

Lecture 6b:

Offshoring – part 2

Thibault FALLY

C181 – International Trade

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4- Evidence on Offshoring

- Offshoring is controversial and is often the topic of intense political debate.
 - Most economists tend to be in favor of offshoring
 - Evidence on the effect of Offshoring?
- + Discussion on other effects of offshoring,
e.g. transmission of shocks

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Offshoring and multinational activity

- “Offshoring” often associated with multinational activity but not necessarily
 - Multinational firms involve suppliers that are affiliated
 - One can also have outsourcing offshoring (offshoring with an unaffiliated supplier)
- Note: “Outsourcing” is not a synonym of “Offshoring”!
 - **“Outsourcing”**: involve an independent supplier.
 - **“Offshoring”**: involves a supplier abroad. One can have outsource within the US, and offshoring without outsourcing.

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Evidence on the US

The fear that offshoring and multinational activity threatens jobs in the United States is overstated:

- Expansion abroad by U.S. multinationals tends to support jobs based in the U.S.
- More investment and employment abroad are strongly associated with more investment and employment in American parent companies.
- Expanding abroad also allows firms to refine their scope of activities.

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Evidence on the US

Amiti and Wei (2014):

- Service offshoring increases labor productivity of US firms by 10%
- Offshoring of manufacturing inputs increases labor productivity of US firms by 5%

If you want to learn more: check articles and videos from Matt Slaughter

- FDI and offshoring
- China and patent protection
- Skill gap

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Evidence on **Denmark**: Workers

- Why Denmark? Allow us to track workers more precisely
- Recent study (Hummels et al 2013):
 - **Coverage:**
 - Entire population of firms
 - Entire population of workers
 - Links & tracks workers and firms: 99% match
 - **Info:**
 - Trade, wages, education, occupation, sex, etc.
 - Work status of entire population once a year
 - Detailed data on export and imports by firm

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Characteristics of Trading Firms

Variable	Effect of an increase in offshoring opportunities	Effect of an increase in Exports opportunities
Log(employment)	-0.196	0.346
Log(gross output)	0.151	0.486
Log(capital per worker)	0.099	0.282
Log(annual results)	0.012	0.831
Log(wage bill per worker)	0.127	0.119
Share of high-skilled workers	0.048	0.066
Share of low-skilled workers	-0.048	-0.066

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Summary of study on Denmark

Offshoring induces:

- Decreases in employment
- Increases in output
- Increases in profitability
- Increases in relative employment of skilled workers

Effect on wages:

- Doubling offshoring leads to an 3-8% rise in skilled labor wage,
- 2-5% fall in unskilled labor wage

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Other remarks and discussion topics:

- US as an offshoring destination
- Transmission of shocks

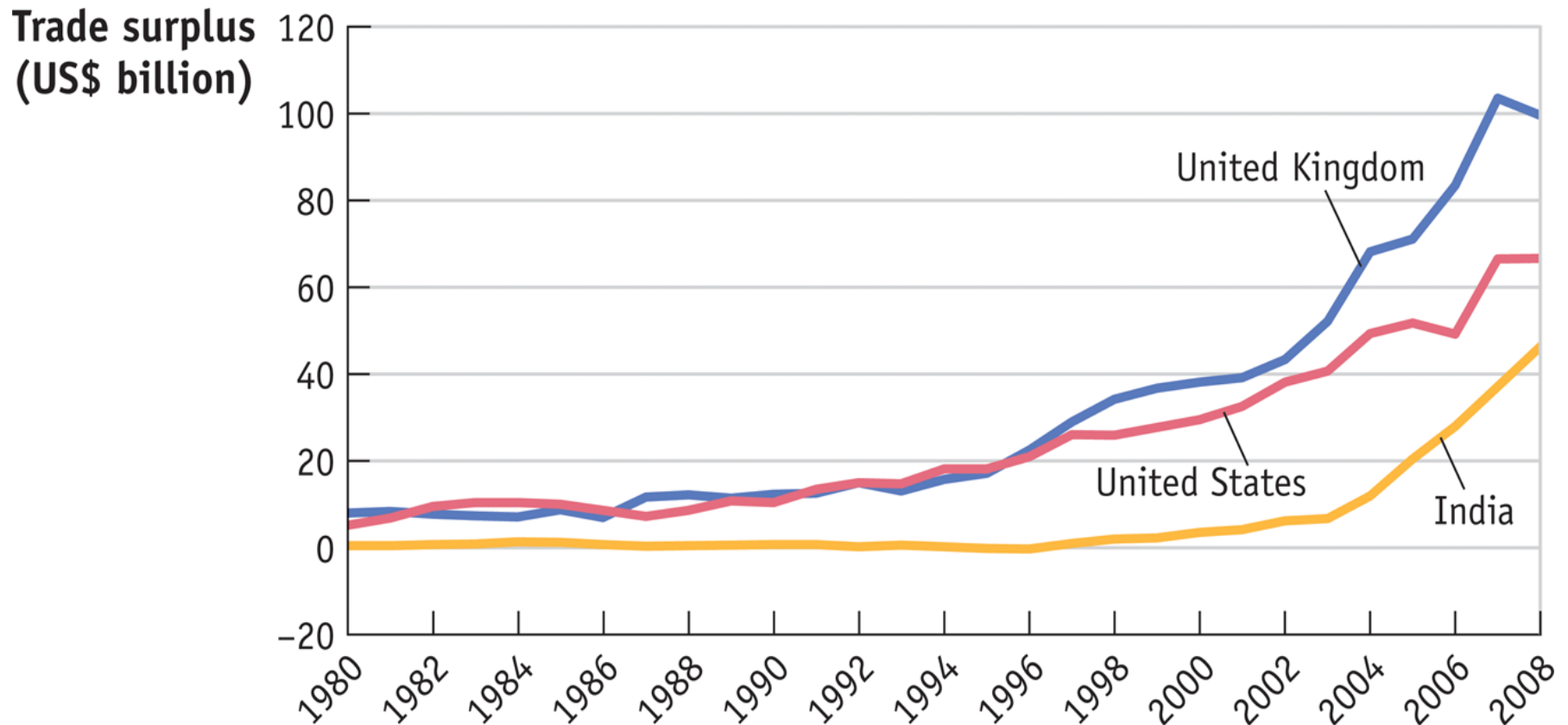
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Conversely: The US is a provider of offshoring activities

- In manufacturing but especially in service industries
- **Traditionally:** offshoring is about trade in components
- **Today:** offshoring of services increasingly important.

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Trade Surplus in Business Services



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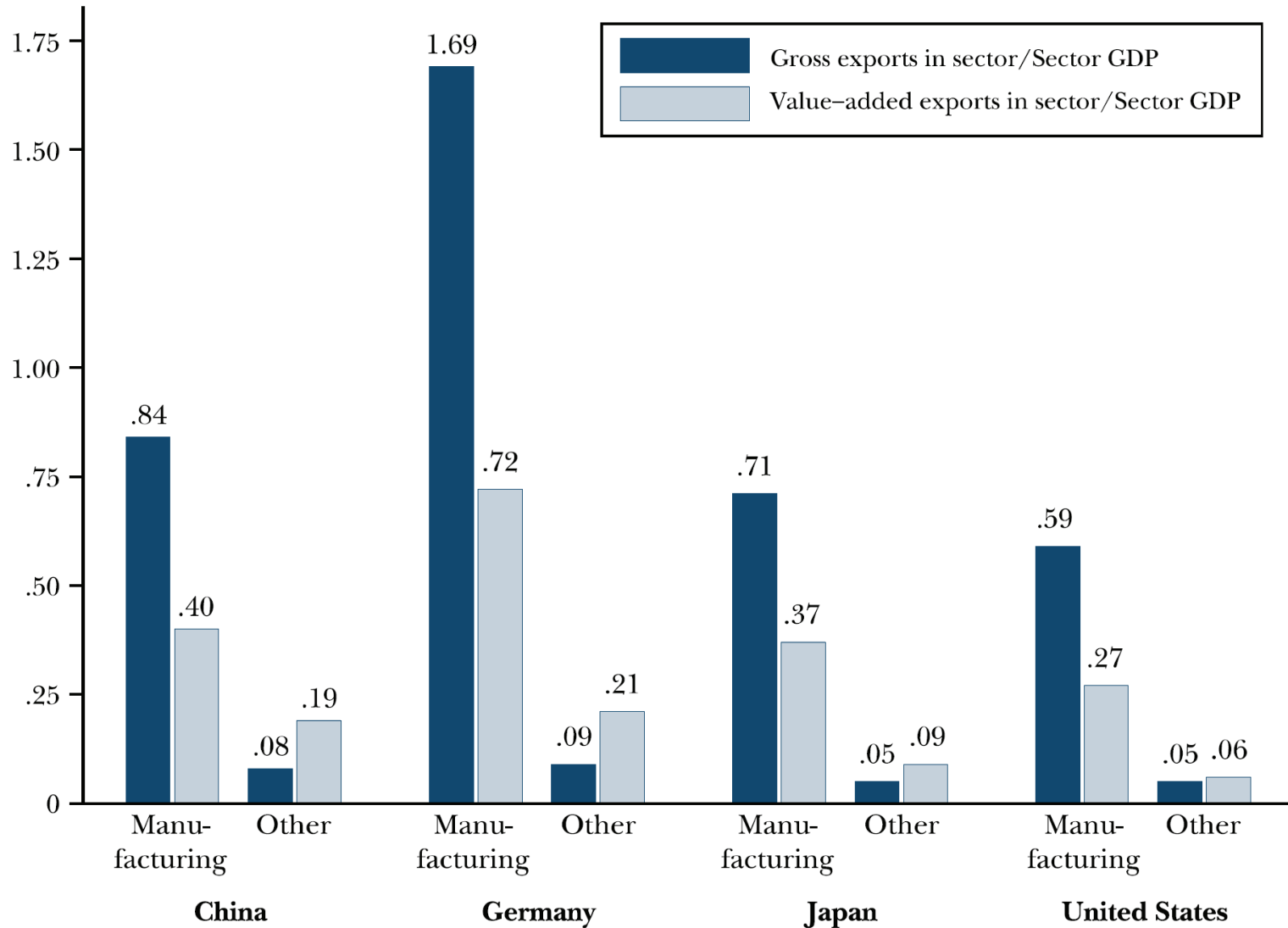
Global transmission of shocks through production chains

Examples:

- 2011 Earthquake/Tsunami in Japan
 - Affected car component supplies
 - Ipad2 components
- 2012 Floods in Thailand
 - Hard drive producers
- And other events such as: Supplier bankruptcy, etc.

Low VA/Export: shocks transmit through production chains

B: Sector Exports/Sector GDP



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“Mars One” Project:

Key challenge: supplying damaged parts and components!! (extreme trade costs bw Mars and Earth)

Same applies to SpaceX



Conclusion

This chapter on Offshoring:

- Definitions and examples
- Offshored tasks likely to be the least skill-intensive
- Offshoring can explain increase in wage inequality in both source and destination countries
- Benefits skilled workers, ambiguous for unskilled workers
 - Debate on the effect of offshoring but generally not as bad as people think
- Other implications: volatility of supply, processing zones, etc.