

Meeting the Offshoring Challenge

By Robert Atkinson

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Introduction

The growing trend of companies moving information-based service sector jobs to low-wage nations is receiving heavy coverage in the news media and is spurring intense debate among policymakers. With unemployment and a general sense of economic insecurity coloring the presidential campaign, both candidates have tried to seize the initiative on the offshoring issue. President Bush faced a storm of criticism after his chief economic advisor expressed optimism about the economic benefits of outsourcing. Now, on the campaign stump, Bush says he is "as concerned about outsourcing as the next person. But the way to deal with outsourcing is to make America a better place to do business, not a worse place." The way to do that, Bush argues, is to lower companies' cost of doing business, primarily by cutting their taxes. Meanwhile, presumptive Democratic nominee Sen. John Kerry argues that the Bush team's initial assessment of the benefits of outsourcing is a true indication of its views. Kerry says Bush and his advisors have "delivered a double blow to America's workers, 3 million jobs destroyed on their watch, and now they want to export more of our jobs overseas. What in the world are they thinking?" Even with strong job growth in the last few months, this issue is not going away, because it stems from the inexorable trend of U.S. jobs -- even middle and higher wage jobs -- being opened up to international competition.

The truth is, the Bush administration has done little to respond to the trend, and in some cases has made matters worse. The administration's economic policy consists primarily of cutting taxes, particularly for the wealthy, while talking tough about the need to reduce non-defense discretionary spending (even as it makes huge new spending commitments, such as the new Medicare prescription drug benefit). On the global front, the administration's economic policies have been a mix of unprincipled protectionism, flaccid attempts to prevent other nations from manipulating currencies and stealing U.S. intellectual property, and annual attempts to cut funding for the International Labor Organization's efforts to raise labor standards. Meanwhile, administration policies to help workers are straight out of a Charles Dickens novel: cutting unemployment insurance, denying laid off service workers Trade Adjustment Assistance benefits, and cutting job training programs. It is no wonder that growing numbers of Americans are questioning our nation's historic commitment to free trade and open markets.

The offshoring panic, meanwhile, has triggered a spate of ill-conceived legislation aimed at punishing companies that send jobs overseas. At least 35 states have proposed legislation aimed at preventing state funds from going to companies doing work overseas, either directly or through subcontractors. At least six states have issued requests for proposals that require the work to be performed in this country. And the 2004 federal budget contained provisions prohibiting the federal government from awarding certain contracts to companies that perform the work overseas.

Such proposals are fundamentally flawed. First, they raise costs for taxpayers, just as restrictions on imports raise costs for consumers. For example, when New Jersey discovered that one of its contractors was using 12 workers in India, the state renegotiated its contract and required the contractor to use U.S. workers instead. The state gained 12 jobs, but at a cost of nearly \$1 million to its taxpayers -- funds that could have been better spent on boosting the state's economic

competitiveness. It is also worth noting that states routinely contract with companies that are based in other states. (To disallow that practice would be a violation of interstate reciprocity compacts.) Contracting with companies that have workers overseas is no different.

Moreover, restrictions designed to curb offshoring can easily have unintended consequences. For example, legislation proposed in Pennsylvania to curb both outsourcing and offshoring would have largely shut down Gov. Ed Rendell's procurement reform efforts, which had saved Pennsylvania taxpayers over \$50 million through May 2004. Finally, there is a risk that undue restrictions on government procurement practices could escalate into a destructive trade war as other nations close off their government procurement contracts to American firms.

Opponents of offshoring also have fanned fears that data sent to a foreign company is less secure than data handled by a U.S. company. For example, legislation was introduced in California that would require companies processing data outside the United States to disclose specific information about the data they share -- including the type of personal information in question, and the country where the information is stored and the countries with which it may be shared. Congress is considering legislation that would provide notice to consumers that their data may be sent offshore. But to the extent that these proposed laws are motivated by the desire to protect citizens' privacy, they may be solutions in search of problems. Privacy regulations that cover how U.S. companies handle their customers' personal information will continue to apply no matter where those companies, their subsidiaries, or contractors process data.

If we are to successfully compete in the global economy -- and preserve support for globalization itself -- then, to paraphrase Monty Python, it is time for something completely different. In a prior report, PPI has argued that while offshoring provides some economic benefits, particularly lower prices for consumers, it is also a potential threat -- to middle-wage jobs in particular. It is PPI's position that neither the right's "get cheap" agenda nor the left's inclination to erect walls makes sense. Instead, the offshoring challenge requires an aggressive three-part Third Way agenda to help the U.S. economy adapt and innovate.

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