider. Stephanie Moore, of Forrester Research in Cambridge, Mass., reports that her research indicated that more companies that send jobs offshore are finding new work for some of the affected U.S. employees. "... the fact is, it's less expensive to repurpose the people than it is to fire them and hire different ones."⁴³

While most companies have stopped disclosing the offshoring of jobs in the wake of the political outcry over the issue last winter, analysts say that there is no sign the trend has abated. Even when companies try to find new jobs for employees whose work is sent abroad, those employees do not always land similar positions. At IBM, some transfers may mean lower pay or a "comparable job" that may be work at a lower employment classification, with up to a 10% pay cut and a shift or schedule change. It is expected that if workers do not take the comparable job they "will be separated from the

company without separation pay," meaning they are fired. IBM's severance is typically two weeks of pay for every year worked.⁴⁴

Conclusion

Perhaps the service industry will follow the strategy recently adopted by Chrysler: outsource 60% of the production of their new Jeep Wrangler to their suppliers with those companies footing the costs of capital and labor. Nothing new to the concept of outsourcing jobs to suppliers except for the fact that this eight-year agreement has the blessing of Lloyd Mahaffey, the Regional Director of the United Auto Workers in Ohio. The deal protects current workers from pay cuts as well as introduces what has been termed as "a highly unusual two-tier wage system" that will see some workers getting paid less than their peers even though in the same manufacturing complex. The alternative being the chance that Chrysler would shut its plant entirely. A fourth of the Chrysler workforce will shift to the supplier – workers have the option to move to the supplier, retrain for another job without sacrificing pay, or retire. To sweeten the deal Chrysler agreed to invest \$1.2b in new vehicles that would keep the plant busy for a decade. This deal pushes the outsourcing phenomenon to a new level as American manufacturers try to narrow the gap between their Japanese rivals and themselves. Some like BMW and Porsche outsource their entire manufacturing so the auto manufacturing industry is closely watching the results of this one-in-fourteen assembly plant.⁴⁵

There is much evidence that indicates that the US and its workers are in a position of "sink or swim", reflected in the responses of those interviewed. While expressing grave concern over the current state of the US economy and their own future, there is recognition that the US cannot isolate or protect its economic borders if the desire is to participate in a global economy.

Eighty-five-year-old Jay Forrester, a retired professor at MIT's Sloan School of Management – no relation to Forrester Research – is skeptical of the burgeoning outsourcing movement. "I think it's going to produce a tremendous political backlash, and will be significantly curtailed in a few years," he warned. "I think it will drive the standard of living of the United States down to the level of the countries that we're outsourcing to."⁴⁶

In October 2003 Robert Kuttner, co-editor of *The American Prospect*, wrote in the *Boston Globe*⁴⁷ about the demise of workers in the manufacturing industry following Levi's announcement that its world famous jeans will no longer be manufactured in the US. His

article questions what happens to workers displaced by outsourcing and whether or not their new jobs, if any, pay a living wage. He believes that the outflow of jobs is part of a natural global economy but believes that the US should "work to retain jobs that can be saved" and explore "what kinds of jobs replace the ones that go". He believes that, while there is no definite solution, government does have plenty of leverage based on two studies by the Russell Sage Foundation.

"The first, titled "Low-Wage America," exhaustively surveyed manufacturing and service industries across America. It found that employers have a lot of latitude in how they structure jobs and career opportunities. In the same industries, some companies chose a low road of high-turnover, low-skill, low-pay jobs as well as outsourcing and moving work overseas. Others made heroic efforts to upgrade worker skills and keep good jobs at home. Some manufacturing jobs simply can't compete with low-wage overseas labor, but others definitely can through better technology and skilled workers."

"Government can help or hinder this process through its training and career-ladder programs (or their absence). It can use tax policies to make it easier for companies to move offshore -- as the Bush administration has done -- or harder. Unions can promote decent and competitive jobs, and government policy can be friendly to union-management partnerships or hostile."

"A second forthcoming Sage book, titled "Downsizing in America," finds that a lot of job shedding is indeed occurring, especially in manufacturing. But over time this process is largely offset by the generation of new jobs. Most laid-off manufacturing workers, however, don't want to work at Wal-Mart. Again, the real question is how we ensure a plentiful supply of good jobs as technology keeps evolving."⁴⁸

It seems that the same findings are applicable to the service industry. It is unfortunate that Government has not clearly addressed solutions to this predicament and so provides no clear vision for the service industry. In fact, the Bush administration has encouraged outsourcing: "Treasury Secretary John W. Snow, in the latest sign that the Bush administration intends to directly defend free trade despite the loss of American jobs overseas, argued in an interview published yesterday that outsourcing ultimately helps the US economy. Snow told *The Cincinnati Enquirer* that outsourcing 'is a part of trade . . . and there can't be any doubt about the fact that trade makes the economy stronger....' Many economists, including the Federal Reserve chairman, Alan Greenspan, say the competition leads to the type of

innovations that drive the US economy forward and ultimately create far more jobs than are lost.”⁴⁹

These statements appear to contradict the Secretary of State, Colin Powell, who during a visit to India in the same month of John Snow’s interview, stated that: “People without jobs are political issues.... We have to make sure that we are . . . creating jobs for Americans who may have been affected by outsourcing. . . .”⁵⁰

While this paper has delved into the advantages, disadvantages and economic reasons for outsourcing, one area needs to be addressed to complete the picture: that of corporate profit translated into shareholders’ interests.

Take the example of the Boston-based company, Gillette, who, although not taking US jobs overseas, announced shifts of manufacturing and distribution jobs from Britain and Germany to Poland to lower costs. This move emphasizes the fact that the United States isn't the only nation losing jobs to low-cost countries. Western European nations are losing jobs to Eastern Europe and even Mexico is losing jobs to China. With a restructuring that underscores the forces behind an economic recovery that is failing to translate into new employment in the United States, corporations are squeezing operations to lower costs and boost profits - rising profits mean rising stocks that benefit executives and shareholders.

“With globalization and free trade, it's only natural that jobs will move to regions with lower wages, Poland is also a more central location for distribution than the UK. The benefits of those things will accrue to the shareholders of Gillette.

But the average US worker is not sharing those benefits, Bitner said. Hourly wages rose only 1.6 percent in the past year, and since September the economy has averaged only 60,000 new jobs each month, well below the 200,000 or so economists say should be created at this stage of the economic recovery.

We need to start talking about this problem and not just blithely saying, ‘Free trade is the solution’ just because it boosts corporate profits and Wall Street likes it.” - John Bitner, chief economist at Eastern Investment Advisors in Boston.⁵¹

So throughout the debate over the practice of outsourcing, any intentions by the politicians and solutions schemed up by the economists and theorists to the plight and outcome of both the manufacturing and service industry worker remains evasive.

Hilary Rodham Clinton advocates a need for a strategy that will focus on critical areas of innovation, new job creation, workforce development, connectivity expansion, and collaboration between industry, academia, labor and government. She believes that government needs to equip companies and workers to be more competitive by further developing the digital economy and by working to end trade and tax practices that undermine competitiveness. Her belief is that innovation will be the force that will allow leadership by the US through a national agenda that promotes research through tax incentives and direct investments in science. Clinton goes on to promote her belief that workers need to adapt, that government needs to attract more people to science, math, engineering and technical disciplines, through grants to universities and loan programs to students, so that the US workforce does not fall behind those in India⁵² and China who graduate far larger numbers of engineers and scientists.⁵³

This theory is part of the current political debate that is becoming more prominent as the presidential election nears its finale in November.

Ironically, at least 18 states are now outsourcing welfare benefits calls to India.⁵⁴ Some economists and politicians now worry that offshore outsourcing could have a negative impact on the US by draining tax coffers. If tax payments equated to a quarter of earnings, the loss of 3.3m white-collar jobs translating to \$136b in wages would effectively mean a decline of as much as \$34b in federal, state and local tax.⁵⁵

It is not particularly clear how the economy will eventually adjust to the current outsourcing situation. Based on research in Fall 2003 by the Fisher Center for Real Estate and Urban Economics, authors Bardhan and Kroll describe four possible outcomes:⁵⁶

1. Services outsourcing proves more costly to the economy than the earlier round of manufacturing outsourcing: There would be slower growth of higher paid jobs in the US as other parts of the world increase skilled high-tech professionals. After prolonged unemployment, workers would be absorbed into lesser paying services jobs resulting in a downward adjustment of salaries and wages. This would eventually make the outsourced positions competitive again.
2. A backlash against globalization that would slow down the outflow of some jobs and provides a measure of protection.
3. Jobs are redistributed: This would see the shifting of jobs from large employers to smaller companies operating

in the support sector. This “vertical disintegration” would be accompanied by internal outsourcing as work moves from high-cost regions to other low-cost regions in the US.

4. The US economy focuses on new development resulting in new service activities, new jobs.

While current hiring figures are on the increase, Paul Gudonis, chair of the Massachusetts High Technology Council in a July 2004 statement, said that the overall technology market still was not able to accommodate the number of unemployed high-tech workers in the state: "I know there's hiring going on but there are still a lot of unemployed and underemployed people out there."⁵⁷

This paper and the theories researched, unfortunately leave little solace for an employee in the service industry today. With few alternatives or solutions to the

outsourcing situation, for many, it is too late to adapt and become competitive in an industry that is so speedily evolving without sacrificing their current standard of living. An alternative would be to transition them, if they are flexible and able enough, to the source of the labor in the hope that their experience can acquire them higher-level positions. The downside of this, as this paper indicates, is that outsourcing appears to be cyclical which means that they may face the same dilemma they currently find themselves in within a few years. Future generations need to look at a strategy by which they can enter this boiling-pot of an industry, arming them with the knowledge that they will need to evolve at an even greater pace than the very industries they are in, in order to stay in the global marketplace. One can only hope that by that time, industry and government can reach a point where competitiveness will not necessarily mean job loss, and corporate profits are a result not of outsourcing and cost saving but of a strong standing in a global economy.

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