The ECONOMIC CASE for MIGRATION

Migration brings many of the same economic benefits of free trade. It is simply not credible to follow a pro-growth policy whilst, at the same time, remaining hostile to inward migration, argues JONATHAN PORTES

The essence of the economic case for migration is very simple: it is the same as the case for markets in general. If people take decisions on the basis of their own economic self-interest, this will maximise overall welfare.

This applies to where people live and work just as much, if not more, than it applies to buying and selling goods and services.

Of course markets fail here, as elsewhere, and "more market" is not always better. But the view that, as a general proposition, markets are good at allocating resources – including human resources – is widely shared among economists.

And this analogy holds in a narrower, more technical sense as well. The classic argument for free trade, as advanced by Adam Smith, is not just analogous to, but formally identical to, the argument for free movement.

It is easy to see this. In economic terms, if markets are perfect, and we ignore taxes etc, allowing somebody to come to your country and trade with you (or work for you, or employ you) is identical to removing trade barriers with their country.

Clearly, people are not as mobile as goods and services, but migration of people is certainly not trivial as the table below shows.

So what then is the impact of reducing barriers to trade or migration? Theory suggests that, for both trade and migration, the impact of reducing barriers will be positive, but there that will be distributional consequences.

That is, national income (GDP) and average incomes (GDP per capita) will increase, but some individuals and households will lose out, at least in the short run.

In particular, trade will hurt those working in sectors where the UK does not have a comparative advantage, while immigration will hurt those who are in direct competition with immigrant workers.

Hence, the standard economists' policy prescription for immigration is much the same as for trade: liberalise, but compensate the losers.

However – inconveniently for economists, who tend to favour relatively liberal migration policies – there is a problem with this approach.

In standard "static" economic models, to the extent that immigrants are complements to native workers, the impact of immigration on GDP per capita and overall economic welfare is positive but small.

On the other hand, to the extent that immigrants are substitutes for native workers, the impact on national income per capita is essentially zero.

So it is often argued that the economic impacts of migration – positive or negative – are likely to be small, with the main impact being to increase both population and total GDP, but with little medium-to-long-term impact on GDP per capita or unemployment and employment rates.

If this were the case then, while the economic case for immigration would still be valid, it would not dominate, nor would it be an important policy priority.

But this is a very static view of the world. It does not reflect how economies actually work, or where growth really comes from.

To see this, we merely need to return to the analogy with

Figure1

Region	Total number (stock) of migrants 1990 (millions)	Total number (stock) of migrants 2013 (millions)
World	154.2	231.5
Africa	15.6	18.6
Asia	49.9	70.8
Europe	49.0	72.4
Latin America and Caribbean	7.1	8.5
North America	27.8	53.1
Oceania	4.7	7.9

Source: United Nations (2013), Trends in International Migrant Stock: The 2013 Revision

trade. Again, estimates of the gains from trade liberalisation derived from static models are small. So, for example, estimates of the benefits to the UK of completing the Doha round of multilateral trade liberalisation are typically no more than 0.1 per cent of GDP.

But of course most economists believe that the economic benefits of trade are quite considerable, and that these static estimates are not the whole story or even the main point: the benefits are dynamic and arise from competition and specialisation rather than simple static comparative advantage.

We do not gain from free trade in, say, cars with the EU because either we or the French or Germans have a fixed and static comparative advantage in different types of car, so we can produce one type of car better and they can produce another better.

Rather, because trade increases competition between different producers we get diversification of the supply chain and an incentive for technological innovation together with the copying of that innovation. And there are all sorts of other difficult to measure but important effects that increase productivity in the medium-to-long term.

The same is, in principle, likely to be true of immigration. Immigration is likely to have long-term impacts on productivity and growth in a number of ways:

- Immigrants could bring different skills and aptitudes, and transmit those to non-immigrant colleagues (and vice versa)
- Immigration could be complementary to trade in goods and services (because of immigrant networks or for other reasons)
- Immigrants could increase competition in particular labour markets, increasing the incentive for natives to acquire certain skills
- Immigrant entrepreneurs could increase competition and bring new ideas into product markets (one very obvious example being the catering sector)
- Workplace diversity (across a number of dimensions) could increase (or decrease) productivity and innovation

THE STANDARD ECONOMISTS' POLICY PRESCRIPTION FOR IMMIGRATION IS MUCH THE SAME AS FOR TRADE: LIBERALISE…BUT COMPENSATE THE LOSERS

It should be noted that the large number of immigrant entrepreneurs and self-employed people is not necessarily an entirely positive phenomenon.

This could be a result of the fact that they are self-selecting so that enterprising people are more likely to migrate. But exclusion or discrimination might also force some migrants into low-productivity self-employment.

Immigration – the evidence

So, what does the evidence say? Well, in contrast to the well-established economic literature on the impact of migration on labour markets, we have much less quantitative analysis on these topics. What there is does, however, support the arguments above:

- There is a considerable body of evidence in the US that suggests that immigration is associated with increased innovation (for example, that immigrants are more likely to register patents, and that this, in turn, leads to an increase in patent activity on the part of natives). Immigration is also associated with international trade and knowledge transfer, particularly in high-tech industries.
- Here in the UK, my NIESR colleague Max Nathan has written a number of papers on similar topics, particularly focusing on the impact of diversity on innovation, patent behaviour, and other measures of firm performance. This, and work in other European countries, suggests that similar effects are at work.
- It is often hypothesised that immigration reduces the incentive for employees to train native workers. However, in the US, Jennifer Hunt shows that immigration increases the educational attainment of natives. She hypothesises this is because of increased competition in the labour market. Meanwhile, NIESR research for the Migration Advisory Committee found that "rather than migrants substituting for home-grown talent, there is evidence of complementarities between skilled migrants and skilled resident workers".
- While, looking at the macro-economic impacts on growth, and explicitly putting the impact of immigration in the same analytical framework as that of trade, a recent paper by Ortega and Peri found that, looking across countries, the positive impact of immigration on growth has been very large. Indeed, they find that it is considerably larger than the gains from trade. Crucially, the channel through which immigration increases growth is through its impact on total factor productivity, which would not be expected in the standard model.

This research agenda is still in its infancy. We still do not know precisely the channels through which immigration impacts on growth. Nor will we ever be able to put precise numbers on it, any more than we can identify the contribution of Britain's history as a trading nation to our current prosperity. But we do know enough to set a clear direction for policy.

Implications for policy

So what does this mean for UK policy on immigration? The government's general approach in this area is completely at odds with the market-oriented approach generally espoused by UK governments in other economic policy areas for the last three decades.

EVIDENCE IN THE US SUGGESTS IMMIGRATION IS ASSOCIATED WITH INCREASED INNOVATION

It assumes that bureaucrats in Whitehall can, with the help of "expert economic advice", determine what skilled workers the country needs, in what sectors, now and in the future.

It purports to suggest that they know who companies should be able to employ to fill skilled jobs.

For obvious personal reasons (I worked as a civil service economist for 20 years) I have nothing against either Whitehall bureaucrats or economists.

But we do not let them decide how many cars the UK should produce and what colours they should be. Any attempt to do so would rightly be ridiculed as a throwback to the worst excesses of central planning. Why would we try to do the same for people?

Reducing immigration by keeping out skilled workers, stopping students from staying in the UK and generally promoting, in the government's own words, a "hostile environment" for foreigners is economic masochism.

It is simply not credible for the Prime Minister to claim that the UK is "open for business" and for the Chancellor of the Exchequer to say that he is prepared to take the "difficult decisions" to boost growth, while at the same time making the primary objective of immigration policy the reduction of net migration.

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