

Selling Services Across Frontiers

Economic development in all countries has involved shifting the focus from agriculture or manufacturing to the service sector. The same is true at the international level – as technological advance and falling transport costs have made it easier to trade services across national borders. The Asia-Pacific region has been at the forefront of these changes – particularly through labour migration, outsourcing and the tourist industry. But policy makers will need to take firm action if the international trade in services is to offer more benefits to the poor.

Asian countries continue to rely on the international trade in goods. But over the last three decades they have been taking advantage of the opportunities to boost the trade in services, and as a result international trade has become much more complex and diverse. This chapter focuses on three forms of cross-border movement: in the first type, the seller moves, as in international labour migration; in the second type, the work moves, as with business outsourcing; and in the third type, the buyer moves, as with international tourism.^{1,2}

All three types of movement have increased significantly. For migration, millions of lower-skilled workers continue to travel abroad on short-term contracts, especially from Bangladesh, Cambodia, China, Nepal, the Philippines, and Sri Lanka. An estimated 10 per cent of the Filipino labour force and 12 per cent of the Sri Lankan labour force now work overseas. Labour migrants have improved their quality of life, and even some of the poorest have earned enough to lift their families out of poverty.

Asia has also been a pioneer in the offshoring of IT and business process services. In some cases IT workers continue to travel overseas on short-term assignments in developed countries, but advances in information and communications technology and falling Internet

connectivity costs have allowed more and more of these services to be delivered remotely – providing jobs for highly educated young people, who might otherwise have struggled to find work that took advantage of their skills.

In tourism too, the Asia-Pacific region is one of the global leaders – increasing its share of global traffic from less than 10 per cent in the 1950s to 40 per cent in 2004. Tourism can offer new sources of employment even to the remotest regions.

There are, of course, many other services that are traded across borders, including health services, financial services and environmental services. In the sections that follow, this chapter looks specifically at three of the main forms of economic service.

Short-term Migration

Asia has long been subject to large migration flows – both within and beyond the region. In the nineteenth century, for example, millions of indentured workers left countries in South Asia and China – some to other parts of Asia, others to North America, the Caribbean and Africa. In the twentieth century, many people left the region for long-term settlement in Europe and North America.

Nowadays migration flows are often more

Asia has long been subject to large migration flows

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complex, but migrants typically fall into one of three groups. The first group consists of more educated and skilled professional workers, who are heading primarily for the developed countries – chiefly the US, Western Europe, Australia or New Zealand. The second group consists of unskilled or lower-skilled workers, who have gone to a greater number of countries, either outside the region – to the Gulf States, for example – or to the faster-growing Asian countries. The third, though much smaller group, consists of business and professional people, who are being transferred within transnational corporations. The overall patterns of movement of unskilled labour are indicated in Box 5.1.

Migration can be considered as a response to international imbalances – as workers move from countries with labour surpluses to those with labour deficits. In practice, however, the destination countries tend to control the flow as they seek to fill gaps in their labour markets – either at the top, for highly educated professionals such as teachers or doctors, or at the bottom, for unskilled workers in plantations or construction sites.

Within the region, the most significant destination countries have included Japan, Singapore and the Republic of Korea, but from the early 1980s to the mid-1990s, economic booms also created labour shortages in Malaysia and Thailand and attracted workers from neighbouring countries. Outside the region, the

most significant destination countries have been the oil-exporting countries of West Asia and the Persian Gulf – which have not only drawn in unskilled and semi-skilled workers for construction and other services, but also attracted large numbers of professionals, especially those working in engineering, accountancy and the health sector. While West Asia remains the most significant for short-term overseas work, the US and Europe have and remain important for migration in general. More recently, there has been an increase in short-term movement of software professionals to the US.

Every country in the region has supplied migrants, but the largest single source has been the Philippines. Filipino workers of varying skill levels have travelled all over the world, though have tended to cluster in specific destinations: domestic helpers, for example, are concentrated in Hong Kong (China) and Saudi Arabia, entertainers in Japan and other South-East Asian countries, and IT professionals and nurses in the US and the UK.

Benefits of Short-term Migration

Migration brings many advantages – economic and social – both for individual migrants and for the countries they leave behind.

Remittances. For the source countries, one of the most direct benefits is the flow of remittances, as migrants send or bring their earnings home. In the 1980s and 1990s most of the source countries, particularly India and the Philippines, enjoyed a steep rise in remittance income (Figure 5.1).

For many countries, remittances represent a significant source of foreign exchange. In Viet Nam, for example, between 1999 and 2002 remittance inflows rose from \$1 billion to \$1.5 billion. They now account for around 10 per cent of export revenues and are roughly equivalent to the annual flows of overseas

BOX 5.1

MOVEMENTS OF UNSKILLED LABOUR IN THE ASIA-PACIFIC REGION

Source countries	Bangladesh, Cambodia, China, Indonesia, Lao PDR, Myanmar, Nepal, Philippines, Sri Lanka, Viet Nam
Destination countries	Brunei Darussalam, Hong Kong (China), Japan, Republic of Korea, Singapore, Taiwan (China)
Both source and destination countries	India, Malaysia, Pakistan, Thailand

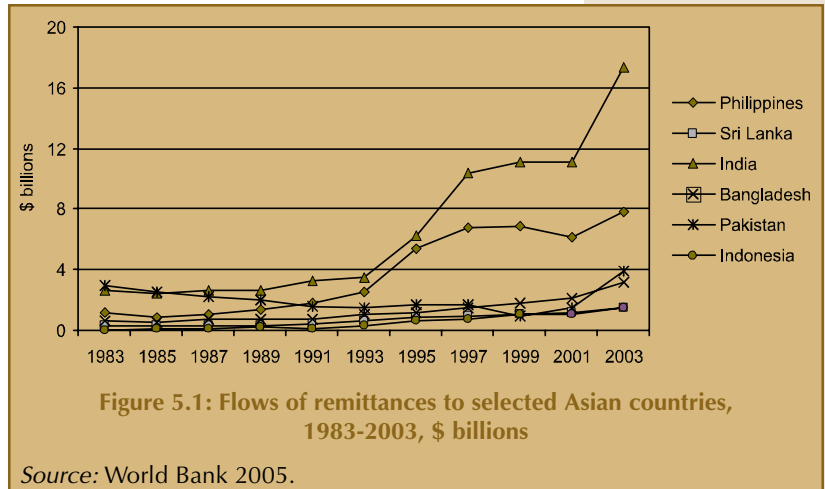
Note: The classification here refers only to the larger flows of lower-skilled workers. It does not include seasonal cross-border shifts of neighbouring populations, often part of a centuries-old pattern in these economies
Source: Based on Wickramasekara 2002.

development assistance or foreign direct investment.³ Even for the larger countries, like India, remittances over the 1990s exceeded all forms of capital inflow. As well as being on a large scale, remittances have the further advantage of being more reliable than other flows: often they come from migrants working in the service sector, which is less susceptible to the fluctuations of business cycles in host countries.

Individual migrants and their families use this income for many different purposes. Some will spend it on immediate needs: food, for example, or education or health care. Others will buy houses or invest in businesses (Box 5.2). For many communities, migration has served as a route out of poverty. Remittances are also used for community activities as migrants build up transnational networks and provide funds that benefit their home villages or regions. For example, migrants from the Indian state of Gujarat who have become shopkeepers, hotel owners and businesspeople in the UK and East Africa have helped develop infrastructure as well as the health and education systems in their home state. Similarly, workers from the state of Kerala helped finance the construction of an international airport to facilitate travel between their home and work countries.⁴

Generally, the largest flows of remittances come from short-term economic migrants. By contrast, long-term migrants are less likely to send money home. Professional workers who settle in developed countries usually want to retain more of their earnings. And when they do send money back, this is typically for investment on which they are seeking a return.

Experience and Skills. Migrants bring home more not only money but also valuable work experience, enhanced skills and useful networks that can promote economic activity, innovation and entrepreneurship. Equipped with these, the migrants themselves can make better use of their remittances.



This skill transfer is particularly important for the professionals, especially in the emerging IT-related industries. In the process of outsourcing, for example, service companies will send key consultants and specialists to customers to acquire knowledge and to transfer back to the companies in Asia information about technical applications, products, processes, and marketing techniques. Similarly in the field of health, returnee doctors and specialists have been able to transfer knowledge about cutting-edge techniques – raising standards of health care and generally improving health service delivery.

Empowerment of Women. Migration also has important social effects, particularly in the empowerment of women. Over recent decades,

BOX 5.2

USE OF REMITTANCES IN BANGLADESH

A survey in Bangladesh found that expatriate workers spent around 30 per cent of their income on personal consumption abroad, sent 45 per cent back home and saved the remaining 25 per cent. Of the amount sent home, 50 per cent was used for consumption, including spending on food, education and health care, 29 per cent was invested in land or other property, and 21 per cent was used for housing improvements, including upgrading existing property.

The same survey also found that a relatively prolonged, stable flow of remittances allowed families to move from wage employment to self-employment and to move from cultivation to a range of non-farm activities.

Source: IOM-UNDP 2002; Raihan 2004.

Migrants can find themselves working in very difficult circumstances and their departure can also create problems in the country they leave behind

Asian women migrants have come predominantly from three countries: Indonesia, the Philippines and Sri Lanka, where they make up 60 to 80 per cent of all legal migrants (Figure 5.2). Some of the least developed countries, such as Bangladesh, also have a smaller, but still significant, proportion of women migrants.

Most of these women are employed in health care and domestic service. The Philippines, for example, is the world's largest source of nurses. During the 1980s there was a huge outflow of Filipino nurses to the US. Subsequently, between 1995 and 2001 an average of

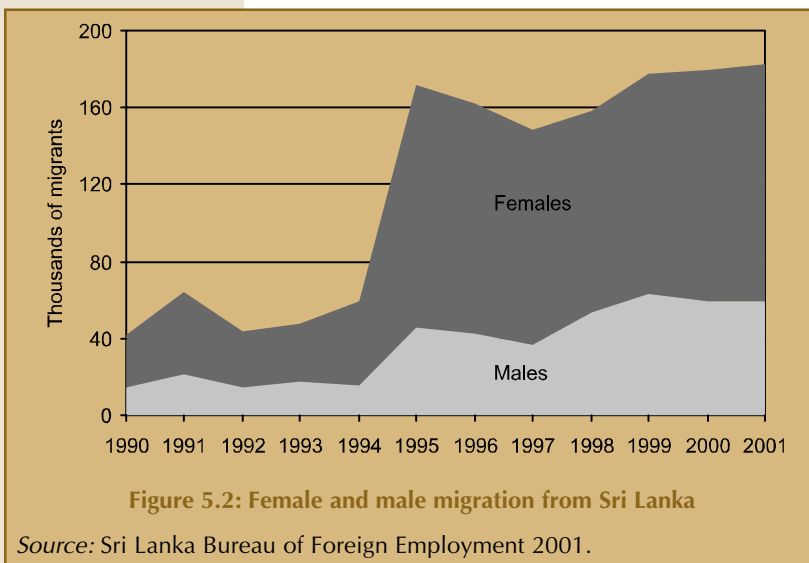
5,700 nurses migrated annually, primarily to the UK and Saudi Arabia.⁵ Women from Indonesia and Sri Lanka are primarily travelling for domestic service, mainly to Saudi Arabia, Kuwait and the United Arab Emirates.

Disadvantages of Short-term Migration

For all its benefits to migrant-sending communities, migration also has some negative aspects. Migrants can find themselves working in very difficult circumstances, and their departure can also create problems in the country they leave behind.

Working Conditions. Compared with local residents, migrants are more vulnerable to exploitation. Low-skilled temporary migrants in particular are often unaware of their rights and have few forms of protection – especially when employers confiscate their passports (Box 5.3). Even professional workers can face discrimination – receiving lower wages and fewer benefits that comparably qualified national personnel. They may also find that the host country does not recognize their qualifications and requires them to pass new exams; architects might have to work as draughtsmen, engineers as technical staff, nurses as nursing aides, or dentists as dental assistants.

Social Effects on Families. For families, migration is financially beneficial but socially disruptive. Prolonged separation can lead to illicit relationships, and lonely spouses left at home may resort to alcohol or gambling. Consequently, migrant families often have higher divorce rates. Migration also tends to delay marriage, and migrant women in particular may have difficulties finding spouses when they return. Children too can suffer due to the absence of parents, especially their mothers, and face psychological and behavioural problems or difficulties at school.



BOX 5.3

DISCRIMINATORY WORK VISAS

Depending on the nature of work, poorer migrants, usually from South Asian countries and the Philippines, have occasionally been subject to exploitation in destination countries. This is especially the case when receiving countries have different visas for different categories of labour. Some West Asian countries, for example, issue two types of visas to temporary migrant workers. The 'Type B' visa is issued to migrant workers hired by companies in the formal sector of the economy. These workers are protected by labour laws, have greater rights and are permitted to live outside the work premises. The 'Type A' visa, however, permits the employer to confiscate the passport of the migrant worker, to confine her or him to the house and to dictate work conditions and hours. Housemaids, for example, qualify only for Type A visas, which makes them dependent upon their employers for their minimum rights, and many have complained about excessively long workdays, loneliness and ill health, difficulties in communicating with their family, and sexual harassment.

For families, migration is financially beneficial but socially disruptive

Increasing Inequalities. Migration can dramatically boost the income of a small number of families – making them richer than their neighbours and generally giving rise to skewed patterns of income and consumption. In the Philippines, for example, remittance inflows have been found to increase local income inequalities.⁶

Reintegration. Returnee migrants can also face social and economic problems when they come home. In Sri Lanka, for example, both male and female migrants generally reintegrate fairly smoothly. However, because of their low level of education, some people may not find the kind of work that they aspire to: those who have worked overseas as housemaids, for example, may be unwilling to do such work in Sri Lanka, where it has a low social status. And their work experience in more developed countries can give them unrealistic salary expectations.

Brain Drain. The destination country may gain the skill of migrants, but for the source countries this can represent a significant loss. In the Philippines, for example, where more than one-third of migrants are professional or technical workers, their departure has led to serious staff shortages in the health sector and to driving up of wages. Between 1995 and 2000, the number of registered nurses in the country fell from 27,272 to 5,874. Many doctors have also migrated, particularly to the US and Canada.

Migration and Meeting the MDGs

Migration can thus have positive and negative effects. These can also be considered in relation to the MDGs.

MDG1: Poverty. Higher incomes from remittances cannot only help reduce poverty and hunger, but also accentuate existing inequalities

and perpetuate poverty among unskilled and powerless migrants.

MDG2: Education. Migration can help parents pay for education, but if it splits up families, it may also serve to remove children from school.

MDG3: Gender Equality. Women may be empowered if they get independent incomes, but can also be vulnerable to exploitation.

MDG4: Child Mortality. Higher incomes and more knowledge about health should make children healthier, but some may lose out if they too have to migrate to more difficult environments.

MDG5: Maternal Health. Women working overseas can have more opportunities to be better informed, which could lead to health-seeking behaviour. However, they could face restrictions on their movements and other forms of exploitation, which inhibit this health seeking behaviour.

MDG6: Combating HIV/AIDS and Other Diseases. Remittance incomes can be spent on controlling infectious disease, but migration itself can help spread HIV/AIDS infection.

MDG7: Environmental sustainability. Migration from highly populous countries can relieve pressures on land and other resources. However, the migrants can live in overcrowded, unsanitary conditions that can worsen environmental conditions in the host country.

MDG8: Global Partnerships. Migration may result in a better understanding among cultures and societies, leading to greater possibilities of creating a global partnership for development. But unregulated migration can also result in a backlash against migrants among local populations.

From the perspective of the MDGs, and of human development generally, it is clear that migration is intrinsically neither beneficial nor detrimental (Box 5.4). Much depends on the circumstances. What can policy makers do to promote the positive aspects and minimize the negative ones?

Source Country Measures

Though many aspects of migration appear to be under the control of the destination countries, in fact, there is also a great deal that the source

countries can do to make migration a more productive and fulfilling experience, especially for unskilled and semi-skilled workers and for women. Viet Nam, for example, has shown how effective such measures can be (Box 5.5). Governments in source countries should therefore develop national strategies for migration. These could include:

Increasing Access to Information. Most migrants get information on migration opportunities from networks of migrants and former migrants. This tends to concentrate the

BOX 5.4		
HUMAN DEVELOPMENT OUTCOMES OF MIGRATION		
Channel of Impact	Nature of impact	Human development outcomes
<i>Positive Impacts</i>		
Employment and income generation	Provides employment to unemployed or underemployed. Incomes are generally higher than those in the source economy and help alleviate poverty for families of migrants.	Empowerment, equity, productivity
Impact on women	Provides employment to a large number of women who have limited access to employment in their home country. This can lead to an increase in family expenditure on health and education and relatively higher rates of savings.	Empowerment, equity, productivity
Skill and knowledge transfer	Migrants gain wider social and professional exposure and greater access to technology and skill development. In the IT and health professions, for example, returnees can then contribute to professional and technical skills in their home countries.	Productivity, empowerment, sustainability
Resource generation	Remittances and savings often form the main sources of foreign exchange – and add to the stock of capital for investment housing, small businesses and other infrastructure. Migrants who spend remittances at home then have a ripple effect on demand and income among local populations and help boost fiscal resources.	Sustainability, productivity, inempowerment, equity
Externalities and spillover effects	Migrants gain broader social and cultural outlooks by living in other societies and can create useful transnational networks.	Empowerment productivity, equity, sustainability
<i>Negative Impacts</i>		
Employment and income	Remittances increase disparities between households and between regions.	Equity concerns
Skills and knowledge	Source countries can lose skills of professionals, such as medical personnel. These professional skills may also be underused overseas if qualifications are not recognized.	Productivity, sustainability concerns
Externalities and spillover effects	Social costs on families, especially children. Social costs on migrants – loneliness, lack of communication with families. Possibility of exploitative work conditions in receiving countries. Reintegration issues, economically and socially.	Concerns about equity, sustainability, long-term productivity

benefits of migration in particular regions or even villages. Governments can create a more level playing field by making relevant information on markets and employment opportunities available throughout the country and across all income categories and social groups.

Recruitment Agencies. Many migrant workers fall victim to unscrupulous recruitment agencies that can charge exorbitant fees or fail to deliver the promised employment. Governments need, therefore, to regulate and monitor recruitment agencies and close down illegal ones. Conversely, they can reward effective agencies – by recognizing their role and treating them as partners in the social development process.

Skills Training and Resources. Workers will be in a much stronger position to take advantage of migration opportunities if they have certified skills. In addition to creating more training institutions, governments should therefore ensure that these and other government agencies and higher educational institutions obtain national, regional and international accreditation. This will provide potential employers with a measure of quality assurance – especially for skilled and semi-skilled labour.

Finance. Migrants have to pay considerable up-front expenses – for recruitment, for example, and for travel. Those from poor communities that have no access to formal institutions often borrow funds from relatives or through other informal channels. In Viet Nam and Bangladesh, surveys have also found that migrants mainly finance their trips by selling family assets. National strategies for migration should therefore include the provision of cheap loans from banks and other institutions.

Cultural Adaptation. Poorer emigrants will often find themselves very isolated in a new environment. To ease the adaptation process,

BOX 5.5

GOVERNMENT PROMOTION OF TEMPORARY MIGRATION FROM VIET NAM

In the 1980s, Viet Nam faced an international blockade and had little interaction with other economies. The Government officially guaranteed jobs to most Vietnamese but their incomes and living standards were very low and there was widespread poverty and even starvation. To help alleviate the problems the Government carefully managed migration abroad under strict regulation.

Recognized recruitment agencies, subject to government regulation, were given the autonomy to explore new markets for short-term workers, develop contacts with foreign partners and directly enter into labour contracts with migrant workers. These agencies were encouraged to enter into new forms of cooperation, such as sub-contracting, turnkey contracts for construction projects and joint ventures with foreign partners. The Government also encouraged migrants by allowing them flexibility on using their income. Migration increased steadily in the 1990s, and the country now sends around 40,000 workers abroad each year (DAFEL 2003).

In Dong Thap province for example, a combination of incentives was provided to encourage and equip locals to work abroad. The Government provided loans for travel through a combined financing programme – 80 per cent from the central government and 20 per cent from the local government through local public sector banks. A local agency, the Centre for Job Services, provided vocational training and conducted language classes to enable people to apply for work in Malaysia, Taiwan (China) and Japan. With the help from local officials, potential migrants could also apply for passports from home instead of having to travel to Ho Chi Minh City. These incentives helped to triple migration from the province in 2002.

Source: Huy et al. 2003.

governments in the source countries can provide language immersion classes and educational programmes that introduce migrants to the cultural nuances of the destination country.

Rights Awareness. Migrants will be in a stronger position to protect themselves from exploitation if they are more aware of their rights and know how to protect themselves from discrimination and abuse. Governments could, therefore, organize premigration seminars to provide the necessary information – collaborating in some cases with NGOs, which can help train workers and offer advice and support through counselling centres.

Support from Embassies. Migrants should also be able to rely on protection from their embassies. Governments should therefore

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strengthen embassies in countries that employ significant numbers of their migrant workers, by offering the necessary support through the posting of labour officers experienced in handling worker welfare and legal issues.

Channelling Remittances. So far, governments in the source countries have done relatively little to channel foreign exchange remittances into specific development projects – such as building local infrastructure or improving health and education services. Governments could therefore encourage the financial sector to develop the appropriate instruments and financial products.

Return Migration. Few Asian source countries offer any support to returnees to help them deal with the social, economic and psychological effects of return, sometimes after a relatively long period abroad into what could be very changed societies. Government agencies could do more to counsel returnees and help them settle. For migrants who have returned with significant funds, the government can provide seminars on entrepreneurship and other self-employment opportunities. For migrants with more limited resources, the government can provide soft loans and offer skills training programmes to help them establish small businesses.

Destination Country Measures

The destination countries have security and other concerns about immigration. They therefore control the arrival of different types of migrants and limit their rights. Recently, they have been increasing these protectionist measures – restricting the number of arrivals, introducing administrative and procedural delays in processing visa applications and work permits, and making renewals and extensions more difficult and expensive. They have also been less willing to recognize the qualifications and experience of such workers. In the IT sector,

for example, there are no formal accreditation procedures, and the outcome can often be opaque and discretionary.

One particular area of concern is the application of an ‘economic needs test’ for the arrival of certain professionals. Some governments oblige employers who propose employing a migrant to demonstrate that they have failed to recruit a comparable national worker. However, in many cases it would be more efficient simply to designate certain clearly identifiable categories of professionals – all of whom would be entitled to enter and seek work.

Migration could also proceed more efficiently if recipient and source countries arrive at mutual recognition agreements (MRAs). They might start, for example, with less contentious areas like the accreditation of higher educational institutions – establishing equivalences in education levels, degrees, and the quality of graduates. Subsequently, they could move on to the recognition of licenses, professional certificates and experience. The private sector, particularly professional associations, can help here.

MRAs can be negotiated at a multilateral level, but this process is often difficult, lengthy and tedious, and therefore bilateral or regional agreements might be more feasible for specific professions and occupations. ASEAN, for example, has lifted visa requirements for its member countries to increase movement of citizens, a precedent that could be extended across the region.

Destination country governments could also reduce the number of temporary migration visa over-stayers by working more closely with employers. Under such schemes, the sponsoring employers cooperate with governments monitoring of their employees and also take responsibility for workers’ return travel – and face the possibility of sanctions if found in breach of the requirements. Evidence suggests that the most sustainable temporary migration programmes are those that are appropriately regulated and

enforced. Bilateral or regional agreements can play an important role in this.

Multilateral Action

For migration, the most important trade agreement, which operates under the aegis of the WTO, is the 1995 General Agreement on Trade in Services (GATS). This was designed to allow developing countries to obtain more liberal access for temporary migrants, and make such migration more secure and sustainable. In practice, however, it does not offer much by way of liberalization and seems to have had little effect on migration patterns in Asia and the Pacific.

One problem is that it is quite narrow. As

might be expected, GATS does not cover migrants working outside the service industries and tends not to cover foreign domestic service workers, although this issue is still a matter of controversy. And since it favours relatively higher-income and highly skilled people, it could even be seen to aggravate inequalities both among and within countries. Moreover, since GATS is not a migration agreement but a trade agreement, it is silent on issues such as the treatment of persons working abroad and on forced migration and trafficking.

Source countries could nevertheless use the GATS framework to promote desirable short-term economic migration. There are a number of ways in which this can be done – as outlined in Box 5.6.

Migration could also proceed more efficiently if recipient and source countries arrive at mutual recognition agreements

BOX 5.6

MIGRATION OPTIONS IN THE GENERAL AGREEMENT ON TRADE IN SERVICES

For migration, the most important trade agreement, which operates under the tutelage of the WTO, is the 1995 General Agreement on Trade in Services (GATS). This defines four ‘modes’ of service supply. Mode 1 refers to cross-border services that might be carried out, for example, across the Internet. Mode 2 refers to consumption abroad, such as tourism. Mode 3 refers to foreign direct investment, when a service company like a bank opens a branch in another country. Mode 4, however, is the only one that covers migration of what it terms ‘natural persons’ – which include intra-company transfers.

There are a number of ways in which source countries could use the GATS framework to promote desirable short-term economic migration.

De-linking Mode 4 from Mode 3. Under GATS, short-term migration is closely linked to foreign direct investment – facilitating the movement of intra-corporate transferees. While this is of benefit to developed countries that are the source of most such investment, it offers much less to developing countries that would like to see greater movement of individual professionals and service providers independent of corporate presence.

Expanding the Classification List. The WTO classification of professionals is insufficiently detailed and different countries interpret it in different ways. Instead, it should break these down further to identify workers more clearly – possibly by adopting the International Standards Classification of Occupations. This should provide a list of individual professions that is independent of professional firms or sectors and thus would be more meaningful to developing countries.

Delinking Immigration and Employment Policies. Developed countries are reluctant to make more binding commitments on Mode 4, fearing that this would give them less flexibility on immigration legislation and procedures. There should therefore be a mechanism to de-link a legitimate immigration policy from restrictions on migration for temporary employment. Governments should also relax or remove various market access barriers to Mode 4 movement, such as quotas and quantitative restrictions, wage conditions and administrative procedures.

Adopting the GATS Visa. One proposal, from India, is to have a ‘GATS visa’ that would be issued to individuals or professionals who have been invited or recruited to perform temporary services in another country. It would thus be timebound, employment-specific, and temporary; moreover, it could not be converted to another type of visa or used to seek permanent employment or residence. This would separate labour migration from the often cumbersome immigration procedures needed to obtain temporary entry.

Strengthening the Emergency and Safeguard Clauses. A commitment under GATS is a permanent obligation. So even when destination countries accept the need for more migrants, they may be nervous about making permanent commitments. However, these concerns can be addressed if GATS rules instead allowed countries to invoke emergency safeguard measures – or permitted a timebound commitment. Countries could still apply economic needs tests, though in a less arbitrary manner.

Outsourcing typically involves shifting functions from higher-wage to lower-wage economies in efforts to increase efficiency and lower costs

Outsourcing Business Processes

Nowadays many more companies are passing some of their non-core operations to third-party service providers. Such outsourcing of business processes occurs both within a country and outside. Cross-border outsourcing, or offshoring, is a new form of trade in services that is enabled by information and communications technologies. Typically, companies use this form of 'global outsourcing' for business processes and back-office functions. This takes advantage of technological advances and falling costs in information and communications technology that now permit delivery over the telephone and the Internet of a wide variety of services at all levels of skill and complexity.⁷

The current scale of outsourcing is difficult to assess, but OECD estimates that in 2001, IT and business process services outsourcing was worth around \$260 billion.⁸ Undoubtedly, the

phenomenon is growing rapidly (Box 5.7). One estimate suggested that between 2002 and 2006 business process outsourcing (BPO) alone would have risen from \$570 billion to \$1,200 billion.⁹

Outsourcing typically involves shifting functions from higher-wage to lower-wage economies in efforts to increase efficiency and lower costs, enabling the company to concentrate more on its core operations. Thus, companies in the US and Europe started to outsource to countries such as India, China, Israel, Malaysia, Mexico, the Philippines, South Africa and Viet Nam. Initially, the work they sent was primarily concerned with data entry and the maintenance, delivery and management of IT functions. Since then the range and complexity of services has expanded rapidly – and blurs the boundaries between sectors and activities. Services are now provided all along the value chain, from data entry to highly skilled tasks such as 3D modelling (Box 5.8).

BOX 5.7

OUTSOURCING BUSINESS PROCESSES – IMPLICATIONS FOR WIDENING EMPLOYMENT

A special contribution from Narayana Murthy, Chairman of one of India's largest outsourcing companies, Infosys.

The global business process outsourcing (BPO) industry today performs services that range from human resources, research and financial activities, to design and engineering functions. Worldwide, BPO revenues were expected to touch \$133.7 billion in 2005, an 8 per cent growth from \$123.8 billion in 2004.

The BPO industry in Asia is estimated to grow by over 13.8 per cent annually through 2008, and job creation is expected to accelerate, resulting in up to 6 million new jobs by 2015. Asia's outsourcing advantage stems from its growing pool of highly skilled, low-cost workers – in India, around 3,000 educational institutions train more than 200,000 software professionals and an equal number of non-engineering English-speaking graduates every year. China trains an estimated 400,000 graduates a year. At the same time, aging populations and falling fertility rates in Western Europe and the US mean emerging labour shortages in developed countries. It is estimated that at present productivity levels, the US alone will need 15.6 million more workers by 2015 to maintain current living standards.

India accounts for over 40 per cent of the global BPO market; from 2000 to 2004, the country saw an estimated 260,000 jobs created within the sector. The industry has also seen competing,

low-cost destinations emerge across Asia – the Philippines, China, Malaysia, Thailand, and Viet Nam. However, to take advantage of the opportunities from outsourcing, countries must remove existing impediments to growth.

The outsourcing industry is driven as much by the availability of skilled labour as by lower costs. Consequently, Asia's long-term success as an offshore destination will depend on how best countries can leverage their intellectual capital. In India today, an estimated 40 per cent of children drop out of school by the age of ten; across Asia, 46 million children are out of school. Clearly, countries must expand the reach of elementary education; academic institutions must focus on modernizing curriculum and aligning higher education with the needs of the industry. In addition, we must establish innovation systems of industry, science and research centres, and universities, to create new knowledge and technology.

China's reformist leader Deng Xiaoping once said, "To get rich, you must first build a road." This adage holds as true in the Information Age as in the Industrial Age. To fully realize the gains of the outsourcing industry, countries must concentrate on upgrading their infrastructure to support industry clusters – modernizing their power facilities, technological infrastructure, airports, highways, and shipping ports. Additionally, effective legal and regulatory frameworks are essential to address security and privacy concerns of outsourcing firms.

OUTSOURCING SERVICES ALONG THE VALUE CHAIN

Global outsourcing of services can be classified into five broad categories, based on their contribution to value and their skill requirements:

1. *Data entry, digitization, conversion, transcription.* At the lowest end of the value and skill chain are back-office functions such as data entry, digitization, and conversion activities, and basic clerical services that do not require domain knowledge or specialized expertise. One of the most common of these is transcription services, whereby dictations by doctors or lawyers are converted to written medical or legal records.
2. *Rule-based processing and simple support services.* Next in the value chain are teleworking services, which involve rule-based processing and simple voice and on-line customer relations services, based on rules set by the client. These include call-centre services, email-processing, data processing, billing and payments, account opening, and screening of credit card applications – all at rates as low as \$10 per hour.
3. *Activities involving problem solving and decision making.* Slightly higher up the value chain are activities that involve problem solving and decision making, such as developing solutions for improving processes or streamlining systems. In developing countries like India these command rates of \$10 to \$15 per hour.
4. *Complex multimedia support services.* Next on the value chain are teleworking services that involve direct interaction with customers and more elaborate transactions with the client, but moving beyond pure voice-based support to mixed media-based support services and beyond writing routine software applications to the remote management of sophisticated networks. These include activities like web support, telemarketing, providing customer help desks, technical back office processing, e-customer relationship management, website design, software development for entire business processes, and hardware support services.
5. *Specialized services requiring domain knowledge and skills.* At the top end of the value chain are services that involve domain expertise and specialized skills. These include research and engineering services such as 3-D modelling, drawing up technical specifications for tenders, plant engineering, piloting prototypes, testing and optimization, redesigning for improving cost-performance ratios, financial analysis, risk management, equity research services, and consulting and advisory services.

As a result, the outsourcing flows between countries are becoming more complex. For instance, several Indian IT firms and some independent BPO providers are outsourcing to other developing countries like China and the Philippines that offer special skills, or to developed countries like Canada that offer proximity to US clients. Singaporean companies such as Singapore Computer Systems are in turn establishing their own outsourcing facilities in India and China. These new patterns of outsourcing are driven by the need to diversify production bases, pool risks and take advantage of individual country strengths.

A number of Asian countries have been seizing these opportunities. According to one study, five of the top ten outsourcing destinations are in Asia. In 2001, for business process operations, for example, India was the leader with \$7.7 billion, while China accounted for \$1.1 billion. This compares with \$3 billion in Israel, \$0.5 billion in Mexico and \$0.4 billion in

Eastern Europe. But many other countries have been establishing themselves as outsourcing destinations.¹⁰

Bangladesh is a host to medical transcription services such as Digital Divide Data.

Cambodia provides outsourced data services to business and public customers both at home and abroad, and is at present engaged in the task of digitizing Harvard University's archives.

China is a key product development centre for GE, Intel, Microsoft, Phillips, and other large electronics firms, for hardware design and embedded software.

India has IT companies such as Infosys, TCS, Wipro, and Satyam that provide IT support, technical help desks, web support, and infrastructure services to overseas companies. There are also companies working in product

development, engineering design, testing, and technical analysis.

Philippines is a host to outsourced work by some 8,000 foreign companies, covering services such as graphic design, architectural blueprints, telemarketing, accounting, and software code writing.

Singapore has service providers engaged in leading-edge functions like remote robotics management, health care, and genetic diagnostics.

Viet Nam carries out simple coding jobs for IBM, Cisco, Sony, Nortel Networks, and NTT, but is also increasingly engaging in higher-value activities connected to geographic information systems, computer-aided design, finance, factory automation, healthcare and computer animation.

Clearly, there could also be opportunities for outsourcing in geographically isolated states – landlocked countries, for example, and small island developing states – especially in those, such as Bhutan and Mongolia, that have a

significant English-speaking population or relatively high education levels.

Reasons for Outsourcing

Global outsourcing is driven by many different factors. In some cases, companies will outsource to an overseas company that provides specific skills. But generally enterprises are seeking to cut costs on more basic activities, and so they will be looking to countries and companies that can provide low-wage, highly-educated workers who offer a broad range of skills – and can do so through good low-cost, high-bandwidth telecommunications infrastructure. Other factors – in both the buying and selling countries – that influence the choice of outsourcing partners are indicated in Box 5.9.

The principal reason for outsourcing is usually to cut costs, and therefore most outsourcing goes to low-wage economies. For example, in the US telephone operators and medical transcribers earn around \$13 per hour, while in India they would receive less than \$2 per hour.¹¹ Similarly, in the US a financial analyst might earn around \$35 per hour while a counterpart in the India might get \$6 to \$15 per hour. One survey concluded that the monthly cost of keeping one high-tech employee in Silicon Valley is \$15,000 per worker, while someone in New Delhi with the same skills, responsibilities and job package would cost \$2,500 a month. This translates into savings of \$12,500 per month, or \$150,000 for a year. By outsourcing 10 jobs to India, a start-up in the US can thus cut payroll costs by \$1.5 million. Initial investment costs are also far lower: setting up a call centre in Delhi, for example, costs only around one-third of what it might cost in the US.¹²

Many outsourcing firms have realized, however, that they are saving even more as a result of productivity gains – fewer errors in data processing, for example, or fewer defects in computer programs, or a higher quality of

Many outsourcing firms have realized that they are saving even more as a result of productivity gains

BOX 5.9

FACTORS SHAPING COMPETITIVENESS IN GLOBAL OUTSOURCING

In the service-providing country

- Availability of labour and skills, the quality manpower and related educational investments
- Competitive wages
- Strength of domestic IT industry and its export orientation
- Physical infrastructure
- Government incentives and support
- The business environment
- Intellectual property legislation
- State of regulation in supporting areas such as telecoms and the Internet

In the purchasing countries

- Business cycle conditions
- Availability of skills and labour
- Relative wages
- The need for diversification, risk pooling, and cost reduction
- Technological developments and possibilities for dis-intermediating services
- Legislation concerning outsourcing
- Data protection and intellectual property requirements
- Legislation on immigration
- International certification for quality
- Diaspora and others with contacts in the providing country

transcription. Outsourcing also allows companies to mitigate risk by diversifying operations across a number of centres. At the same time, they can reshape their activities at home to concentrate their energies on their core competencies.

Constraints on Outsourcing

Not all countries have been able to take advantage of outsourcing opportunities. The main constraints are:

Lack of Infrastructure. Some of the poorer countries, for example, do not have the necessary telecommunications systems or reliable power supplies.

Lack of Skilled Manpower. Only a few countries in the region have enough educated people with the right skills, including computer literacy and knowledge of foreign languages, especially English.

Weak Legal and Regulatory Frameworks. Outsourcing companies demand strong legal systems covering data protection and privacy, particularly in areas like health care and financial services. Similarly, they demand a robust regulatory framework to protect online payments and transactions. Many developing countries in the region do not have legal systems that can meet international standards in these areas.

Even countries with considerable experience in outsourcing can run into problems. India, for example, is now having difficulty recruiting enough skilled people: the education pipeline is not producing sufficient educated young people; turnover rates are high, wages are rising and service providers are poaching among themselves.

In addition, there are constraints imposed by the outsourcing countries. Some of these might be indirect, such as greater restrictions on

temporary work visas for professionals who need to spend time overseas preparing and maintaining outsourcing contracts. Other constraints are more direct, as workers in the outsourcing countries object to a loss of jobs. In the US, labour unions, like the Communication Workers of America, are lobbying against outsourcing by US companies or demanding parity in wages between developing and developed country service providers. In December 2002, for example, 22,000 engineers in Seattle threatened to walk out to protest Boeing's decision to outsource work to Russian engineers – as a result of which Boeing halved its employment of Russians.

In response to such pressures, several states have been restricting outsourcing by public bodies. In 2002, New Jersey, for example, passed a bill banning the outsourcing of government contracts to other countries. It is difficult to gauge the net impact of such protectionist pressures. Bans on government outsourcing are not likely to have a major impact, since in countries like India such projects constitute 1 per cent or less of outsourcing. However, the protectionist challenges could grow and start affecting the volume and type of business outsourcing.

Employment Impact of Global Outsourcing. Outsourcing employs relatively small numbers of people at the top end of the labour market and might be thought unlikely to affect poverty directly. India, for example, has just over a million people working in software and IT-enabled services, but this amounts to just one-quarter of 1 per cent of all workers. Even if the sector were to grow fourfold over the next few years, it would still account for only 1 per cent of the work force, and the opportunities would be limited to those who have basic literacy and computer skills and access to training opportunities.

However, such work does have some advantages for human development. First, it draws in a wider social spectrum than many

Outsourcing employs relatively small numbers of people at the top end of the labour market; the availability of relatively high-paid jobs helps to stem the 'brain drain'

other forms of employment. Call centres, for example, which employ around 50,000 people in the Philippines and 150,000 in India, have quite inclusive employment policies: in countries facing shortages of skilled labour, companies are happy to hire people who might traditionally have been outside the labour force, including women and retirees. In India, for example, Wipro has 5,000 employees, of whom almost half are women; and for ICICI One Source and DakshIndia the proportion of female employees is around 60 per cent.

Some companies are also experimenting with locating data centres and telecentres closer to residential areas, or allowing people to work from their homes – making it easier for homemakers and retirees to participate. Others have deliberately focused on expanding employment opportunities beyond the usual target group of graduates and the economically well-off. The Cambodian NGO-initiated enterprise, Digital Data Divide, a digitization and data-entry services provider, offers jobs to physically challenged people, those affected by land mines and polio, and orphans, at monthly rates (\$65) that are higher than those in manufacturing (\$40). Half of the company's workforce of a staff of 93 are females.¹³ Thus, global outsourcing can enable less visible and even marginalized groups to integrate with the labour market. Moreover, as wage rates in this business tend to be higher than elsewhere, it can provide them with a big improvement in their standards of living.

Outsourcing can also help boost national levels of skill. This can happen both overseas and at home. Overseas employees can take in workers to learn about their technical applications, products, processes, and marketing techniques. But even the workers who stay at home will acquire many skills in customer relationship management – thus learning to focus on quality and timeliness. The workforce thus acquires greater discipline, a more professional work culture, and a greater sense of accountability.

The availability of relatively high-paid jobs also helps to stem the 'brain drain'. Outsourcing by multinationals like GE and IBM in developing countries like India and China has been accompanied by a significant upward movement in salary levels that reduces the incentive for skilled people to emigrate. Indeed, there is some evidence of reverse migration: a number of companies are relocating expatriates to offshore operations, and many senior professionals and managers are also returning voluntarily to their country – attracted by the internationally comparable salaries, improved working conditions and changing image of their countries.

However, not all the employment effects are positive, and there is some evidence that outsourcing can also lead to de-skilling. This is because outsourcing companies can tempt even highly trained people to take lower-skilled but highly paid jobs. In Bangladesh, for example, doctors are accepting work as medical transcribers; and engineering and science graduates are often employed in routine tasks such as software programming and web applications design and support. As well as underutilizing skills, this also risks skewing national education and training policies towards meeting short-term needs for lower-skilled people and away from education in more fundamental disciplines and the longer-term research and development that will be needed to help build indigenous manufacturing capabilities.

Spillover Employment Effects

The benefits of outsourcing are not just, of course, felt by people directly employed. These workers will spend their wages and produce important externalities and spillover effects. Most outsourcing employees tend to be in their 20s and 30s, an age group that stimulates demand for consumer durables and other services. The Gurgaon district of Delhi, one of India's main outsourcing hubs, has seen a rapid

The rapid growth of the outsourcing industry is also widening disparities

expansion in shopping centres and related infrastructure in response to demand from employees in the BPO industry.

Outsourcing workers also stimulate a wide range of ancillary services – in housekeeping, security, catering, transport, real estate, telecoms, and computer equipment provision and maintenance. Caterers are required for shift catering services. Cleaners, janitors, and other support staff are required to maintain world-class premises. In the absence of reliable public transport, fleets of vehicles and drivers are hired to ferry call centre employees to and from their homes. Thus, while the sector itself may be directly geared to a certain kind of employee profile, it can indirectly create equitable employment opportunities, which are neutral to gender, type of business, and skill level.

Outsourcing also triggers the creation of new training institutions and infrastructure, such as computer technical schools, diploma programmes, and IT training and applications courses in colleges and universities. As outsourcing providers look further afield, these institutions are now appearing beyond the metropolises in the smaller cities and towns – helping to distribute income and employment benefits.

Social Impact of Outsourcing

Outsourcing can have many positive social benefits – by providing age- and gender-neutral employment to many thousands of people. But it can also have social costs. Some of these are related to difficult working conditions. These include adverse health effects due to working night shifts, the sedentary nature of the jobs, and the constant use of computers. Long night shifts at call centres can also prevent young employees from having a normal social life and may isolate them from their communities.

The rapid growth of the outsourcing industry is also widening disparities. In India, for example, Bangalore's explosive growth has

aggravated inequalities between cities and rural areas and small towns. Within the city, too, while some special enclaves are being developed for teleworking establishments, other areas are being neglected. Meanwhile, the urban poor are suffering from rising costs, deteriorating civic amenities, and an influx of migrants. Outsourcing can thus contribute to a labour market and information divide that cannot be in the interests of sustainable long-term development.

Fiscal and Trade Impact

Given its scale, outsourcing might be an important source of tax revenue that could enable developing-country governments to spend more on social services. Often, however, the fiscal benefits are fairly limited. In order to encourage such activities, many governments have exempted them from taxes – or from import duties on hardware and telecoms equipment. Indeed, the government may have spent considerable amounts in building communications infrastructure for teleworking establishments. As a result, in fiscal terms outsourcing firms may not be net contributors but net recipients.

Likewise, on the trade front, although outsourcing contributes to export earnings, there is also a significant foreign exchange outflow from outsourcing providers – buying bandwidth from telecommunication firms, for example, or purchasing hardware from the outsourcing economies.

Domestic Strategies on Outsourcing

Outsourcing can have many effects, both positive and negative, for human development (Box 5.10). The challenge for governments is, therefore, to create an environment that is conducive for outsourcing while integrating it with the rest of the economy, so as to capture the associated developmental benefits. This can cover a range of policy areas (Box 5.11).

BOX 5.10

HUMAN DEVELOPMENT OUTCOMES OF OUTSOURCING

<i>Channel of Impact</i>	<i>Nature of Impact</i>	<i>Human development outcome</i>
<i>Employment and income creation – positive</i>	Creates well-paying jobs for the computer-literate. Creates high-level jobs for persons with specialized skills and domain expertise. Absorbs young entrants into the labour force. Creates opportunities for less-integrated sections such as disabled and women in the workforce.	Empowerment Equity Productivity
<i>Employment and income creation – negative</i>	Underemploys and underutilizes human capital. Distorts employment choices. Provides low amounts of employment relative to requirements.	Negative sustainability and equity effects
<i>Skill and knowledge transfer – positive</i>	Promotes acquisition and transfer of specialized skills and domain knowledge. Enables acquisition of generic and portable skills. Develops capabilities for indigenous production and innovation.	Productivity, empowerment
<i>Skill and knowledge transfer – negative</i>	De-skills due to misallocation of human capital. Re-prioritizes educational investments and policies away from developing long-term capabilities. Limited impact of skills developed on other parts of the economy.	Concerns about productivity
<i>Resource generation – positive</i>	Enhances investment by domestic and foreign companies. Encourages small and medium enterprises. Value creation. Increases export earnings. Increases fiscal resources.	Productivity, empowerment, equity
<i>Resource generation – negative</i>	Leads to foreign exchange outflow through imports and repatriation of profits. Fiscal concessions, other incentives and diversion of resources from other areas of the economy.	Equity concerns if the sector is an enclave and a net recipient of benefits
<i>Augmenting the human capital base – positive</i>	Helps retain skilled persons. Helps to attract skilled persons into country.	Productivity
<i>Augmenting the human capital base – negative</i>	Limited impact so far. Repatriation leads to loss of employment opportunities and wages.	Productivity
<i>Externalities and spillover effects – positive</i>	Leads to growth in ancillary industries and activities and related employment and investment creation. Development of related physical infrastructure. Encourages spread of education, training, computer literacy, and Internet penetration. Creates demand and a consuming middle class.	Empowerment, productivity, equity, sustainability
<i>Externalities and spillover effects – negative</i>	Increases urban-rural disparities. Increases disparities within urban areas. Increases disparities across regions. Leads to enclave-type growth and associated inequities with other sectors. Diverts resources away from other sectors.	Concerns about equity and sustainability
<i>Social, cultural, occupational aspects – negative</i>	Leads to undesirable lifestyle and working hours, loss of cultural identity. Increases social inequity. Increases the information divide.	Concerns about equity, sustainability, long-term productivity

DOMESTIC MEASURES TO PROMOTE OUTSOURCING

<i>Areas for policy action</i>	<i>Specific measures</i>
<i>Labour market deepening and human resource development</i>	Investments in education and training to: <ul style="list-style-type: none"> – create a pipeline of manpower for lower-end activities – create a high-tech workforce – develop curricula, programmes, institutions, training infrastructure, specialized skills – ensure quality certification and recognition Labour laws and standards for: <ul style="list-style-type: none"> – welfare-oriented human resource management practices – employee retention and career development strategies
<i>Physical infrastructure</i>	Invest in communication services by: <ul style="list-style-type: none"> – dismantling the government monopoly of provision – promoting competition in telecom services through deregulation, especially in Internet service provision and long-distance telephony – investing in satellite links – expanding bandwidth – promoting teleworking establishments by creating technology parks and outsourcing hubs – facilitating the acquisition of real estate, power, telecom links, and the procurement of equipment
<i>Regulatory framework</i>	Intellectual property legislation <ul style="list-style-type: none"> – on data privacy, data protection and piracy Consumer protection laws Spectrum liability legislation E-commerce regulations E-governance-related legislation Regulation on cross-border payments and Internet transactions Technology licensing framework
<i>Tax and subsidy policies</i>	Tax incentives and their withdrawal <ul style="list-style-type: none"> – provide fiscal incentives in initial stages – bring the industry under the tax net once it has matured and grown in size – use fiscal resources to target industry-specific and wider investments in infrastructure, training Export incentives <ul style="list-style-type: none"> – provide import duty concessions and rebates in initial stages only, remove later and treat at par with other sectors – discourage firm- or sector-oriented export subsidies that could distort trade – provide general infrastructural subsidies that are not trade-distorting

Human Resources and the Labour Market. Targeting the high end of the market will require investment in professional training. The Chinese Government, for instance, is investing in training programmes in partnership with MNCs, and Indian firms are providing greater emphasis on skills like software development with appropriate quality certification. The Vietnamese Government too is encouraging overseas training institutes from Australia and India to train thousands of Vietnamese in dedicated centres across the country.

Labour Standards and Regulation. Some of the negative social, cultural and occupational outcomes can be mitigated if governments focus on core labour standards, human resource management practices, and domestic labour laws. Governments and industry can also work together to combat high attrition rates, by providing more training and development and offering structured career paths.

Telecommunications and Other Physical Infrastructure. Smaller countries and companies

Some of the most important opportunities for multilateral action on outsourcing should be through the negotiations on the General Agreement on Trade in Services (GATS)

will need to develop their infrastructure. They can, for example, deregulate telecoms and Internet services and eliminate public monopolies so as to bring down costs. Viet Nam, for example, is planning to dismantle the state monopoly in Internet services, and to allow foreign equity participation in the telecom sector. Malaysia has invested heavily in IT infrastructure (Box 5.12).

Regulatory Framework. Governments may need to introduce internationally compatible laws and regulations concerning the protection of intellectual property rights and Internet transactions, data privacy, consumer protection, e-governance, and spectrum liability.

Fiscal Policy and Incentives. While tax breaks may be necessary to encourage growth in the initial stages of a business, the long-term aim should be to bring the outsourcing providers into the tax net, so that part of their profits are reinvested in the society.

Negotiation through GATS

Domestic strategies need to be supplemented with international action. The recent surge in opposition to global outsourcing in key markets like the US and the UK makes it all the more

important to address this issue through multilateral, regional, and bilateral negotiations and agreements.

Currently, the electronic marketplace is largely free of explicit trade barriers and WTO members have agreed to temporarily exempt electronic commerce from customs duties and taxes. These commitments now need to be bound into agreements to preclude the introduction of new barriers to e-commerce.

Some of the most important opportunities for multilateral action on outsourcing should be through the negotiations on the General Agreement on Trade in Services (GATS). However, in areas such as distribution, advertising, architecture, legal work, accountancy, and computer and related services, less than half of the commitments in the relevant clauses of GATS are full or unrestricted – mainly due to the lack of commitments by developing countries. This kind of liberalization is best addressed through a ‘positive list’ to allow countries to pace the degree and scope of liberalization in accordance with their needs and their ability to prepare supporting domestic regulations.

Countries can also pursue their interests in outsourcing through regional and bilateral trade and investment agreements, which can prepare the ground for regulatory frameworks that can later be extended to the multilateral level.

Partnerships

Governments should also be able to rely on support from bilateral aid organizations, various parts of the UN System, and the World Bank – for developing infrastructure, organizing training and providing policy advice. They can also help in improving national statistics on outsourcing.

In addition, private enterprises, national and multinational, and their industry associations can assist in efforts to liberalize markets and counter protectionist threats. In India, for

BOX 5.12

CREATING COMPARATIVE ADVANTAGE FOR OUTSOURCING IN MALAYSIA

Labour costs are far higher in Malaysia than in China and India. Nevertheless well-developed infrastructure and government support have made it an attractive outsourcing destination. As part of its multimedia Super Corridor project, the Government has invested around \$10 billion in setting up two IT cities – Cyberjaya and Putrajaya – with hi-tech parks, fibre-optic networks, new roads, and laws promoting e-commerce.

Malaysia is also emerging as a hub for research and clinical services in biotechnology. Based on local capabilities in a variety of Asian languages, like Mandarin, Cantonese, Hokkien, Bahasa Malay, Bahasa Indonesia, Tamil, Hindi, Thai, and Japanese, the Government is promoting the country as a high-end contact centre for customer services in the Asia-Pacific region and a pan-Asian hub. Outsourcing is expected to provide employment to 50,000 persons in the corridor cities by 2011. However, the country faces a shortage of skilled IT workers, and currently imports these from India and China.

After oil and petroleum, the world's second largest industry is travel and tourism

example, the National Association of Software Service Companies (NASSCOM) has helped to highlight the mutual benefits from outsourcing and dispel misconceptions. Domestic firms engaged in outsourcing may also want to establish some local presence in their export markets, to enable them to lobby more effectively with concerned governments and industry bodies.

A New International Division of Labour

Global outsourcing represents a new international division of labour. While in manufacturing production was split across countries based on competitive advantage, in outsourcing different countries will occupy different parts of the global services space.

For many developing countries, this can be a valuable source of growth and economic and human development – creating employment and incomes, and empowering many sections of society and promoting growth with equity. It can also transfer new skills, technologies, and processes.

Realizing the potential of outsourcing will, however, require determined and focused government action to spread the benefits beyond small enclaves and ensure that it stimulates broad-based growth by integrating outsourcing activities with the rest of the economy. To accomplish this government will need to invest in physical and social capital and try to ensure that enterprises move steadily up the value chain. Overall, global outsourcing must be seen not as a single engine of growth but as another potential avenue for promoting economic and human development.

International Tourism

After oil and petroleum, the world's second-largest industry is travel and tourism. Globally, in 2005 this was expected to generate \$6.4 trillion of economic activity, equivalent to 3.8

per cent of global GDP, though if one also considers the many other parts of the economy that also depend on tourism, the 'travel & tourism economy', the proportion rises to 10.6 per cent. Directly the sector employs 74 million people, 2.8 per cent of total world employment; indirectly it employs 222 million people, 8.3 per cent of total employment.

A tourist, according to the United Nations and World Tourism Organization definition, is someone who is staying outside his or her usual environment for not more than one consecutive year for leisure, business or other purposes. Some of these people may not travel very far; others will traverse half the globe. Since this report is about international trade, it is concerned specifically with tourism across international frontiers, though many of the same considerations apply to domestic tourism, which can often make a more significant contribution to human development (Box 5.13).

In 2004 there were 763 million international tourists, spending around \$623 billion. But by the year 2020, WTO predicts that the number of international arrivals will reach 1.6 billion – spending a total of \$2 trillion per year.¹⁴ Of these worldwide arrivals in 2020, 1.2 billion will be those of intra-regional travellers and 0.4 billion will be of long-haul travellers.

BOX 5.13

THE SIGNIFICANCE OF DOMESTIC TOURISM

With the recent decline in long-haul travel post-9/11, SARS, the Iraq war and the Asian tsunami, many destinations, especially in the larger countries, have come to place greater reliance on the domestic market. This has significant advantages over international tourism: domestic visitors are more likely to support smaller local enterprises, help even out the seasonality patterns – and help conserve foreign exchange.

China has the world's largest domestic tourism market. In 2004, the number of domestic tourists reached 1.1 billion, and domestic tourism revenues totalled \$57 billion, accounting for 67 per cent of China's gross tourism revenue.

India too has a huge domestic market. Unconfirmed estimates suggest more than 350 million domestic tourists, around one-quarter of which is pilgrimage traffic. Although national tourists spend less than international tourists, they travel in large numbers and tend to stay longer, and thus help create more jobs (Aibara and Gopalani 2005).

Many more of these people are arriving in the Asia-Pacific region. In the 1950s, the region contributed less than 10 per cent to global tourist volume, but by the early 1970s, its contribution had risen to 20 per cent, and by 2004 to 40 per cent.

As elsewhere in the world, tourism in the Asia-Pacific region was greatly disrupted by the triple shocks of September 11 in 2001, the SARS outbreak and the war in Afghanistan as well as in Iraq. The September 11 attacks alone caused a 10 per cent drop in travel worldwide – up to 30 per cent in some countries – and cost 6.5 million jobs. In 2004 there was a spectacular rebound: while tourism grew in all the world's regions, in the Asia-Pacific region it increased by 29 per cent – though a number of tourist destinations in the region were later hit by the tsunami in December 2004.

The distribution of these arrivals is indicated in Table 5.1. The significance of tourism to a particular country can be considered in a number of ways. One is through the total number of arrivals. This tends to be greater for the largest countries – with China in the lead, followed by Malaysia, Thailand and Singapore respectively, all of which in the past decade have developed huge tourism infrastructures.

Another approach is to consider international tourist revenue as a proportion of GDP. This gives some indication of how economically dependent a country is on tourism. For those countries with GDP figures available, the Maldives is at the top of the list with tourism representing 32 per cent of GDP, followed by Vanuatu and Fiji respectively. Were the data available, other Pacific Islands would also rank highly.

A third way of assessing the distribution is to consider tourist arrivals per head of population (Figure 5.3). This too indicates the degree of dependence on tourism but also gives an idea of the social impact. In this case, Palau comes out ahead followed by the Maldives, but even Singapore has more annual tourist arrivals than its total population.

Finally, one can consider arrivals from the perspective of poverty. The most popular destinations seem to be the middle- and upper-income developing countries. Nevertheless,

TABLE 5.1
TOURIST ARRIVALS IN ASIA-PACIFIC COUNTRIES, 2005

Country	Population* (millions)	Arrivals (millions)	Growth (%)	Tourism earnings (% of GDP)
<i>East Asia</i>				
Mongolia	2.4	0.2	...	...
China	1280.4	42.5	7.5	2.4
Korea, Rep.	47.6	6.0	5.0	1.6
Korea, Dem. Rep.	22.5	...	4.7	...
<i>South-East Asia</i>				
Lao PDR	5.5	0.2	-2.9	5.5
Cambodia	12.5	1.0	...	7.3
Philippines	79.9	1.7	-4.6	2.7
Viet Nam	80.4	2.1	9.3	2.2
Indonesia	211.7	5.4	2.4	3.1
Thailand	61.6	12.4	6.5	5.2
Malaysia	24.3	18.1	12.7	5.3
Singapore	4.2	7.8	4.3	2.6
Brunei	0.4	1.0	1.0	3.3
Myanmar	48.8	0.2	1.8	...
<i>South Asia</i>				
Afghanistan	28.0	...	...	...
Iran, Islamic Rep.	65.5	1.9	7.1	3.6
Maldives	0.3	0.5	4.1	32.3
Bangladesh	135.7	0.2	4.7	...
India	1,048.6	2.5	0.4	2.1
Nepal	24.1	0.2	-19.7	4.4
Sri Lanka	19.0	0.3	-3.3	3.8
Pakistan	144.9	0.6	3.8	2.6
Bhutan	0.9	0.0	-1.6	...
<i>Pacific</i>				
Vanuatu	0.2	0.051	-0.8	17.2
Kiribati	0.1	0.004	-4.3	9.7
Fiji	0.8	0.361	-0.2	12.0
Papua New Guinea	5.4	0.043	-8.9	5.8
Marshall Islands	0.1	0.005	...	...
Samoa	0.2	0.096	2.7	...
Micronesia	0.1	0.021	5.5	...
Palau	0.0	0.054	-2.0	...
Solomon Islands	0.4	...	...	3.1

Notes: Population data are for 2002; tourist arrivals are for 2004 and growth in arrivals in 2004 over the previous year; tourism as a percentage of GDP is based on estimates by WTTC for 2005.

Source: Aibara and Gopalani 2005.

some countries with high levels of poverty also depend on tourism for more than 5 per cent of GDP including Cambodia, Lao PDR and Vanuatu.

The Human Development Impact of Tourism

From the human development perspective, the most important effect of tourism is to create employment. The tourist industry employs people at many levels of skill, from holders of MBAs to unskilled migrants from the rural areas. They can have a broad range of skills – hotel managers, fitness instructors, drivers, masseurs, beauticians, chefs – and some are employed directly, others indirectly, in support sectors such as retail trade, transport, or arts and crafts.

The scale of employment from international and domestic tourism is indicated in Table 5.2. This also estimates the ratio of indirect to direct employment, which for the region overall is greater than two to one, though this is swayed by the high figure for China. Another aspect of employment is highlighted in the table: which the proportion of the total workforce employed in tourism. In the Maldives, for example, this is very high, at around two-thirds. For the region as a whole, it is close to 7 per cent. Currently, many countries of the region are focusing on the development of domestic tourism, which is showing fast growth (Box 5.13).

Compared to other modern sectors, a higher proportion of benefits in the travel and tourism industry go to women – whether through formal or petty trade and informal employment. According to the ILO, women constitute 70 per cent of the entire tourism workforce, though the percentage varies enormously by country, and in Muslim countries can be less than 10 per cent.

The tourist industry and related services also have the merit of being quite labour-intensive; for each visitor, beds have to be made, food

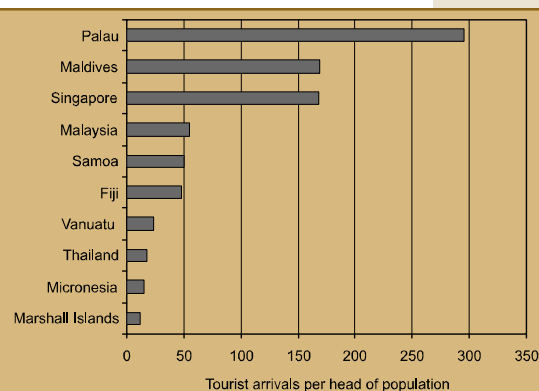


Figure 5.3: Tourist arrivals per 100 people, 2002

Source: Aibara and Gopalani 2005.

TABLE 5.2

EMPLOYMENT IN THE TOURIST INDUSTRY

Countries	2004 (Millions of people)				
	Direct	Indirect	Total	Direct/ Indirect	Share of (%) labour force in tourism (%)
<i>East Asia</i>					
China	14.8	47.5	62.3	3.2	8.3
Korea, Republic of	0.5	1.3	1.9	2.6	8.4
<i>South-East Asia</i>					
Cambodia	0.2	0.4	0.6	2.0	8.3
Indonesia	3.2	5.3	8.5	1.7	8.5
Lao PDR	0.1	0.1	0.2	1.0	7.3
Malaysia	0.5	0.8	1.3	1.6	12.7
Philippines	..	..	2.8	..	9.6
Singapore	..	..	0.1	..	6.0
Thailand	1.5	1.6	3.1	1.1	8.9
Viet Nam	0.6	1.8	2.4	3.0	6.5
<i>South Asia</i>					
Bangladesh	0.9	1.4	2.2	1.6	3.0
India	11.4	13.1	24.5	1.1	5.6
Maldives	0.0	0.0	0.1	..	64.4
Nepal	0.3	0.4	0.7	1.3	7.0
Pakistan	1.0	1.2	2.2	1.2	4.1
Sri Lanka	0.3	0.4	0.7	1.3	8.8
<i>Pacific</i>					
Fiji	0.0	0.1	0.1	..	25.4
Kiribati	..	..	..	..	22.6
Papua New Guinea	0.1	0.2	0.3	2.0	11.2
Solomon Islands	0.0	0.0	0.0	..	8.3
Tonga	0.0	0.0	0.0	..	12.3
Vanuatu	0.0	0.0	0.0	..	47.0
Total	35.9	76.4	115.3	2.1	6.9

Note: The final column is the ratio of indirect to direct jobs.

Source: Aibara and Gopalani 2005.

From the human development perspective, the most important effect of tourism is to create employment. The poor can have a direct stake in the tourism industry, not just through jobs but also through many business opportunities

cooked and floors swabbed. In India, for example, it has been calculated that a \$23,000 investment will generate 89 jobs in the hotel and restaurant industry, compared with 45 in agriculture and only 13 in manufacturing.¹⁵

Many of these jobs are low-paid and seasonal, but they do offer low-skilled workers opportunities to move up the income ladder. Many poor people, who have lost work in agriculture as a result of more liberalized and competitive global food markets, have been transferred to the tourist industry either to work permanently or as part-time or casual labourers during the high season.

The poor can have a direct stake in the tourism industry not just through jobs but also through many business opportunities, particularly in the informal sector, where there are many small-scale, locally run tourism enterprises. These benefits can also be geographically dispersed. Although high-volume tourism can be concentrated in beach resorts, cities or famous sites, there are also opportunities to create tourism-related jobs in remote areas that have few other options.

In addition to its contribution to poverty reduction through employment, tourism also helps boost government revenues through taxation. This can be generated directly through a tourism tax that is paid either to the local or national authorities, or through taxes on the profits of tourist-related businesses. These revenues can then be invested in public services. More indirectly, by boosting foreign exchange earnings tourism supports macro-economic stability, which again contributes to poverty reduction.

However, it should also be noted that much tourist revenue leaves the country – through payments to foreign-owned hotel chains, imports of goods for the tourism industries, or revenues accruing to foreign airlines. In small island nations these ‘leakages’ can be quite large – though not necessarily higher than for other sectors such as manufacturing.

For its contribution to poverty reduction, tourism can be considered in three main segments: business travel, leisure travel, and nature-based eco-tourism.

Business Travel. In the Asia-Pacific region, business travellers are most likely to go to large urban centres like Bangkok, Hong Kong, Mumbai, Shanghai and Singapore. Here they, like other travellers, create a demand for services, though the extent to which these services are provided by the poor will differ from city to city – greater in Mumbai and Shanghai, for example, which have millions of poor people living in urban slums, than in wealthier Singapore. In addition, business travellers can help combat poverty since they further their own businesses; this should in the longer term boost economic growth, which, if equitably distributed, will expand opportunities for all.

Leisure Travel. As with business travellers, the impact of leisure travellers on poverty will depend on their choice of destination. Also important, however, is how they interact with the local environment. People travelling on package tours, especially those going to enclave developments or all-inclusive resorts, or who are arriving on cruise ships, may meet very few local people. They will certainly encounter waiters or receptionists, or others formally employed in the tourist industry, but they will generate less work for informal businesses. Budget tourists, on the other hand, although they spend less in total on their trip, may spend more on local goods and services. Nevertheless even the income from high-end tourism can help combat poverty if it is redistributed through government spending. A number of Asian countries, such as Bhutan and the Maldives, have pursued this low-volume, high-yield route (Box 5.14).

Nature-based and Eco-tourism. Leisure visitor flows continue to be driven by mass tourism, but

there has been a noticeable shift towards niche, special-interest and experiential tourism. Leisure visitors are increasingly seeking to spend time on understanding the culture, heritage and natural environment of the places they visit – a trend that bodes well many rural and remote areas. The fastest-growing form of special-interest tourism is eco-tourism – which refers to travel to natural areas in responsible ways that conserve the environment and sustain the well-being of local people. Bhutan and Nepal, for example, and the relatively underdeveloped North-East region of India, are uniquely placed to build on their comparative advantage in this area. Indeed, Asia as a whole has many of the world’s major Buddhist heritage sites. Nature-based tourism offers many advantages for poverty elimination. It takes place in remote areas where residents are likely to be poor. It involves a higher proportion of independent travellers who may spend more locally. It also contributes to the conservation of the local heritage and to biodiversity. But it also brings risks. Nature-based tourism does not necessarily have low impact, particularly if it occurs in fragile areas. It can also suffer from high ‘leakage’ if it requires importing supplies and skills.

Potential Negative Impacts of Tourism

As with other components of economic growth and globalization, tourism can also have some negative effects.

Inflation. Investment in tourist destinations can push up prices of land, accommodation and food – in some cases driving poor people out.

Resource Conflicts. Tourist enterprises can also harm many livelihoods by taking over natural assets such as land or beaches or by polluting waterways. People in coastal communities in many Pacific Islands, for example, rely on fish

BOX 5.14

HARNESSING LEISURE TRAVEL IN THE MALDIVES

The Maldives has been extremely successful in developing a viable tourism industry, which directly and indirectly is responsible for over 70 per cent of GDP. And with an economically active population of 88,000 people, this provides 25,000 jobs, though 6,800 of these are held by expatriates.

In the late 1970s and early 1980s, the Maldives had no choice but to promote the mid-scale tourist segment – till such time as the islands attained the critical mass required to sustain and encourage commercial air traffic and the requisite infrastructure. Lately, however, given the small size of the country and its fragile ecosystems, the Government has taken a conscious decision to focus on high-end tourism and has encouraged the growth of boutique-style, luxury resort developments. This approach has helped maximize revenues generated for both government and private sector investors while maintaining environmental and social sustainability. The Maldives does still offer a mix of properties to cater to different groups, but it also hosts some of the world’s top resorts. These are clearly attractive since the visitor repeat rate is 20–30 per cent. These are also very profitable, and the high rates of return for most projects are encouraging many investors and top hotel chains to establish a presence.

Source: World Bank, ADB and UN 2005.

for their main source of protein and income and can see their food security and livelihoods undermined by tourist development.

Burden on Services. New tourist enterprises put pressure on water supplies, for example, and on waste management services – burdens that are often passed on to other local residents and businesses.

Environmental Destruction. Mass tourism is generally associated with high consumption of water and energy. Hotels are often concentrated in small areas, and they contribute to the increasing traffic congestion and air and water pollution. In some cases tourists who are attracted by the remoteness or beauty of locations can effectively destroy what they have come to visit – as roads and hotels intrude on natural vistas, for example, or trekkers erode paths. And in coastal areas, activities such as snorkelling and scuba diving can endanger fragile marine ecosystems.

Spread of Disease. There is no established correlation between AIDS and tourism, but it

Tourist enterprises can also harm many livelihoods by taking over natural assets such as land or beaches or by polluting waterways

While tourism can lead to developmental problems, these can be resolved or minimized with proper planning and management

does seem that in many countries, such as Thailand, the HIV prevalence rate is particularly high in tourist areas, and the continuing increase in tourist numbers can aggravate the problem.

Cultural Issues. Many tourists, who are typically richer than the local population, can undermine age-old cultures by introducing consumerist values. Their hedonistic lifestyles can also offend the sensibilities of conservative communities. In addition, adapting local culture to tourism, through special performances, for example, can lead to a loss of identity and authenticity.

Exploitation of Women. Women may while gain new jobs in the tourism industry, here, as in most other sectors, they are often at a disadvantage. Since they have less control over land and other properties, they find it more difficult to take full advantage of economic opportunities. Being vulnerable, women can also be subject to sexual exploitation.

Pro-poor Tourist Development

While tourism can lead to developmental

problems, these can be resolved or minimized with proper planning and management. Among the priorities should be:

Planning and Support. Governments need to be involved in establishing national and regional parameters for the industry as well as in creating support institutions, such as tourist boards and training institutes.

Infrastructure. This is particularly important in remote regions, where tourism represents one of the few economic development opportunities – though in some cases the lack of infrastructure may be beneficial if it deters mass tourism to environmentally sensitive destinations.

Cultural Diversity. Governments need to protect cultural diversity – allowing local people to participate in the economic benefits of tourism, while protecting their cultural heritage. One of the most remarkable examples of rapid development of infrastructure for tourism is at Angkor in Cambodia (Box 5.15).

Training. Jobs in the industry do not normally require academic qualifications, and in many countries the major hotel groups and travel companies tend to rely on their own inhouse training facilities. This puts smaller enterprises at a disadvantage. Government agencies may, therefore, work with the private sector on training, mentoring and short education courses that will help more people benefit.

Linkages for the Poor. Economic ‘leakages’ need to be examined and, where possible, counteracted. Large tourist operators can, for example, build partnerships with local small- and medium-size enterprises – purchasing local materials, outsourcing laundry and other such services, showcasing handicrafts and creating packages of local excursions. The operators can thus take into account commercial returns, while

BOX 5.15

RAPID TOURIST DEVELOPMENT IN A REMOTE AREA: ANGKOR, CAMBODIA

The Angkor temples near Siem Reap in Cambodia are perhaps the single largest cultural tourism ‘discovery’ in the last decade for Buddhist heritage. After the fall of the Khmer Rouge and the installation of a democratic government and the subsequent opening up of the country, the temples of Angkor caught the attention of the international culture tourist. From scarcely any in the early 1990s, annual international visitor arrivals rose to 561,000 in 2004.

Tourism has changed the economics of the entire region. The town of Siem Reap has seen phenomenal growth in roads and air connectivity. Over the period 1998-2003 the number of hotel rooms increased by 29 per cent per year. Tourism has also spawned hitherto-forgotten industries in stone carving and handicrafts – and boosted many other local enterprises.

This success is attributed to the quality of the temples themselves, the ambience of the area, with its tall leafy trees, and the combined efforts of the Government, the private sector and NGOs. Now a region that had been exporting workers to the rest of the country is importing labour.

Source: Ministry of Tourism, Cambodia 2004; Mahajan and Aibara, 2001.

simultaneously seeking to optimize benefits for the marginalized.

The New Trade in Economic Services

The Asia-Pacific region is in the forefront of the international trade in services – in particular, through international migration, business outsourcing and tourism. But in all these areas policy makers will need to take firm and wide-ranging action to ensure that these dynamic sectors fulfil their potential to promote human development.

For migration, both source country and destination countries can do more to make migration a more productive and fulfilling experience. Source countries can ensure that

migrants are well informed, financed and trained before they depart, and destination countries can make the migration process simpler and more transparent.

For business process outsourcing, governments have a range of policy options to ensure that it makes a stronger contribution to human development, including building infrastructure, training the workforces and ensuring the best regulatory and fiscal environment.

Regarding tourism, many of the problems can be resolved or minimized with proper planning and management – building the appropriate infrastructure, for example, providing training to people working in smaller enterprises, and ensuring better economic links between larger tourist operators and poor communities.