

OUTSOURCING AS AN BUSINESS STRATEGY AND ITS ROLE IN INTERNATIONAL TRADE



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ÖZET

Outsourcing global ve rekabetçi ticaret alanında yaygın olarak kullanılmaktadır. Outsourcingde şirketler özgün faaliyetleri üzerine odaklanırken, diğer hizmetleri yabancı partnerlerinden tedarik etmektedir. Özellikle bazı gelişmekte olan ülkeler daha önce gelişmiş ülkelerin gerçekleştirdiği outsourcing faaliyetlerini yapmaktadır. Bu durum gelişmiş ülkelerin bazılarında işsizliğe neden olmaktadır.

Gelişmiş ülkeler avantajlı oldukları sektörlerde outsourcingin işgücü üzerindeki olumsuz etkilerini azaltmaya çalışmaktadır. Outsourcing genellikle telekomünikasyon, gayrimenkul, yönetim, lojistik, üretim, müşteri hizmetleri, insan kaynakları ve finansal hizmetlerde uygulanmaktadır. Şirketler outsourcing'in yaygın olarak uygulanması ile yapabilecekleri en iyi işi yapma fırsatını yakalayacaklardır.

Anahtar Kelimeler: Dış Kaynak Kullanımı , Uluslararası Ticaret, Gelişmekte Olan Ülkeler , Küreselleşme, Strateji.

ABSTRACT

Outsourcing process is used extensively in globalized and competitive trade. Thus, corporations focus on their specific activities and provides other services from foreign partners. Especially, some developing countries initiated outsourcing which is previously carried out by developed ones. That situation causes unemployment in various developed countries analysed.

Developed countries try to diminish the negative effects of outsourcing on labour force in their advantageous sectors. Outsourcing is used mostly in areas including

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telecommunication, real estate, management, logistics, production, customer services, human resources and financial areas (Öztürk, Sezgili, 2002). Companies will find an opportunity to do their best jobs with the intensive application of outsourcing.

Key Words: Outsourcing, International Trade, Developing Countries, Globalization, Strategy.

INTRODUCTION

In today's world, developing countries have started to do some businesses in some sectors that were previously done by mostly developed countries by outsourcing. In these sectors, developed countries have labour force losses as a result of the competition of the developing countries. In accordance with the division of labour that the World Trade Organisation tries to form in the new economic system. It is inevitable for the developed countries especially that has labour force losses in some sectors change the situation of division of labour in favour of themselves by following a repressive approach. In the recent years labour force losses as a result of outsourcing has been discussed.

OUTSOURCING AS AN BUSINESS STRATEGY

By outsourcing piecing the production and distributing to the subcontractors-research and development that's a component of production, and services like design and marketing is bought from foreign countries. By outsourcing the enterprises avoid making capital investments and taking risks and they buy these with the possible lowest cost. (Erol, 2002)

Outsourcing can be defined as having the expert service providers make the business which is not included the enterprises skills. (Elmuti, Kathawala, 2000) By outsourcing among these provided business, enterprises get labour force, various equipments and some materials from foreign providers. (Gavin, Matherly, 1997). According to another definition it is an agreement between the provider of the service and the enterprise with the aim of providing any enterprise's services by the supplier. (Fan, 2000).

In our era of globalisation and rising competition the level of benefiting from outsourcing as a business strategy has increased. As it can be understood from the above mentioned definitions, by outsourcing some business related to the enterprise can be obtained by foreign sources. Thus enterprises focus on the core competences-core business and obtain other business from foreign firms.

It is not a new approach for the enterprises to take the advantage of outsourcing. In England there are examples of this by the private sector in the 19th century. In this period, especially in metal production there was an outsourcing application. Also in public sector these these applications were commonly used. In these years there are outsourcing applications in England in the fields of management of prisons, works of road construction, collection of public income and collection of waste material. In France outsourcing is applied in areas like railway construction and management and water storage and distribution (Öztürk, Sezgili, 2002)

In 1990s outsourcing was seen as a tool in the subjects like providing the economies of scale and efficiency in cost control fo the enterprises. In 2000s it has played an important role by having competition advantage in global strategies. (Öztürk, Sezgili, 2002) The outsourcing trade business between countries is seen as a new international trade type in the last quarter of the century that the globalisation process accelerated

While putting forward the various ways of modern world trade Krugman (1995) mentioned the distribution of production, the geographical regions as the concept of international or foreign outsourcing. According to the Feenstra's study in 1998 the development of international trade by outsourcing is a result of globalisation. The results of this new development are evaluated by economists and academists. Especially the retrogressive effect of the international outsourcing in industrialized countries on employment and costs are focused on. (Yoo, 2000)

One of the reasons of the common application of the outsourcing is the approaches that says enterprises should tend to use core business. As well as this it has been commonly applied in administrative business, estate, distribution and logistics, production, customer services, human resources and finance (Öztürk, Sezgili, 2002) Every Fortune 500 company in today's decade thinks about the application of the outsourcing. Among these 20 % of

them declared that by the end of the decade they will have realised the outsourcing agreements. (Lankford, Parsa, 1999)

Table 1: *Commonly used areas of outsourcing*

The usage areas	%
Information technologies	20
Administrative activities	15
Estate	10
Distribution	10
Human resources	9
Production	7
Finance	7
Customer services	7
Marketting	6
Transportation	5
Management	4

Source: Öztürk Azim, Sezgili Konuralp, (2002), “Dış Kaynaklardan Yararlanmanın Yeni Bir Rekabet Stratejisi Olarak Kullanılması ve Uygulama Süreci”, Uludağ Üniversitesi İktisadi ve İdari Bilimler Fakültesi Dergisi, Cilt XXI, s.2.

One of the reasons for the development of the outsourcing is the technological renovations. Technological renovations caused most of the services to be the subject of trade. As well as this, another factor is the great number of professional labour force by making relatively satisfactory educational investments in the developing countries. The lack of suitable job opportunities in these countries created a potential of labour force that can

work for lower incomes. Also the renovations in the business world enabled the business of the service sector is done by outsourcing (Matto, Wunsch, 2004).

Most companies evaluates outsourcing as a strategy that decreases the costs, brings in new skills and talents and provides financial flexibility. (Linder, 2004) One of the most important reasons why enterprises apply for the foreign sources is obviously the costs. But as well as the cost factor the main reason for the outsourcing is providing new technologies that the enterprises apply and put forward their own skills more efficiently and reach new information. Realising the enterprise functions like new product development, design, production, marketing and advertising there will be opportunities to reach new technologies (Koçel, 2005).

THE ROLE OF OUTSOURCING IN INTERNATIONAL TRADE

Today most of the business problem can be solved by outsourcing especially in information technologies area. The effect of outsourcing is bigger. Everyday the application of outsourcing is increasing in an organised way (Beaumont, Sohal, 2004) Most of the developing countries that have millions of low income employees enable the business shift to them. In the developed countries the risk of labour loss for the white collar workers, architects, scientists and etc can be mentioned. For example in USA it can be seen that these labour shifts to overseas countries like Far East, Latin America and North Europe. As well as these countries India is also an important country that attracts attention of service sector in Europe and USA. South Africa, Russia, Hungary and China is also trying hard to take part in the outsourcing process in America. The figure below shows the data about the issue.

Table 2: *Main companies of USA that exports engineering and scientific labour*

Name of the company	Number of the employees and the countries where they work	Labour
Accenture	5000 people in Philippines	Accounting and software
General Electric	22000 people in China and India	The plane production and medical research and development
Intel	3000 people in India	Design of chip and information technologies
Microsoft	500 people in China and India	Software design and information technologies
Oracle	4.000 people in India	Software design
Philips	700 people in China	Electronics, research and development

Source: Hira Ron, "Recent Trends and Possible Implications", Testimony of P.E. Chair, Research and development Policy Committee The Institute of America to the Committee on Small Business United States House of Representatives on Global Outsourcing of Engineering Jobs, 18 June 2003.

As the labour shift from the developed countries to the developing countries continues, in the near future projections we see that this shift would be faster in the near future. In the figure below the projections by 2015 the results of the labour force losses can be seen

Table 3: *The projection about the probable labour that is thought to go overseas countries*

Occupation	2005	2010	2015
Architecture	32.000	83.000	184.000
Business activities	61.000	162.000	348.000
Computer sciences	109.000	277.000	473.000
Law	14.000	35.000	75.000
Natural sciences	3.700	14.000	37.000
Management	37.000	118.000	288.000

Source: Hira Ron, "Recent Trends and Possible Implications", Testimony of P.E. Chair, Research and development Policy Committee The Institute of America to the Committee on Small Business United States House of Representatives on Global Outsourcing of Engineering Jobs, 18 June 2003.

As it can be understood from the figure business especially about the computer is expected to increase in foreign countries by outsourcing. By business operations the management business is expected to shift from USA to overseas countries. These kind of business operations has lower numeric values than the business about computers. But in the evaluation done until 2015 the number of these business going to the foreign countries is more rapidly increasing than the business about computers.

Because of the international outsourcing the developed countries has the loss of labour and income not only that requires knowledge and experience but also based on skill. Despite the risks the loss of labour and income, should developed countries continue the import of clothes and food stuff from the developing countries? The result of Global Trend Research that Globescan applied in 20 countries answers the question (Tamer, 2004); With an overview %50-55 of the European countries has a positive

perspective to the rising markets but on the other hand in USA the ratio of the people who say no to the rising market is %55. As for the developing countries the average is approximately %30-35 in the import of clothes and food stuff. Results can change in accordance with the level of affection of the countries from import and export of the food stuff and clothes.

Traditionally USA has become the leader country in technological inventions. But the application of the developments in information Technologies by outsourcing outside the USA decreased the opportunity of renovation in the field of software in the country (Hira, 2003) According to a calculation in 2004 every labour in ten in the software industry will shift to the developing markets (Power, Bonifazi, Desouza, 2004)

By outsourcing not only labour but also the wages for this labour goes to the foreign countries. In the following 15 years approximately 3.3 million of the 136 billion dollars wage may go to the foreign countries (Benkovic, Robert, 2004)

Although, bargain-basement labour rates constitutes a significant part of outsourcing cost, moving jobs overseas can be more expensive proposition than expected. In optimistic opinion, savings from outsourcing can not be more than 50 percent. substantial savings take years of effort and a huge up-front investment for many corporations. As just one example “United Technologies” known as a leader outsourcing practising company saves just over 20 percent by outsourcing to India.

Contrary to bargain basement labour rates, lower productivity and poor process can diminish potential savings from outsourcing activities. Thus, it would be regarded as a long-term investment with long term payback. Various factors affects the cost of outsourcing. The expense of selecting service providers yields the cost from 0.2 percent to 2 percent in addition to the annual cost of the deal. It comprises documenting requirements, evaluating the responses and negotiating a contract. The cost of transition which is the main burden of outsourcing. It takes a long-time period from three months to a full year to completely hand the work over to an offshore partner. During this training period, offshore employees work in paralel with similarly costly in-house employees on temporary visas. It is needed to build infrastructure in expected. Offshore providers demand much more money for employees than they paid them. As just one example, Indian companies charge US companies 20 US dollar an hour for an

employee they pay around 10 US dolar. The cost of layoffs result in unanticipated amount of money loss due to offshore contract in which severance and retention bonuses must be paid to laid-off in-house employees. In-house employees are required to keep there long enough to share their experience with their offshore replacements. Layoffs can also produce moral disorders resulting in disaffection and work slowdowns. It can take very long time to constitute consensus for moving work offshore and laying off some workers among in-house employees.

Language and other cultural factors affect the productivity for the offshore savings. In addition to this, offshore vendors often lack developer experience. Thus, process takes more time and money to complete. Deficiencies in productivity can rise average 20 percent cost to the offshore contract. Higher turnover at offshore vendor is another factor diminishing the productivity. In accordance with National Association of Software and Service Companies.

Attrition rates increased to 35 percent in India. In addition to paying for offshore vendors to learn firm's products. They can turnover the work. Turnover can average rise the expense as 1 percent to 2 percent. In order to diminish communication problems, intensive use of face-to-face interaction is needed. Language and other cultural differences increase the cost as 2 percent to 5 percent. The expense of managing an offshore contract and the actual relationship produces an additional cost which includes invoicing, auditing and insuring the work.

Outsourcing model is not made out of something, rather an experienced trend due to effect of globalization. The impact is worldwide with increased use of global trade and exchange of goods and services to maintain balanced resources for changing needs in competitive business world. As each product or process or model has its own life cycle to reach maturity and stand true to its advantage. There is always loss and gain on both the ends, outsourcee and outsourcer. If it is managed the system, communication, engagement, and relationship properly, outsourcees would see more benefits than losses. Driving the offshore engagement with clear understanding and co-ordination provides advantages in terms of cost, timeline and quality.

In USA thats mostly affected by the loss of the labour force, there are a lot of opinions about the issue:

In today's environment, managers are searching for any edge that can provide them with success. Outsourcing is one approach that can lead to greater competitiveness (Embleton, Wright, 1999) Outsourcing can bring significant benefits to regulated firms and their customers (McCormack, 2003)

According to Samuelson (2004) in American history most of the production business is done in other foreign countries by outsourcing and economic operation continues in this way. Also it is mentioned that most of the labour in the service sector by outsourcing will not harm to the USA economy. Gumpert (2004) says that half of the population of the USA in 1900 were working in agriculture and today this percentage is 5% and this shows that the people working in agriculture sector is employed in the new sectors new businesses. According to Palmer (2004) even if 3 million people go to a foreign country in the following 15 years, every year 200.000-300.000 labour will be created in USA. Samuelson supports the opinion that if we think that even 3.3 million people go to a foreign country in the following 15 years there will be 138 million labour in America So that makes this number unimportant. Furthermore every 100 dollars labour sent to foreign countries by USA firms will be back to USA as an investment worth of between 130-145dollars (Pastore,2004)

According to Paul Craig Roberts, one of the economists of Reagen the theory of David Ricardo shows that in the 19th century in England the import of private goods will make more profit by providing comparative advantages to the countries. In such a case producer has better technology, cheaper raw material, higher level of education or some other advantages. When all countries that came into together by free trade they will have a higher standart of living. According to Robert in the mentioned period the production factor was moving relatively hard. But today this movement can be obtained with the increasing rate. According to Robert in Cold War years this old trade theory lost its validity with the collapse of Russia and East Block Countries. The cheap labour force of East Europe suddenly was added to the labour force in the world. China and India that has millions of experienced labour force capacity gained some advantages. In many fields low cost of transportation in communication caused to do production by outsourcing in overseas countries and by having cost advantage to the firms to return America.

But Joan Williamson doesn't agree with Roberts about his thesis. USA economy creates more than 2 million labour every year. This is enough

to compensate the labour that are sent to India and other countries. According to classical arguments if a firm does some labour in another foreign country more profitably, the cost saving of this labour creates new labours in the host country. Furthermore almost all of the economists say that in America labour can be created and lost not only outsourcing but also some other reasons. The labour that is losing overseas countries can replace the other well paid labour in the USA (In Age of Outsourcing, 2004)

According to Supachai Panitckoakdi the director of the WTO the labour that needs high salary and skill is created by exportation. But every labour in USA is under the threat of importers. If we compare the importation in USA 10 years ago it was responsible for 7 million labour but today this number is 12 million. Lost labour by the international outsourcing can be compensated with new labour like finance and communication technologies. While there are some discussions about the shift of the labour in USA to the India and other countries, Europeans are complaining the shift of well paid labour to USA by outsourcing (Outsourcing and the World Trade Organisation, 2004).

RESULT

Most of the economists say unemployment caused by outsourcing but despite this outsourcing will be effective in the increase of welfare in the long term period. One group of economists say that the old trade theory is no more in use.

With the loss of labour in USA because of outsourcing, some different ideas about the issue came into the agenda.

-Outsourcing must be prohibited. Because it causes the losses of labour force and the closure of factories

-Sending labour to the overseas countries and the competition for the lowest income among the employees is a result of NAFTA and WTO. Because these organisations make it impossible to put taxes and tariffs on the labour of outsourcing. In the study conducted in the countries that employees don't belong to any union and the environmental conditions aren't enough it is said that the regulations of NAFTA and WTO and the free trade areas of

USA should be cancelled and these should be replaced by trade policies that have bilateral trade agreements (which provides employees more livable wage and environmental conditions)The cancellation of NAFTA and WTO will prevent the high technology labour outsourcing. But USA administration have adopted outsourcing today and have seen it as a new international trade method.

According to the supporters of the outsourcing, the loss of labour is temporary. Lost will bring new labour in the future. And this will improve the level of labour force in USA economy.

In EU countries the production by outsourcing in low cost places put forward the idea of in order to provide long term growth, we should focus on research, development and infrastructure activities. In getting the suitable industrial strategies for EU the idea of choosing sectors the high technology plays a key role. Because of this in the sectors that has cost advantage it is said that developing countries can be benefited by outsourcing. The idea of EU in industrial production that requires high technology, qualified labour force should try to be successful is common.

It has also been criticised by the developed countries that developing countries produce mostly disregarding the standards like and environment. Developed countries criticise that the production that is not in accordance with these standards decreases the costs and this causes unfair competition. They support that especially not complying with labour force and environment standards, increases the production by outsourcing in developing countries.

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