

MADE IN  
CHINA

# Anywhere But Here

*The merits and perils of  
offshoring and its consequences  
for the North Bay*

By Gary Brady Herndon

**T**he United States has always been a land of opportunity and innovation. From its roots in agrarian society to the marvel of the Industrial Revolution to today's high-tech economy, American businesses and their workers set the standard for the world to follow. Ironically, now that America is the world's sole reigning superpower, some scholars, legal experts and a growing number of industry insiders now believe America's position as the leader on the world's business stage is changing. A new global economy and the growing trend toward outsourcing of jobs that historically have been the lifeblood of the American workforce are reshaping how American companies do business.

To address this issue and its impact on the San Francisco Bay Area, SofTECH, a Novato-based non-profit trade organization, held a panel discussion in late June titled "Outsourcing/Offshoring: The Good, The Bad, The Reality." *NorthBay biz* spoke with several of the panelists invited to participate in the discussion. Our goal is to provide our readers with a better understanding of the process of outsourcing and what lies in store for Bay Area businesses as more companies turn to outside sources to meet their needs.

Outsourcing is not a new phenomenon. American businesses have outsourced goods and services throughout the history of our nation. Historically, textile and manufacturing jobs went to areas of the country where labor was cheap and products were readily

available. To maximize their bottom lines and remain competitive with their U.S. counterparts, businesses focused on cutting costs and streamlining production.

The last two decades of the 20<sup>th</sup> Century saw the rapid growth in the field of information technology (IT). When, in the 1990s, companies began offshoring IT jobs, the trend escalated, taking jobs from American workers and relocating them to countries where labor is cheap, thus enhancing the companies' profits. Now, other areas of the economy, most notably in the service sector, are seeing jobs leave for offshore destinations, causing concern in the eyes of some, and hope for new and more profitable markets for others.

#### **Academia grapples**

Dr. Robert Eyler is chair of the department of economics and director of the Center for Regional Economic Analysis at Sonoma State University in Rohnert Park. He sees the North Bay as being in relatively good economic health despite the massive layoffs in the IT industry over the last several years. When industry jobs left for India, Ireland and Southeast Asia and, to a lesser extent, the desert southwest in the United States, Marin and Sonoma counties weathered the crisis well.

"The North Bay was insulated to a degree from the negative effects of the dot-com bubble bursting, due in part to the positive housing market and the highly attractive living conditions here," Eyler says, but adds, that the high quality of life in all of the

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San Francisco Bay Area also worked against area high-tech companies rebounding. “It was simply cheaper to go elsewhere where wages and the cost of living were relatively lower compared to California.”

Eyer says outsourcing, and by extension the growing trend of offshoring jobs, are by-products of growth, especially the rapid growth as seen in the area’s IT industry in recent years. As companies expanded rapidly in the 1990s, growing from small regional firms to international players in relatively short periods of time, he says the companies couldn’t meet their employees’ demand for higher wages that the area’s cost of living and housing prices required.

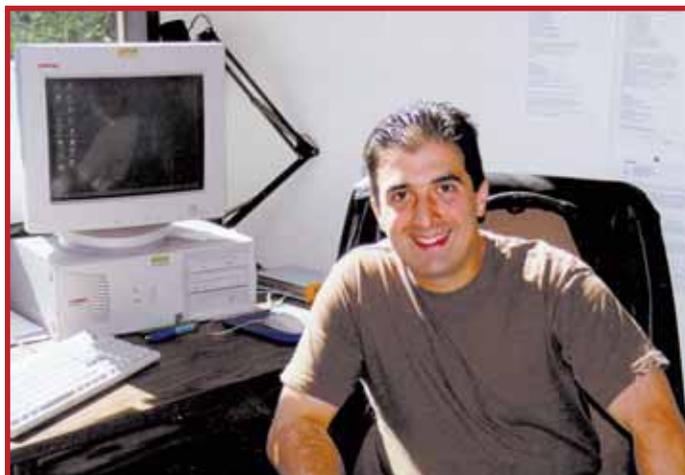
“You can’t expect a whole lot from business,” Eyer explained. “Ethics aside, businesses have to survive. In reality, outsourcing has been with us since U.S. manufacturing jobs were created. The difference is that, historically, the jobs were outsourced to other companies within the United States. Now those jobs are going to Malaysia, Singapore and India.”

In the past, Eyer says, living and conducting business in the United States gave manufacturers an edge over companies in other parts of the world. This positive business environment depended to a certain degree on national pride, a highly trained and quality workforce and the convenience of doing business on American soil. With the advent of the Internet and the emerging global economy, those days are passing, if not already passed. How Americans will react in the future is yet to be seen.

“We may begin to see communities placing new restrictions on businesses that locate into their communities with incentives for the companies to commit to keeping jobs at home,” Eyer says.



Knox Lundgren of MyPoints.com says his company has offshored simple service calls to India and Ireland, but warns that there are cultural issues to be aware of before you ship service jobs offshore.



Dr. Robert Eyer, chair of the department of economics and director of the Center for Regional Economic Analysis at Sonoma State University in Rohnert Park, holds to the traditional economic doctrine that globalization is here to stay and that education and retraining are the American worker’s best defense against global competition.

The moral issue of whether or not companies opt for American workers’ job security or the companies’ bottom line is ultimately with the stockholders, he notes. The lesson for American workers is “not to put all your eggs in one basket.” Workers, he suggests, might find it wise to retrain themselves in such a way to be more competitive and, in the end, more valuable to the company in the long term.

#### **Management feels your pain.**

Knox Lundgren understands the issue of offshoring from a management standpoint. Lundgren is senior vice president of operations and technology at MyPoints.com, a leading provider of Internet direct marketing services. His company became involved in outsourcing when MyPoints began sending customer service duties to an outside contractor within the United States. In 1997, the company went international, first to India then to Ireland, then back to India.

While the need to fill customer service jobs led to offshoring in Lundgren’s company’s case, he is quick to point out that there are obstacles that every company must confront to ensure customer satisfaction. Businesses, he says, have to pay attention to the small details and take steps to keep their customer base satisfied.

“The cultural component is often overlooked by executives,” Lundgren says. “The reaction of your clients to something as simple as a customer service agent with an accent can (upset) some customers. Any kind of communication, even e-mail, carries risks of being perceived negatively by clients.”

MyPoints, Lundgren says, focuses on outsourcing services that require a “template” response or answers that are consistently given to problems that fall within certain parameters. Real-time questions or questions that require contemplative answers are handled by in-house personnel so the customer gets an answer from a culturally sensitive company representative.

For Lundgren, tracking customers’ satisfaction to keep them happy is simply a matter of dollars and cents, “It costs more money to get new customers—up to five times more—than to keep the customers you have already.”

Lundgren is certain that in today’s global marketplace, “people go wherever they can get the best price.” But part of the reason he cites for the growing trend in offshoring is that companies can’t find enough workers with high-level skill sets in the United States to meet industry needs. The logical alternative is to tap into the growing number of technical workers from emerging economies



Jonathan Storper, a corporate lawyer and partner in the firm of Hanson Bridgett LLP, specializes in representing start-up companies and businesses interested in outsourcing or offshoring goods and services.  
(Duncan Garrett Photography)

abroad. Offshoring goods and services, even in a controlled technical environment, however, can present unique problems not found when doing business at home.

Lundgren uses software development as an example. The process, he says, requires a tremendous amount of effort and focus from everyone on the development team. When outsourcing in countries where cultural differences and language barriers come into play, things can go wrong.

“Trying to develop new software with workers on the other side of the world can lead to misunderstandings,” Lundgren says. “What you say to a foreign worker can be perceived differently. These things add up.”

As business as we know it changes, Lundgren believes industry will begin looking for new avenues of revenue, creating new jobs for displaced workers due to outsourcing. American workers will need to keep their heads up and “not assume the industry they started out in” is the one they will be in at the end of their career. Retraining, he says, will become a way of life for the American worker in the future.

“People need to be flexible and willing to change,” Lundgren, a former lumberjack, explains. “Workers need to see their career as their own little corporation. They have to become opportunistic to be able to take advantage of new opportunities that will be created.”

### **The legal bugaboo**

While management and boards of directors by nature focus on the bottom line to keep their companies competitive, the pain of losing a job to outsourcing falls squarely on the shoulders of the American workers. As a corporate lawyer and partner in the Bay Area law firm of Hanson Bridgett LLP, Jonathan Storper specializes in representing start-up companies and businesses interested in outsourcing/offshoring goods and services. He acknowledges the practice can be painful for workers but believes American workers will have to contend with the process for the foreseeable future.

“Outsourcing will continue,” Storper says. “We’re becoming a global economy whether we like it or not. We have had to stay ahead of the curve. If California and the United States does it right, it doesn’t have to be a bad thing for businesses or workers.”

Storper brings up a point that many within the outsourcing community, both employers and workers, think is partially responsible for the current migration of jobs from the United States to countries of the Third World. The H1B immigration program was created as a non-immigration work program that

allowed qualified workers to come to the United States to work for a specified length of time. These workers return home with the knowledge of how American businesses operate, thus creating the opportunity for them to start up their own companies to compete on the global market. Storper says blaming the loss of jobs on H1B immigrants, however, is not the answer. These immigrants are simply doing what new business owners have always done—learning the trade, coming up with new ideas and setting up shops of their own. The difference is they’re setting up shop around the world instead of across the street. American businesses don’t seem too worried enough about this process to object to the H1B program. In fact, they’re so dependent on the science- and computer-savvy workers that they’re continually petitioning the government to increase the number of the workers allowed in the country on H1B visas.

“Workers who come to the United States (whether H1B immigrants or foreign companies) are very important to our economy, especially in California,” Storper notes. Storper says not enough energy and resources are being put in the educational system to train American workers to be competitive in the fields of

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engineering and science. In the past, he says, the United States’ strength has been in creating new technologies and the jobs that are required to make them work. While immigrants from India and China have taken jobs away from California workers, immigration is not the problem.

“Well-educated foreign-born workers have been essential to our economic growth,” Storper says. “(In reference) to outsourcing/offshoring, I see it less as a brain drain than as brain circulation. Workers trained here in the United States are returning home and setting up businesses there,” creating a cheaper workforce that makes outsourcing profitable. “But they don’t just take jobs,” he continues. “They also start businesses while they’re here, and they create jobs here. Many tend to go back and forth between the U.S. and their homeland, building business in both places.”

This, of course, doesn’t help the American worker who just lost his job to offshoring. Still, Storper believes that restrictions to keep jobs in the United States would make us less competitive in the global marketplace. The answer, he says, lies with our government doing more to help train our workers and, where necessary, to retrain workers to help them keep their competitive edge.

“We shouldn’t demonize the world economy,” Storper says. “The important thing is to be sure our workers are the best trained in the world to ensure they are able to jump on the next new technology and remain on the cutting edge of industry.”

### **The other side of the coin**

The offshoring of IT jobs has become a template for other industries hoping to maximize their companies’ bottom lines. The



UC Davis computer science professor Norm Matloff has written extensively about the H1B immigration program and outsourcing/offshoring. He feels offshoring is an unsustainable trend that doesn't bode well for U.S. competitiveness in technology or for U.S. workers.

numbers and types of jobs projected to leave the United States in the next decade are sobering, to say the least. Consequently, not everyone embraces the economic siren call that proponents of outsourcing are so quick to espouse.

A vocal and widely respected opponent of offshoring can be found on the campus of the University of California Davis. While unable to attend SofTECH's panel discussion, Norm Matloff shared his thoughts on the effect the process is having on our economy. He is a professor of computer science and has written extensively about the H1B immigration program and outsourcing/offshoring, and the effect it is having on our economy. While he agrees that of the various job markets in the Bay Area the IT market has been the hardest hit by outsourcing, the impact on the region is just beginning.

"While there are always individual cases which are exceptions, any shift in the economic paradigm creates winners and losers. The executive class is the winner (in this case)," Matloff says, but even then he has reservations. "I think everyone loses in the long run. I don't think ultimately that offshoring/outsourcing is good for the bottom line."

Matloff admits that his hypothesis might place him outside the prevailing line of thinking in today's upper management decision-making circles. He notes, however, that many in those circles have indicated, when surveyed, that they are disappointed by the quality of work done offshore, and he questions whether the long-term effects of the process will be beneficial.

"Interestingly, many will still pursue offshoring, simply because they are mesmerized by the prospect of cost savings. They hope that once the bugs are worked out, they'll save lots of money. But suppose I'm right, and offshoring is not good for the bottom line in the long run," Matloff says. "Will companies (in the near term) even realize their mistake? It's not clear that management in America will be able to do that."

He poses the question: What if in three to five years businesses decide that offshoring is bad for business and opt to return to the United States to meet their manufacturing needs? The net result, he says, will still be devastating for the American worker.

"Those who lost their jobs have lost them for good," he says. "Historically, businesses have been unwilling to rehire qualified workers who have been out of work for an extended period of time."

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If such a hypothetical situation were to arise, Matloff sees other problems on the horizon. In the interim, American young people would be scared away from IT and other technical jobs after seeing the generation of workers before them lose their positions to outsourcing. The H1B worker program would have to be expanded to accommodate the needs of returning businesses, effectively leaving American workers jobless.

"Although politicians love to set up retraining programs to address such problems, retraining has always been a red herring," he says. "In the past, the problem has been that employers of programmers and engineers preferred to hire newly trained young Americans and young foreign workers in the U.S. on work visas, rather than hiring newly retrained older Americans. Now with globalization, the employers would rather train programmers and engineers abroad."

The UC Davis professor predicts dire consequences ahead if the offshoring trend continues unchecked. The current situation, he thinks, will create a ripple effect. While IT jobs have been hardest hit in the Bay Area thus far, other consequences loom in the future, including the demise of labor unions, the middle class and a general lowering of expectations in society. Already, he notes, other areas, including financial, architectural, legal and medical jobs, are being relegated offshore to take advantage of cheap labor forces abroad.

Regardless of which side of the issue you support, there are several points that are not up for conjecture. Outsourcing/offshoring is here to stay. It's happening at breathtaking speed. With the advent and rise of the Internet, no job is entirely secure; in fact, expect to see the spectrum of jobs lost offshore to expand exponentially as more companies turn abroad to meet their production quotas and to enhance their profit margins. ■

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