

Globalization, Job Creation and Inequality: The Challenges and Opportunities on Both Sides of the Offshoring Divide¹

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I. INTRODUCTION

The topic of globalization inevitably attracts feverish attention, and usually, strongly held polarized viewpoints. This is to be expected of an economic phenomenon that has created clear “winners,” while strategies for harnessing the growth potential of globalization for broader social and economic growth in developing countries, and for compensating those who lose out in developed ones, still prove elusive. On one side, there are the gushing advocates of globalization, who see it as a solution for many ills that beset the world today, including the curse of global poverty, a viewpoint best exemplified in a simplistic way by Thomas Friedman (2005). While the latter may just be the most clichéd among the votaries of globalization, there is a legion of believers in the seemingly limitless possibilities unleashed by a combination of technological hubris wedded to free market-based economic optimism. The suggestion that globalization can solve all problems for everybody, that it is an ideal state to aspire to, in a context where the reality often clashes with the hype, reminds one of Gandhi’s response to an insistent reporter’s query on what he thought of Western civilization,.... to which Gandhi is said to have replied...”I think it would be a good idea”....

On the other hand, many commentators confound the dislocation and churning in much of the developing world with the impact of forces of globalization, when actually public ire is aimed at policies inspired by a particularly extreme form of laissez-faire capitalism.

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Local failures at the level of policies and governance are quickly attributed to global forces, and the seemingly intractable problem of poverty is laid at the feet of increasing international trade and investment. The record of globalization, however, whether in exacerbating poverty or eliminating it, is not so clear. As Pranab Bardhan (2006) points out, it has been neither a panacea nor a plague.

This article focuses on the phenomenon of offshoring,² which has become one of the iconic manifestations of globalization. By offshoring, I mean a process whereby the production of a good or service that was earlier being carried out domestically in the industrialized countries, say the US, is now transferred to a developing country, with the primary objective of importing the product or service back into the US. This definition serves to highlight the difference between offshoring, on the one hand, and foreign direct investment for purposes of serving foreign markets, as well as other standard international trade transactions, on the other. It also underscores the one-way nature of offshoring and its politico-economic aspects. While offshoring of blue-collar jobs in manufacturing, mostly to the countries of East Asia, has been going on for a while, recent years have seen significant amounts of offshoring of white-collar jobs in information and communications technology enabled services activity, such as back office work processes, call center operations, medical transcription, accounting, legal research, radiology jobs among others. At present, there is increasing evidence of the offshoring model having climbed the “value chain,” implying that higher paid, critical jobs in the realm of R&D and innovative activity are now at risk in the developed countries.

While initial reactions in both the US and India, the two main economies involved in the present stage of services offshoring ran along predictable lines, with some in the US media calling for a ban on the continuing hemorrhaging of jobs and many in India celebrating their influx, there is now an awareness of the greater complexities involved. It needs to be mentioned at the very outset that there should really be no dispute regarding some of the basic facts at play, i.e. that the number of jobs impacted adversely in the developed countries, such as the US, is not huge, perhaps less than a million until

² Sometimes inaccurately referred to as outsourcing.

now. Also, there is no question that the process of offshoring has created a number of jobs in countries such as China and India, which perhaps would not have materialized otherwise. However, it is when one goes beyond this immediate, comforting fact that some of the complexities begin to emerge.

Rapid increase in global economic interdependence and technological change has now given rise to a worldwide labor market in a wide range of occupations, where workers in high-wage, advanced industrialized countries compete with workers in the lower-wage developing world; competition has been atomized, as it were, - in addition to competition between countries and firms, one can now refer to competition between individual workers, based in distant parts of the world.³ A large number of jobs have become globally footloose. As offshoring in services activity joins in the outflow of manufacturing jobs, concerns are being raised in industrialized countries about serious future job losses, or at the very least, about healthy job creation in the future. With offshoring reaching Research and Development related jobs, there is growing disquiet about the potential impact on job quality, future competitiveness of developed economies, and their standards of living.

On the other hand, developing countries are facing their own set of problems associated with offshoring. It is true that there have not been any job losses due to offshoring, indeed the opposite being the case. However, rapid growth and broadening opportunities in these countries are posing challenges of growing inequality, uneven job creation, cultural clashes, lopsided development, widening rural-urban divide, and educational, infrastructural and institutional constraints. Both China and India are grappling with the issue of how to harness the opportunities created by globalization/offshoring and technological developments to help eradicate poverty, and utilize them for broader social and economic development. The initial understanding of offshoring as an unqualified gain for the developing world and a loss for the advanced is now being supplemented by the realization, on both sides of the world, of gains, as well as potential dislocations and

³ Of course, in the absence of offshoring US labor would have competed, to a lesser extent, with immigrant labor.

disruptions, including a more sober appreciation of the distractingly seductive charms of the IT industry in India.⁴

This essay takes a look at some of the issues surrounding the impact of offshoring on future job creation, inequality, and related issues on both sides of the geo-economic divide, focusing on the US, the leading country involved in services offshoring, and on India, the primary beneficiary of this process. Some of the questions raised by this exercise are: What is involved in the process of offshoring, in terms of the disparate and seemingly contradictory concerns and issues of individual countries? What issues come up while trying to promote job creation in developed countries and broader social development in the developing countries?

2) The US Perspective

The past couple of decades have witnessed the confluence of a number of political, economic and technological factors that have given rise to a global, white-collar labor market and to the consequent upsurge in services offshoring. To begin with, this period has seen an ascendance of market economics and the opening up of previously, relatively closed economies to trade and foreign investment. This made possible the shifting of manufacturing plants, back-offices and R&D centers of multinationals to China, India, Russia and E. Europe. Additional factors include the large wage differentials between high wage developed and low wage developing countries, and since the colleges and institutions of higher learning in these countries have been successful in producing large numbers of graduates, there was also the added bonus of skilled labor being not just cheap, but plentiful as well. The combination of the factors listed above, and the ever looming cost cutting imperative have compelled western companies to embrace the emerging opportunities for shifting cost centers overseas. The final element that made the global labor market viable in practice has been the revolution in information and communications technologies, and the coming of age of the Internet. Some specific factors that were instrumental in India's getting the lion's share of services offshoring,

⁴ Many on the Indian side disapprove of looking a gift horse in the mouth, but investigating the impact and fallout of offshoring is necessary for exploiting its potential for broader growth.

apart from the much cited usage of English as a medium of communication, include what might be termed general institutional similarity, as in similar financial, accounting, marketing and legal systems, as well as compatible business culture and practices (see e.g., Bardhan, Kroll, 2003). In the case of offshoring of R&D, the diminishing cost-effectiveness of innovative activity in developed countries, the need to “design to market” in developing countries, and of course, the availability of low-cost scientific labor are among the reasons leading to the now global spread of corporate R&D (See Bardhan, 2006).

i) *Impact on Jobs*: There is little data, and also little agreement on the ongoing and future potential impact of offshoring on job loss in developed economies. Pressed on by media reports of continuing job losses in the US, and simultaneous establishment of offices of US firms in India, varying estimates of job migration and potential future job losses have been developed in recent years for the US, as well as for other OECD countries; some of these estimates focus on direct job outmigration that can be attributed to offshoring, some on potential job losses in future, and others on the overall macroeconomic effects on the economy. Forrester Research (2002) led this stream of investigation and projected a loss of 3.3 million jobs in the US by 2015 due to offshoring. Bardhan and Kroll (2003) analyzed the attributes of jobs and occupations that make them offshoreable, and matched them to the entire occupational structure of the US economy. They claim that there are upto 14 million jobs, or 11% of the entire employed labor force, in white-collar occupations that are vulnerable to being offshored. More recently, Mckinsey (2005) arrived at the same proportion (11%) of jobs at risk, whereas Alan Blinder (2006) now calculates that the number of offshoreable jobs is closer to 40 million, and that economists and others have “underestimated both the importance of offshoring and its disruptive effect on wealthy countries.” In any case, the prospect of major churning in the labor markets of the developed countries is a distinct possibility in the future.

Academics, economists and policy makers have lined up to debate the extent of the impact on jobs, as well as the other pros and cons of offshoring for the US economy. While there is broad agreement that direct job losses from offshoring have been small to date, relative to the size of advanced economies, the effects on future job creation and

income levels are heavily contested. A number of business and academic economists argue that the effects are “win-win,” or at worst insignificant, in terms of employment and income (see McKinsey (2003), Mann (2003)). Others argue that the current stage is different from earlier periods of offshoring because of changes in comparative advantage, and could potentially have negative income effects (Samuelson, 2004).⁵ Many belonging to the latter camp also claim that there are few signs of any emerging sectors or occupations that will create significant numbers of new jobs, such as those created by the US software sector during the 1990s at the height of the first wave of manufacturing offshoring. On the other hand, the adherents of the minor-impact school suggest that China, India, Malaysia, Philippines and Eastern European countries that have been the beneficiaries of offshoring, have severe constraints on how many more offshoring related jobs those economies can create, absorb and sustain.

ii) *Distributional Impact and Disruption*: While the resolution of the job creation debate may well lie in the future, even the most optimistic concur that offshoring has been a disruptive process with strongly negative distributional effects. There is evidence about the contributory effect of manufacturing offshoring, as one of two key factors, technological change being the other (Feenstra, 1995), to the rising inequality between blue collar and white collar workers in the US. There is growing recognition that globalization (in the form of services offshoring) is partly responsible for the increasing wage inequality between white collar occupations that are offshoreable and those that are not. There is also evidence that manufacturing offshoring has led to urban decline in areas losing manufacturing jobs (e.g. in the US Midwest), and there is concern that this could be repeated in urban or suburban centers specializing in services activities vulnerable to white collar offshoring. The “hollowing out” of manufacturing, a phrase popular since the 80s, may be accompanied by the “pockmarking” of services sectors, if many occupations across different sectors start becoming “at-risk”. While offshoring has contributed to value-addition and productivity growth, mentioned by Mann (2003) among others, the gains have appeared in the form of corporate profits, and have accrued

⁵ A partial list of significant contributors to this debate would include Jensen and Kletzer (2005), Bhagwati et al (2004), Dossani and Kenney (2004), Atkinson (2004), Hira (2005).

primarily to the employers, senior executives, shareholders, some high-skilled, non-tradable, non-offshoreable occupations, and as CEO/Management compensation. In 2005, corporate profits as a share of national income, at around 14.5%, were at their highest point in US history. Economic growth has not translated itself into robust job growth, and more importantly, into growth of well paying jobs.⁶ Even the *Economist* had to concede: “The pace of productivity growth has been rising again, but now it seems to be lifting fewer boats. After you adjust for inflation, the wages of the typical American worker—the one at the very middle of the income distribution—have risen less than 1% since 2000. the increased offshoring of services to India and other countries has expanded the global supply of workers. This has reduced the relative price of labour and raised the returns to capital.”⁷

iii) *Long-Term Issues of Competitiveness and Standard of Living*: Economists are largely in agreement on the importance of continued innovation as the primary way to create high-paying new jobs in the US and other developed economies.⁸ One of the key characteristics of the economic history of the United States going back to the era of rapid industrialization in the late 19th century shows that the innovative dynamism of the US economy, the creation of new goods, new services, new value, and the temporary global monopoly that comes with them, as well as the spillover effects that these innovations have on productivity in other sectors of the economy, have played a large part in the creation of high paying jobs, and in the sustained rise of living standards. The response to job loss concerns on the part of many economists has been to point to domestic

⁶ While some may argue that an average American profits as well since many people are invested in the stock market directly or indirectly through pension funds etc., what most lose through low wages and disappearing jobs is not compensated by dividend income and capital gains. Major holdings of stocks, bonds and other financial assets are, by and large, the preserve of the wealthy (The Wealth of US Families; The Survey of Income and Program Participation, US Census).

⁷ See also Mahoney et al (2006). Of course, not all of the increase in inequality is to be blamed on offshoring. Other culprits include low bargaining clout of labor, technological bias favoring some skilled labor, and fiscal and other policies.

⁸ This is also a key assumption of the “win-win” school of thought, since both US and India stand to gain in this scenario, with the latter continuing to get the “older” jobs. On the other hand, lead times for individual countries and for Schumpeterian profits for firms are getting squeezed, with greater implications than before for policy intervention (see Smith, 2006).

innovative activity as the key to future job creation and economic growth.⁹ Recently, however, there have been increasing signs of offshoring of R&D and innovative activity to China, India, Russia and some E.European countries, in the form of the global spread of corporate R&D centers. While the innovations coming out of these centers are still the intellectual property of the parent companies in the West (further exacerbating the distributional consequences mentioned above, since the benefits will again largely accrue to the shareholders of these companies), the increasing innovative capacity being built up in many countries around the world in the critical masses of engineers, scientists, entrepreneurs and the necessary support personnel may change the balance of competitive advantage for innovation and job creation in the longer term. The steady erosion of a base of skilled workers from the West, through the education and hiring of critical, innovative occupations abroad, and the movement overseas of many research, developmental and support activities that are crucial to the whole infrastructure of innovation clusters may result in a more globally distributed origin of future innovations than had hitherto been the case. It is possible therefore, that the next wave of innovation, and its job and income benefits will bypass the US and other advanced countries. On the other hand, there is also the possibility, at least for the immediately foreseeable future, that the infrastructure of innovation in places such as Silicon Valley in the US, in the form of the financial, legal and the public-private institutional structure, built up to shepherd start-up companies to their initial public offerings, and the entrepreneurs to their sought-after riches, as well as the profit potential of the large US market, will continue to attract start-up technology firms, even if the products are initially conceived and developed abroad by fledgling Indian or Chinese firms.

The combination, therefore, of increasing offshoring of high paying jobs, sluggish domestic job creation, growing inequality and rapid technological change, in an environment buffeted by irresistible global forces, has led to a situation where the prospects for a healthy labor market are fraught with uncertainty and a backlash against globalization and offshoring is a distinct possibility. Add to this mix the speed with

⁹ After all, if the same job can be effectively carried out at a distance, but at a fraction of the cost, after adjusting for productivity difference, then it stands to reason that the developed countries need to create jobs that are “new,” or not easily replicable or non-offshoreable; hence the need for innovation.

which services offshoring has gained momentum, and the broad spectrum of occupations and sectors it can potentially affect, and it is easy to see why the political economy of the topic can be so contentious.

The fact that many of the vulnerable white collar jobs are high-paying ones, and those occupying them are better connected to a greater range of levers of power than the blue collar workers affected by manufacturing offshoring, sheds further light on the nature of the political debate. Some obvious suspects have lined up on the two sides of the issue. While the unions, and some politicians, have been in the forefront of the anti-offshoring battle, the corporate sector and much of the academic and policy establishment has concentrated on stressing the positives, and adopted a “wait and you will see job growth” position. The policy debate has largely revolved around a hands-off policy, R&D spending to promote innovation, renewed stress on math/science education, retraining for workers, workers wage insurance¹⁰ and administrative measures to curtail offshoring, with the political right mostly favoring the earlier options, and the left the latter ones. However, it should be noted that many political positions have become scrambled due to the offshoring of white-collar jobs. While the left appeals for protectionism, the right has staked a moral claim to be on the side of the working people in poorer countries, with the disingenuous internationalism of the right replacing the traditional internationalism of the left. On the other hand, some of the free traders of yesteryears have mutated into xenophobic protectionists.

3) The Developing Country Perspective: The Limited and Exclusive Impact of Offshoring

In the developing world, job creation in large numbers has always been considered an effective weapon in the struggle against poverty. So initially, the sudden influx of jobs created by manufacturing and services offshoring seemed like an answer to the problems of economic backwardness and development in both China and India. Indeed, one can get the impression, from reading the business press, that the ongoing boom in services offshoring, and in the IT and ITES (Information Technology Enabled Services) sectors is

¹⁰ See Kletzer and Litan (2001) for the wage insurance proposal.

the major engine of growth for the Indian economy. Recently, however, there has been somewhat increasing recognition of the limitations of, and the challenges thrown up by offshoring related rapid development, both of the manufacturing base in China and the Information Technology sector in India. While the number of jobs created, in India at least, is again a matter of some debate, the consequences, both positive and negative (even though the latter may have emerged due to the very success of attracting large numbers of offshoring jobs), are being better appreciated.

The manufacturing miracle of China, fueled partly by the offshoring by multinationals from developed countries (a significant part of China's exports to the US, for example, are actually carried out by US multinationals with manufacturing plants in China¹¹), has created a large middle class, primarily, although not exclusively, in the coastal regions and some of the larger cities. This has led to a significant economic divide between these regions and the rest of the country, as well as to broader urban-rural disparity. Rapid increases in productivity, while a sign of the dynamic learning curve of the Chinese manufacturing sector, have also resulted in unemployment and underemployment, conservatively estimated to be in the hundreds of millions. These numbers, taken together with the population released from agricultural occupations and the accompanying urbanization have accounted for the large migratory populations in search of work. Pollution and growing wage inequalities have also been some of the other byproducts of this wave of offshoring of manufacturing to China.

In India's case, it is surely nobody's contention that offshoring has been purely detrimental to her economic fortunes. According to NASSCOM figures, there are approximately 1.3 million people now employed in the IT and ITES sectors. While the benefits of job creation due to business process outsourcing (offshoring from the US) in India are indisputable, a number of factors need to be clarified. They include the questions surrounding the magnitude of job creation due to the job inflows, the issue of sustainability of the offshoring model, the geographic and social distribution of economic gains, the extent of spillover benefits to the rest of the economy and some potential

¹¹ See http://www.epinet.org/content.cfm/briefingpapers_fdi_fdi.

economic consequences and side-effects of the offshoring boom. In short, a critical appraisal of the impact of the IT industry therefore runs along the lines of “too little, too concentrated, too hyped and too detached from the rest of the economy”.

i) Magnitude of Job Creation: One of the stylized facts of our time seems to be that it is the era of large countries. Earlier, there was a widespread impression among laypeople that small countries (read Singapore, Hong Kong, Ireland etc.) have all the advantages – they are easier to govern and manage, they are more responsive to policies, and they have a greater propensity for faster economic growth. Globalization has now unleashed the power of the larger developing countries, with their large labor pools, and large supply and demand side economies of scale, although most of the large developing countries figure way down in terms of GDP per capita. In other words, a country’s role on the international stage today, more so than in earlier times, is a function of its GDP rather than GDP per capita – one could call it the comforting solace of large absolute numbers, a mirage that sometimes blinds one to relative figures and per capita achievements (or the lack thereof). Impressive achievements at the national level, whether they are the size of the IT industry, the number of engineers graduating each year and so on, are put in their proper perspective once the relative and proportional context is applied.

For example, the newly released provisional data of the Indian Economic Census are quite revealing, when it comes to the magnitude of net job creation by the IT industry (Note: The provisional release does not include data on wages, incomes or inflation) . The Census covers the boom years of the Indian IT and ITES sectors, 1998-2005, the period when services offshoring acquired a sustained momentum. Table 1 shows rural and urban non-farm employment and employment growth data for 11 states and the union territory of Delhi, which together account for 80% of non-farm employment in India. A surprising finding of the Census has been that non-farm rural employment grew faster (3.33% per annum) than urban employment (1.68%) in this period. As Table 1 shows, the fastest employment growth overall, among the major employment generating states, has occurred in Kerala, Tamil Nadu, Punjab, UP and Andhra. If one looks at urban job growth rate alone, then the fastest growing states are Kerala, Tamil Nadu, Punjab, Delhi and Gujarat, in

that order. In terms of absolute numbers of urban jobs created, Tamil Nadu and Kerala again occupy the top two spots leaving the traditional giants Maharashtra and Gujarat, as well as the states most identified with the IT phenomenon in India, such as Karnataka and Andhra Pradesh, further down in the list.¹² Of course, since the jobs created by the IT industry are significantly higher value jobs, the state GDP data may end up looking somewhat different. In any case, seen in the context of the country as a whole, or even in the context of the component states themselves, the magnitude of job creation by the IT related sectors does not seem very large. As a minor digression, one might note that while West Bengal's net urban job creation rate of 0% might seem to confirm the steady decline of the state's industrial base, which is only now being addressed, the extraordinary performance of Kerala, a state with somewhat similar political and economic culture, is a puzzle. In the absence of more data, one could perhaps speculate that the inflow of remittances from the state's diaspora, because of its more dispersed nature of recipients, succeeds in mitigating credit constraints of small entrepreneurs. This might end up creating more jobs than the much larger, but concentrated investment flows to the IT oriented states.

TABLE 1

	Total Employment 2005			Ann.Avg Growth Rate		Jobs Created	
	Rural	Urban	Combined	1998-2005		1998-2005	2005
				Urban	Combined	Urban	Combined
Andhra Pradesh	5,718,202	3,152,389	8,870,591	1.32%	2.40%	276490.62	1,356,908
Bihar	1,382,776	893,304	2,276,080	-1.77%	0.27%	-118951.8	42,557
Gujarat	2,569,131	3,245,054	5,814,185	1.48%	1.39%	317137.29	535,534
Karnataka	3,319,579	2,658,856	5,978,435	0.91%	1.86%	163368.64	723,567
Kerala	3,683,752	1,875,585	5,559,337	8.08%	5.39%	786856.98	1,709,634
Madhya Pradesh	1,868,201	2,352,283	4,220,484	0.54%	1.04%	87026.404	294,858
Maharashtra	4,625,398	7,201,168	11,826,566	0.91%	1.79%	442462.86	1,381,219
Punjab	1,059,033	1,628,475	2,687,508	2.64%	3.59%	271522.67	587,964
Tamil Nadu	5,188,276	4,678,357	9,866,633	3.78%	4.62%	1070098.1	2,674,363
UP	4,195,837	4,344,201	8,540,038	1.40%	3.03%	402858.05	1,610,346
West Bengal	4,921,382	4,396,644	9,318,026	0.00%	0.87%	0	548,224
Delhi	73,079	4,006,954	4,080,033	2.31%	2.21%	591977.15	578,889
Total	38,604,646	40,433,270	79,037,916			4,290,847	12,044,065

¹² Tamil Nadu does have a sizeable IT presence, but more importantly it has a diversified manufacturing industry as well, which has been doing well and which probably accounts for the high rate of urban job growth.

ii) Selective Impact: A general matter of concern to many economists, social scientists and activists in India has been the fact that liberalization and reforms are being carried out on an already very unequal distribution of income and wealth. The recent benefits from the Indian IT sector have by and large bypassed large segments of the population, particularly those at the bottom of the social spectrum, thus further exacerbating economic disparities. Indeed, as things stand at present, the IT and the ITES sectors are mostly confined to a handful of large cities, and to the westernized, upper-middle classes of these metropolitan areas. Even the lowest paid offshoring jobs, such as call center operators or customer care representatives immediately place the recipients in the top decile of the income strata, and in a majority of cases, the employees come from a relatively affluent economic and social background to begin with. Needless to say, the resulting increase in income and wealth disparities has had an adverse impact on the price of housing and the general cost of living for those not involved in the IT industry in these metros, particularly in the absence of affordable and reliable public services, such as transportation. Skewed development priorities, such as inadequate expenditures to combat widespread illiteracy, neglect of the physical infrastructure, due to both private and public failures, and a general inability of the state structures to marshal resources commensurate with a booming economy do not make for a sustainable and conducive environment in which the gains from offshoring can be usefully tapped. The rural-urban divide, as well as increasing inequality in urban areas further add to the mix of factors that can create social instability and impede harmonious economic development.¹³

iii) An Industry-Isolate: Although a number of other countries-competitors, in Asia, E.Europe and Africa, exist in the marketplace for offshoring of services, the significant mass of expertise built up in India in the whole spectrum of IT and ITES activities suggests that the outlook for services offshoring for the foreseeable future is sustainable, despite the well-known problems of wage-inflation in some selected occupations, selective shortage of skilled personnel and so-on. The problem again lies elsewhere. Since the general path of development of the IT sector has been largely linked to the

¹³ With the notable exception of the Rural Employment Guarantee Act, many government policies in the economic sphere in the past couple of decades have been skewed in favor of the top decile or so, whether it is the absence of a long term capital gains tax on equities or the inheritance tax.

offshoring model, with the domestic market playing second fiddle, the social exclusivity of the sector referred to above is compounded by economic isolation. IT is potentially an input into practically every industry and sector, and is a major factor in productivity growth wherever it is used. It requires widespread dissemination to be really effective, and hence the importance of a large domestic market. The potential size of the domestic market should therefore be both an incentive as well as a pre-requisite for rapid growth on a sustained basis, whereas technological islands of excellence can be difficult to maintain.¹⁴

In addition to the specific attributes of the IT sector in India mentioned above, there are some other reasons for its somewhat exaggerated importance in contemporary Indian discourse. It could be said that the IT sector fits in well with the pervasive white-collar ethos of India's upper social strata and its aspirations for global recognition. While the dignity of blue collar labor has never been traditionally highly prized by the upper classes, although attitudes are changing, information technology represents modernization, power and prestige in today's global economy and polity, and to display surpassing expertise in it is to be a global player of some importance. One could also say that India has its own version of the "blackboard rule",¹⁵ and that the IT sector is compatible with the educational structure in the country as well as the underdeveloped physical infrastructure.

The challenge faced by the emerging economies of China, India, South Africa, Russia, Brazil, and other countries, therefore, is how to ensure that the benefits of this new,

¹⁴ Some claim that the rapid development of offshoring, the construction of back offices of US MNCs, establishment of corporate R&D centers in Bangalore and a few other cities has given rise to an Indian version of the Dutch disease of old. To recall, the latter is an economic term to denote the connection between an increase in revenues from natural resources, or indeed any development that results in large inflows of foreign currency, such as offshoring from the US to India, and an increase in the exchange rate, which has an adverse impact on other sectors, such as manufacturing, by making them less competitive. In the Indian context, the wooing of skilled professional and managerial talent by the IT related sectors has bid up their wages in other sectors as well, impacting growth potential there (see Kocchar, 2006).

¹⁵ "Blackboard rule" was a term coined to describe the propensity of Russian science to be biased in favor of subjects that involved use of a blackboard and did not need sophisticated apparatus/infrastructure/equipment/supplies etc. The underlying reasons are the relatively simpler logistics and "planning" involved.

emerging, white-collar specialization of labor, brought about by technological and institutional changes, can be channeled and harnessed for larger social and human development goals. Despite the differences in the economic structures, and even the institutional and political setup in these countries, they all face somewhat similar developmental dilemmas, particularly when it comes to the joint impact of the twin forces of technology and globalization.

4) Policy Matters, and Is There a Joint Perspective?

The problem of mitigating the pain of adjustment from the changes wrought by globalization, in its present stage of services offshoring, is common to both developing countries and developed countries alike. The interplay of trade and technology has created “gainers” and “losers” in both sets of countries, leaving us grappling with some critical questions - What are some of the issues involved in economically feasible yet socially responsible approaches, which can help reconcile what may seem to be contradictory and conflicting objectives on the two sides? Are policies promoting job creation in developed countries consistent with, in conflict with, or irrelevant to goals for developing countries? Glib formulations about a win-win situation arising out of offshoring, or the gains from trade and technology, rightly seem simplistic and patronizing, particularly to those who are dislocated and displaced. Ideally speaking, even in the absence of globally sustainable and reconcilable policies, a search for long-term, global strategies is necessary for a better understanding of the issues and problems confronting those impacted adversely in both sets of countries.¹⁶

¹⁶ That the experience of globalization has been a mixed one, especially for developing countries, is well summed up by Rodrik (2002), “For most of the world’s developing countries, the 1990s were a decade of frustration and disappointment. . . Latin American countries experienced growth rates significantly below their historical averages. Most of the former socialist economies ended the decade at *lower* levels of per-capita income than they started it. . . East Asian economies, which had been hailed previously as “miracles,” were dealt a humiliating blow in the financial crisis of 1997. That this was also the decade in which globalization came into full swing is more than a minor inconvenience for its advocates. If globalization is such a boon for poor countries, why so many setbacks?”

Issues in the US:

If there is an economic environment of rapid growth in innovation with broad dissemination through the economy, accompanied by the attendant economy-wide benefits of productivity growth and creation of high paying jobs in the context of an overall positive global growth environment, then the political economy of offshoring will be somewhat manageable on the US front. However, there is really no law in economics or the sciences that says innovation has to accelerate and that the “next big thing” is around the corner. While there will always be gradual, creeping innovation, the development of general purpose technologies, such as IT, which has an economy-wide positive impact, both on job creation and productivity, is not inevitable. The newly emerging international specialization of R&D activity, however, gives rise to the possibility of carrying out cooperative, international efforts to increase the pace of innovation and benefit both developed and developing countries. The challenge for developed countries is thus two-fold - in addition to promoting innovation, with all that implies in terms of education, R&D spending/subsidies, retraining and so-forth, they will have to ensure the widest possible social returns of these innovations so that the benefits are not appropriated by the top management of firms alone.

The unprecedented challenges that developed countries face in restructuring their economies are further underscored by a structural attribute of these economies. The economies of most developed countries are primarily services based, with manufacturing playing an increasingly minor role, leading to three additional sets of challenges. 1) Unfortunately for them, most of the services that are not offshorable are precisely those where productivity growth is intrinsically slow, or sometimes not even desirable, which means that they become relatively costlier, condemning advanced economies to even higher cost structures.¹⁷ 2) Many of these non-offshorable occupations operate in winner-take-all markets leading to large disparities in incomes within the same occupation, in addition to rising inequalities across occupations. 3) To further add to the labor market woes, the competitive advantage that many developed countries enjoy in a range of services is difficult to exploit from a domestic job creation point of view, since

¹⁷ See Blinder (op. cit.) and Nordhaus (2004) for what is known as Baumol’s disease.

the exports of services, such as consulting, legal, technical services and so on, frequently leads to establishment of offices abroad, and as a consequence, local hiring rather than at the headquarters.¹⁸

Faced with this dilemma, the more progressive among policy makers, recognizing that protectionism at home pits workers here against those in the developing world, call for extracting additional resources from those quarters that are the prime beneficiaries of the offshoring in order to pay for measures that can insure and retrain displaced workers, promote innovation and create new jobs.

The issue of global labor standards is also brought up by many. Anderson and Cavanaugh (2004), while arguing that “The U.S. government should ensure that tax, government procurement and subsidy policies are instruments for supporting good U.S. jobs....,” also suggest that “raising standards overseas is vital to retaining stable and substantial jobs at home....” While any attempt to improve labor standards anywhere is to be welcomed, the issue is somewhat of a red herring, at least in the case of the present crop of services jobs. In any case, the constant invoking of global labor standards tends to put the onus of adjustment on the developing world. The predicament that the developed countries find themselves in is after all a natural consequence of the twin forces of capitalism and globalization.

Issues on the Indian Side:

In India’s case, the economic challenges revolve around boosting the job creation rate, and spreading the largesse more equitably across the country and across a broader cross-section of society. The critical question, therefore, is perhaps not the nature of the jobs themselves, which is of greater political importance in the West, unlike in India, where there are vast, relatively untapped human resources, and there is overwhelming need to attack poverty through job creation. The offshoring connected job bonanza has come about primarily because of a copious supply of relatively cheap, skilled labor. Some

¹⁸ This is due to the manner in which most of these services are delivered to customers - production and consumption occur at the same place.

policies, therefore, suggest themselves. A significant increase in the numbers of graduating college students, together with incentives for moving offshoring operations to secondary and tertiary cities is called for. While the market is taking tentative steps in the latter direction because of rising costs in the main metros, policy intervention is still required to hasten and direct the process.¹⁹ In the matter of boosting numbers in higher education, the recently enacted reservations policy, in addition to its other social objectives, has succeeded in giving a jolt to the moribund system, hopefully leading to the proposed 54% increase in the intake of students.

Services offshoring, however, is unlikely to deliver the goods in terms of a sizeable number of generated jobs. To make any serious inroads into unemployment, India will have to tap the emerging opportunities in manufacturing. The Chinese success in manufacturing can be quite instructive in a number of different ways. The ongoing offshoring of manufacturing from all around the world to China has had a relatively more beneficial impact on the socio-economic structure than services offshoring has had in India's case. This is due to the fact that manufacturing has created, in absolute terms, a significantly larger numbers of jobs in China; because local sales and purchases by foreign MNCs in the domestic Chinese market have also been sizeable, with all the spillover effects that accrue to manufacturing both from upstream and downstream sectors; and finally, because it created blue-collar jobs, the natural and traditional employment transition for the peasantry throughout history. Manufacturing has created employment opportunities for a critical group, and mitigated somewhat the potential inequality and social tensions that might have emerged had the new job opportunities accrued to the traditional urban elite alone. There are increasing indications that manufacturing offshoring spillovers from China are already finding their way to other neighboring countries. The potential of a sizeable domestic market, low cost, blue-collar labor, and infrastructure improvements, particularly in the transportation nodes and coastal entrepôts may attract more manufacturing to India from the developed world in the near future.

¹⁹ There are additional benefits to this policy of urban decentralization in terms of relieving the pressure on larger cities and bringing urbanization to the hinterland.

Development of rural entrepreneurship is another potential source of job growth. Indeed, the Economic Census data referred to earlier seems to suggest that like in China, where small, rural, self-employed enterprises have grown fast, are financially healthy and have contributed significantly to employment growth (see Zhang et al, 2006), the self-employed, rural landscape in India is also showing signs of dynamism. Incidentally, while offshoring surely cannot be a major job creator for rural unemployed, a few non-profit and quasi-non-profit organizations have launched efforts recently to help train people in non-urban areas for some of the non-IT related offshoring occupations, which do not require higher education, such as in selective design-animation related work.

Although India is somewhat better placed to harness globalization and offshoring for economic growth and job creation than many other developing countries, the lack of a political consensus at the national level, and the absence of an effective public-private strategy limit the possibilities. While the market enthusiasts would like to downsize the government and the public sector²⁰, those on the left seem to be in constant opposition to various economic policies, and have few suggestions for tapping global opportunities for poverty alleviation. For example, a consensus could revolve around politically feasible, job creating FDI and public-private initiatives in infrastructure. As the successful examples of many other countries have shown, the most effective way of exploiting the possibilities from globalization for broader development is actually through national policies that take into account distinctive national features, institutions and imperatives, rather than an obsession with standardized international ones.²¹ As a matter of broad strategy, a politico-economic policy oriented toward job growth will deliver both jobs and economic growth, and help mitigate poverty.

²⁰ Few in India know that the US, with a labor force less than one-third of India's, has approximately as many people in the state sector. True, the composition of the state sector in the US is entirely different, being concentrated in educational, regulatory and governance spheres; the point here, however, is that the relevance and importance of an effective government in India is greater and broader.

²¹ See Kumar and Sharma (2006). As pointed out by Rodrik (2002), "China's economic policies have violated virtually every rule by which the proselytizers of globalization would like the game to be played. China did *not* liberalize its trade regime to any significant extent. ..to this day, its economy remains among the most protected in the world. .. Most striking of all, China achieved its transformation without adopting private-property rights, let alone privatizing its state enterprises.".

Academic and policy literature has been prolific in suggesting lessons to be learnt by India from the Chinese economic experience. It should be borne in mind, however, that in addition to India's better ability to politically manage conflicts,²² there are a number of other areas of a purely economic nature where India is either better placed, or in a position not to emulate some of the more harmful economic policies of the Chinese.²³ The responsiveness and viability of the Indian banking system, the wide array of expertise developed in services sectors that are of increasing importance in the global economy, more transparent political and economic governance, a growing tradition of technology entrepreneurship, and an assertive civil society that tries to ensure that the more egregious and disruptive of reforms will be kept at arms length, bode well for India's ability to seize the opportunities of globalization in an equitable manner.

Some General Remarks: Having started with manufacturing processes, offshoring has embraced large swaths of services sectors, and now innovative activity as well. This single largest burst of restructuring of the global economy since the colonial era presents many challenges, to developed and developing countries alike. The issue of job creation has been the key issue stressed in this paper, since it is critical to poverty alleviation in the case of developing countries, and is a matter of increasing concern in the developed ones. The prospect of job losses in industrialized countries far into the future, and rising concerns about creation of new, well paying jobs may lead to calls for protectionism, to political pressures on developing countries or to efforts for some sort of global accommodation. On the part of developing countries, offshoring has brought home the lopsided nature of economic growth, and is leading to efforts to seek ways to tap the growing opportunities of globalization for creating jobs for broader development. Since offshoring presents challenges on both sides of the geo-economic divide, then given the present economic and political realities it is necessary to pose a broad question : How can the process of globalization in general, and offshoring in particular, be managed

²² See Pranab Bardhan (2003).

²³ China seems to have enjoyed for a while the best of both worlds – capitalism and socialism. The Chinese version of this “equilibrium” is unstable and fraught with contradictions, and is “addicted” to unsustainably high economic growth rates. The opaque public decision-making of quasi-private enterprises, the high savings rate driven by a disappearing safety net and a Soviet-style penchant for gigantism are just some of the stranger features of the economy.

politically and globally in a manner that is conducive to broad-based growth for both sides?

The easy answer would be innovation, which may allow the present structural shift to continue without undue dislocation, and push the day of reckoning with increasing inequality further into the future. While the future rate of innovation is inherently uncertain, the increasing global specialization in innovative activity, the creation of a global scientific labor force, and the synergy between globally dispersed innovative regions might boost the chances of scientific breakthroughs. In the absence of a healthy rate of innovation, or indeed an accelerating rate of innovation, which would be required in developed countries in order to stay one-step ahead in new job creation, the global distribution of jobs may turn out to be a bitterly contested and divisive issue. It may also turn out to be difficult to postpone dealing with issues of rising inequality in the US if some pre-emptive measures are not taken soon, whether in terms of a national wage insurance policy, or some other fiscal or regulatory measures.

For India, offshoring has resulted in the creation of jobs, albeit in a few concentrated locations and with limited impact. While the present stage of net-job creation due to offshoring has been result of foreign and domestic investment in India, with a view to exporting to US markets, many on the left seem to suggest in a knee jerk reaction that it is the thin end of the wedge for other kinds of FDI that might displace local firms and jobs, because it may also target the domestic market in India. A politico-economic consensus is necessary for utilizing the present global conditions for harnessing globalization, in general, and offshoring in particular, for broader economic development, whether it is on issues relating to FDI, infrastructure or education.

While the search for a consistent, global approach might seem difficult in the light of the contradictory labor market issues on the two sides, a number of other contradictions of present day global economy and polity further bedevil the attempt. There may be one global economy, but there isn't one global polity; there may a global labor market, but there is no free labor mobility across borders; there may be one political superpower, but

there are a rising number of economic powers; the global supply of labor may have suddenly increased from the point of view of MNCs, but the supply of capital is the same; indeed, the present model of economic globalization is also being accompanied by political localization and fragmentation, leading to unforeseeable consequences. As Freeman says...” The world needs a new model of globalization,”...

It is interesting to note that while most of the criticism of globalization, until recently, originated in the developing world, the critiques of offshoring have come, for obvious reasons, from the developed West. As noted earlier, some of the criticism is misdirected. Part of the reason for conflating the impact of globalization with those of other economic, political and social policies is due to the fact that globalization, or the broader, more general opening up of societies and economies has, at times, been the vehicle for bringing in the more radical of the pro-market ideas to the developing world. On the other hand, if it is understood in its expansive form, it has also served to bring together many of the NGO activists and political voices from across our shrinking world. This new stage in international consciousness has been brought about by a realization, that unlike in the past when the “winners” and “losers” were separated by national boundaries, this time around both reside in the same country, leading to the complex nature of cross country alliances that we see developing today in some of the grassroots, global social movements. It is perhaps fitting that an issue with global resonance should have a global constituency in search of global solutions.

END

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