

International Outsourcing: Trends Across U.S. Firms

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Abstract

Outsourcing is a popular trend among U.S. firms, and likely to grow significantly in the future. Outsourcing involves purchasing a value-added activity from an external source; typically, one company hiring another company to execute tasks that used to be done in-house. It is also called international outsourcing if the task is performed overseas. This may include downsizing departments in order to transition the activities to an environment (often to another country, such as India) where they are better executed, usually due to cost efficiencies. Functional areas susceptible to outsourcing include manufacturing, accounting, engineering and particularly information technology. In the 21st century, U.S. companies continue to move away from completing non-core activities themselves in an effort to emphasize and deploy resources in support of core competencies. *In this paper we will explore the following:*

1. *Why has international outsourcing become increasingly attractive to U.S. firms?*
2. *What are the overall implications relative to competitiveness for U.S. firms?*

Introduction

Most U.S. companies strategically plan to maximize profits and gain a broader consumer base in the most cost effective way. Firms today embrace the concept that they must go global to maintain or gain a competitive edge, as well as grow their markets. Moreover, friendlier domestic and international government doctrine has been adopted by way of subsidies, export financing, establishment of foreign trade zones and the creation of special government agencies, which have made “outsourcing” key in the pursuit of such growth. Milan Sheth, member of Ernst & Young’s BPO Advisory Center lists the following factors that drive outsourcing:

“There are a wide variety of factors that are driving the increase of outsourcing but ultimately, many organizations are looking for bottom line impact. Factors influencing demand consist of: focusing on core competences, market requirements, access to skills and knowledge, cost measurability and control, high cost of system upgrades, benefits from economies of scale, fast market entry, and flexibility.”¹

Why has international outsourcing become increasingly attractive to U.S. firms?

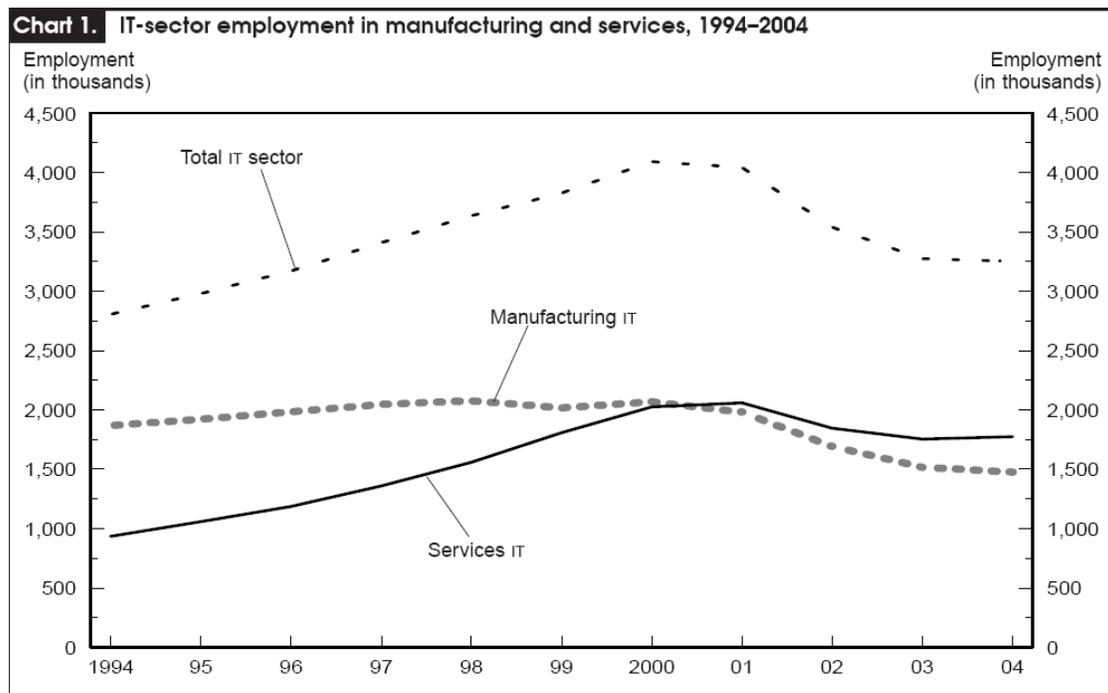
Numerous firms, such as Microsoft, Oracle, and Sun have found India a very attractive country for outsourcing. India holds a spectrum of inexpensive and well-trained engineers that are phenomenally high-tech oriented. The Indian connection has and will continue to become a candidate for overseas outsourcing. In particular, they have dominated in low labor cost, project management skill, and technological cleverness. India lifted strong during the mid-1980s with the software industry. Approaching the 1990's, they became the forefront supplier, contracting services in software, because of its skilled low-cost labor and manageability. Labor costs are not the only significant factor attracting U.S. firms, but also adequate supply of labor. For instance, many U.S. firms call centers are being relocated in low-end rural areas. This transition may have engaged the company with high shortages of labor, high call volumes, and a fairly low education rate. With dissimilarity, India has cities that offer a wealth of the same services with a strong labor power that can permit conditions mandated through labor regulations. US firms specializing in call centers have approximately fewer than 400 employees' staffed. India's call centers have a median size of about 1,000 employees. Currently, the sectors that are aggressively leading India are healthcare, banking, technology, and insurance sectors. The business processes have been claims processing, accounting, medical transportation, and call centers. The United States and other developed countries are hardly affected by India's growth with call centers and financial data processing. Weaknesses in India that could deter US firms are there shortage of managerial talent. Secondly, maintaining a flawless relationship with transerfered entities and organizations in developed countries.

In the past, countless financial, IT and computer service industries have only outsourced their production/technology activities. Today, several firms are moving customer service, engineering, accounting and many back office operations to foreign locations. During an earlier outsourcing boom, many blue-collared low-skilled jobs were outsourced to developing countries, including Mexico following NAFTA. Most white collar jobs were considered unsuitable for outsourcing. Today, many white collar jobs are also outsourced to low-wage, developing countries. The U.S is an 80% service industry economy, with many white collar jobs to complete. Robert W. Bednarzik, visiting professor at the Georgetown Public Policy Institute, Georgetown University expounds on the current trends of employment by industry and occupation in relation to outsourcing:

“The immunity from global competition that U.S. white-collar workers have enjoyed for so long has seemingly started to vanish. There is an increasing concern the next great wave of globalization will come in services—in particular, white-collar services. Numerous articles have described the concerns of computer programmers, software engineers, and other workers in the information technology (IT) field— about losing their jobs as companies move service jobs overseas to take advantage of lower labor costs” (p.11).ⁱⁱ

A major question is the impact such transitions to greater international outsourcing impose on general levels of competitiveness, as well as the economy as a whole.

In Chart 1, Bendnarzik illustrates the IT-sector employment in manufacturing and services from 1994-2004:



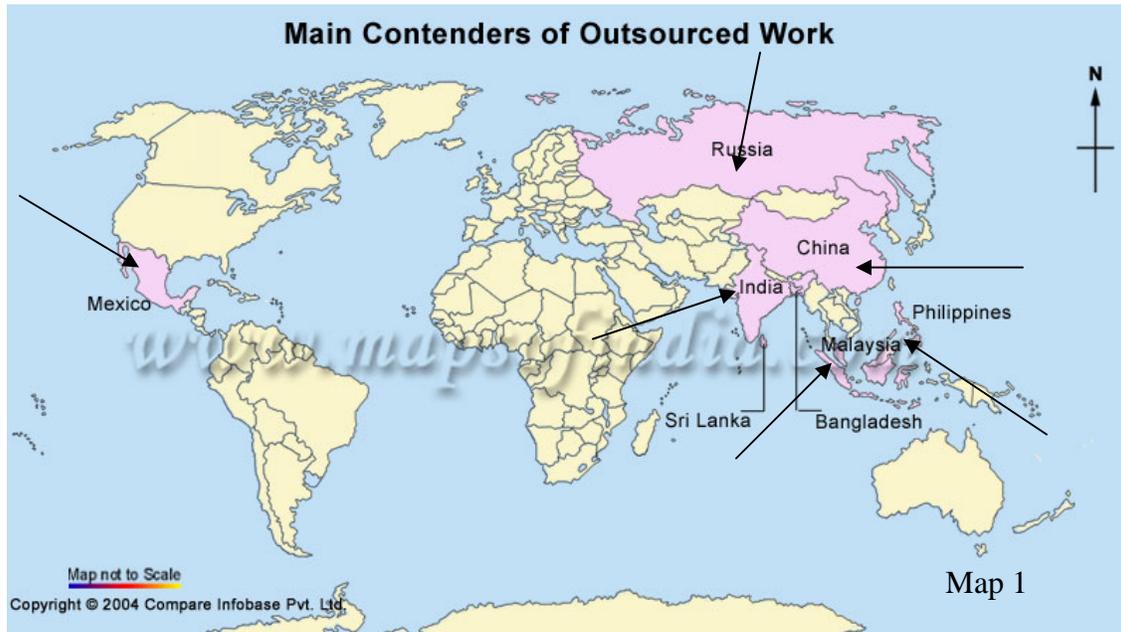
Bednarzik, R. "IT- sector employment in manufacturing and services" Visual Scale. In Robert W Bernarzik "Restructuring information technology: is offshoring a concern?" Monthly Labor Review, 128(8), p.14.

Such trends have not only affected large companies, but many small companies as well. For instance, a small company, Cognizant Technology Solutions, has migrated services to India to better compete and globalize its services. An article sponsored by Nucleus software exports, Ltd., a U.S. firm that focuses on global banking software, cite testimony of small and large firms who insist that outsourcing is on an upward climb:

"Outsourcing is big business, generating global revenues of \$298.5 billion in 2003, according to the research firm of Garter Inc. Some Americans have realized they can actually make money on this and grabbed the opportunity. "We didn't create the market, we are following the market," says Michael Parks, CEO of Deerfield-based Revere Group Ltd., a mid-sized consultancy that acquired a 70-employee firm in Bangalore recently, in order to compete for outsourcing contracts. Outsourcers reap gross margins of 25% to 50% on projects sent overseas, says Jai Shekhawat, CEO and co-founder of

Fieldglass Inc., a Chicago-based firm that advises companies on outsourcing. A contractor typically pays between \$11.70 and \$16.25 per hour, including benefits, to a computer programmer in Mumbai, India, and charges its American client between \$18 and \$25 hourly for that worker, says he” (para. 3).ⁱⁱⁱ

Map 1 gives a visual geographic outlook on countries who are main contenders of outsourced work:



“Map Contenders of Outsourced Work” Visual Scale. Maps of India: Jobs Outsourcing to India. From [http:// www.mapsofindia.com/outsourcing-to-india/index.html](http://www.mapsofindia.com/outsourcing-to-india/index.html) (December 21, 2006)

What are the overall implications relative to competitiveness for U.S. firms?

In the past, the United States has set the standards for leading innovation in new services and technology. With increased research and development (R&D) in other countries, the competitiveness for the U.S. has become threatened. Overall, to remain competitive, the United States government must acknowledge and address illiteracy and lack of advance training among its work force. It is estimated that every ten years the literate population of India goes up about 10 percent. In contrast, literacy rates among the United States citizens are have declined significantly.

Conclusion

Historically, the U.S. has traditionally been a dominant player in technological advancement. Today, research and development (R&D) activities by firms in other countries often far exceed those of the U.S. This pattern has emerged as we increasingly outsource such activities, hindering efforts to remain dominant in innovation. As international outsourcing on a number of levels continues to be a significant part of U.S. firm activity, we must explore the ramifications on both current and future competitiveness of U.S. firms and the country as a whole.

References

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