

1 Globalization, Offshoring and Jobs

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In recent years, the labour market consequences of globalization in general, and offshoring in particular, have been the subject of intense debates in the general public and among experts. News about the numbers of positions offshored from EU or US companies to countries in Asia or Latin America regularly make the headlines. The presumption is that those offshored jobs represent net job losses for the outsourcing economy. The reality is more complex.

Offshoring being a relatively recent phenomenon, empirical work on the effects of globalization on labour markets has traditionally focused on the effects of trade. Early work concentrated on the relationship between trade and wages, as the presumption was that there would be no effect on aggregate levels of employment if labour markets function smoothly. Since the 1990s, this view that there should be no substantial link between employment and trade has slowly changed, due to new theoretical developments and new empirical results. These results generally suggest that trade (imports) may cause job displacement in the short run, due to adjustment costs. While far fewer studies have been able to consider differences between the long and short run, those that have done so generally find that, in the long run, there appears to be a positive relationship between imports and employment. However, this may not be true for all firms that engage in importing, as suggested by a number of recent studies.

The phenomenon of offshoring has been the focus of an increasing number of studies in recent years. Offshoring involves the breaking up of the production process, which allows the relocation of some parts abroad and increasing specialization at home. Offshoring frequently leads to productivity increases and expanded sales in the company that offshores. The result may be that the same company ends up employing more rather than

less people as a consequence of offshoring. This is the so-called “scale effect” of offshoring. The jobs created may be of a different type, though, than those offshored. In addition, there is a strong likelihood of indirect employment effects of two forms that are triggered by offshoring. First, if as a consequence of offshoring a company can provide its services to other businesses at lower cost, the latter may be able to expand activity and employment (depending upon their employment-sales ratio). Second, if offshoring results in lower prices to final consumers, their real income increases and some proportion of that real income will be spent on domestically produced goods and services, again raising overall employment.

The employment effect of offshoring, thus, does not correspond to the number of jobs directly affected. It consists, instead, of the combination of a number of different effects the net-outcome of which is difficult to predict. Indeed, empirical work has found that the net-employment effects of offshoring differ across countries. Although it is statistically significant in most countries, it is in general considered to be small.

The employment effects are, however, likely to differ across type of workers. The evidence points in the direction that low skilled workers are more likely to lose and high skilled workers more likely to benefit. Very recent work also emphasizes that the effect of offshoring may differ across occupations, with workers in “tradable occupations” being more likely to lose than those in “non-tradable occupations”. To take a simple example, a taxi driver with relatively low educational attainment may not need to fear that his job be offshored to India, while a computer programmer with a university degree may see his job being relocated, as it can be performed online by similarly skilled people in China.

Just like trade, offshoring is likely to trigger a reshuffling of employment with some workers temporarily losing their jobs and possibly taking time to find a new one. This reshuffling can in theory lead to temporary surges in an economy's level of unemployment, but there is not much evidence that this indeed happens in practice. For the individuals losing their job, though, this is not much of a consolation as the transition may cause significant hardship for them and their family.

In this context, it needs to be kept in mind though, that offshoring and trade are not the only phenomena which result in separations between employer and employee: changes in technology; changes in consumers' tastes and preferences; and cyclical changes in economic activity all impact on job destruction and job creation. And the scale of churn, or turnover in labour markets, in modern dynamic economies is quite staggering. There is evidence that in countries like France, Germany and the United Kingdom job losses due to offshoring represent well below ten per cent of the total job losses in a given period of time. The corresponding figures were significantly different though in Austria, Denmark, Portugal and the Slovak Republic, where more than a quarter of total job losses were due to offshoring. One of the effects of the constantly ongoing processes of job destruction and creation is that OECD countries have experienced a shift in employment away from manufacturing into services industries.

Overall, the relatively scarce literature on globalization and employment can be summarized as follows. Firstly, globalization and, in particular, offshoring of activity may lead to higher job turnover in the short run. Secondly, in the long run, there is no indication that trade or offshoring leads to higher unemployment (or lower employment) overall, though, employment of low skilled workers may suffer while high skilled employment may expand. Thirdly, while the literature finds that these effects are statistically significant, the economic magnitude thereof is still debated, with many studies concluding that they are economically negligible. Fourthly, there is evidence that the structural change away from manufacturing towards services sectors in advanced economies goes hand in hand with the process of globalization. However, whether or not there is a causal relationship is still to be investigated.