THE TRANSATLANTIC TASK FORCE ON IMMIGRATION AND INTEGRATION

European Immigration and the Labor Market

Walter Nonneman
Professor of Economics, University of Antwerp

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MPI and Bertelsmann Stiftung have convened a task force to promote thoughtful immigration policies and assess and respond to the profound challenges of integrating immigrants and building stronger communities on both sides of the Atlantic. It addresses its recommendations to European Union institutions and Member State governments, the governments of the United States and Canada, and state and local governments and civil society everywhere.

Introduction: Public Opinion and Politically Correct Standpoints

Public Opinion

The fear that migration inevitably leads to more unemployment is deeply embedded in public opinion, as well as among opinion leaders and policymakers. The Eurobarometer opinion polls that are regularly organized in the EU Member States are informative in this regard. In March 2000, Eurobarometer specifically investigated attitudes toward minority groups in the European Union.[1] The majority (51 percent) of the EU-15 citizens agreed with the statement that "the presence of minority groups causes unemployment to rise." A great many Belgians (probably Flemings more than Walloons) were also convinced of this. Almost two-thirds of Belgians (64 percent) were inclined to agree with this statement. Only the Greeks (85 percent) were more xenophobic in this respect.

In March 2003, Eurobarometer conducted an opinion poll about the expansion of the European Union.[2] This too clearly revealed the public's fear of migration, unemployment, and loss of welfare provisioning.

Approximately 60 percent of Belgians and 64 percent of Europeans feared an influx of people from the new Member States. Nearly half of Belgians (49 percent) feared an increase in unemployment as a result of the expansion. Forty-one percent were convinced that the expansion would erode the welfare system.

In November 2006, Eurobarometer conducted a further opinion poll on European society. This poll reaffirmed the public's fear of the presence of people from other ethnic groups, especially in relation to unemployment. Forty-two percent of EU citizens reported that the presence of people from other ethnic groups causes insecurity, while 46 percent of EU citizens believed that their presence increased unemployment in their country.[3]

More detailed investigation of these Eurobarometer surveys[4] indicates that negative and xenophobic individual viewpoints are closely related to factors such as voting behavior (with voters for right-wing / nationalistic parties and green voters at opposite ends of the spectrum), education (higher education reduces the likelihood of negative views), family connections with people of other races, religions or cultures that reduce the chance of xenophobia (although there are exceptions to this), and episodes of unemployment that reinforce negative attitudes.

In Europe, public opinion has a powerful impact on the formation of national policy. For the career of a politician, a trade union leader, a journalist, or even an academic, it is usually sensible to fall in with common opinion, and adopt "politically correct" standpoints. Corroborating public opinion with arguments and one-liners that rationalize common viewpoints often reaps political rewards. Such arguments from opinion leaders with access to the mass media confirm public convictions in turn.

Complexity, One-Liners, and Political Correctness

The reality of the economic consequences of immigration for the labor market cannot be reduced to simplistic one-liners such as "Holland is full!" Identifying the effects of immigration on the labor market is a subtle and technically complex exercise.

Such complexity derives from the fact that the labor market is intricate and difficult to fathom. It is simultaneously affected by multiple factors, and immigration is just one element among these many influences. In order to discern the effect of migration on unemployment or wage levels, the skein of influences must first be untangled so that the influence of immigration in and of itself can then be assessed.

As this is a technical exercise, in which the methodology partly determines the results, such assessments are always open to doubt. Each evaluation fuels academic debate, and that debate creates the impression that nobody knows exactly what the truth is, with the result that everyone's opinion is regarded as equally reliable.

Because work is the main source of income for many families and therefore has a profound effect on the lives of most people, emotions in the debate about the labor market and labor market policy run high. Much of the discussion about the labor market is disfigured by a priori assumptions and normative judgments that are so pronounced that people suppress realities and refuse to see the mechanisms really involved, because they do not tally with the normative conceptual framework. Discourse about the labor market is therefore beset with codes and taboos. Certain aspects of labor market policy are virtually taboo in political and socioeconomic circles.

Policies are often confusing, too. Typically, governments tend to have not one but several ministers of employment. All parties in a coalition government and numerous ministers want to achieve prominence with employment schemes and measures. Frequently, the result of such efforts is a cacophony of employment measures that are often ineffective, but which cannot be scrapped because different political parties in a coalition government are committed to their particular scheme.

The Complexity of the Labor Market

The labor market is one of the most intricate markets in European economies. Different factors simultaneously affect the demand for workers, the labor supply, the level of wages, and the cost of wages. Attributing changes in unemployment totals or wage levels to a specific factor — such as immigration — is a difficult technical exercise, because one has to be able to check for the influence of other factors. The labor market displays a number of specific characteristics such as its segmented nature and the way in which the "price" (wages) is determined. Additionally, labor carries most of the burden of paying for the welfare system. The demand for labor — job opportunities — is also influenced by globalization of the economy and advances in technology on the demand side. For its part, the labor supply is influenced by demographic developments and leisure preferences, but also the level of welfare provision and benefit payments.

The "Balkan" Labor Market

The labor market consists of numerous segments — a veritable "Balkan peninsula" of professions, sectors, and territories. For example, wage settlements are agreed on for each individual sector, and each sector has its own peculiarities. The numerous different professions vary greatly in terms of educational and training requirements. Regional and local markets all have their own dynamic. A complex process of interchange exists between all segments. Some sectors are closely related, while others are not. In professions that require limited education or training, workers are easily substituted by other workers or by capital. Professions that require lengthy education or intense training are less susceptible to competition and substitution. Highly educated professionals are often deployed with low-skilled or unskilled workers, so that the two sectors are complementary.

Detecting the mechanism of these interactions, feeding them into a model, and checking what effects immigration has in these segments is a complex matter. Moreover, the whole question is complicated still further by the fact that migrants are also a diverse group, ranging from highly educated and sophisticated newcomers from the new EU Member States to uneducated migrants from the developing world through to criminals involved in human trafficking.

The Immobility of European Labor

The European labor market is characterized by territorial fragmentation. Thus the differences in unemployment between Member States of the EU are considerable, while the regional variations within each individual Member State are often even greater. Although there is a clear correlation between the level of economic activity, measured in GDP per head, and the level of unemployment, that correlation is far from perfect. In some wealthy parts of the EU — such as Germany, Belgium, and France — a high average standard of living goes hand-in-hand with substantial unemployment. This points to the pronounced immobility of the European workforce that, despite high unemployment in the local area, is disinclined to resettle in areas with more job opportunities. Less than 0.5 percent of European workers move to a different region every year. This is very little, compared, for example, with the 2.5 percent of Americans who take up residence in a different state every year.

Of the numerous reasons why European workers are so immobile, one is definitely cultural.[5] Language differences are doubtless a major cause of immobility, because they increase the cost of mobility and of maintaining productivity among those who relocate. Belgium is a good example. Labor mobility between Flanders and Wallonia is extremely limited compared with interregional mobility.

Much of the labor immobility in the EU has nothing to do with cultural or historical factors, but is the result of post-war institutional developments and government policies. Social security and welfare provision systems were set up on the basis of national or regional solidarity without mutual coordination. Migrating from one region to another often means losing welfare rights, pension assets, and tax benefits.

Another cause of immobility is wage compression due to centralized collective labor agreements (CLAs). The system of centralized, binding CLAs has priced low-paying jobs out of the regular labor market, yet such jobs are typically a way for newcomers to enter the market. Systems for safeguarding employment — through subsidization, government participation, the prospect of early retirement schemes — encourage employees to stay put in a job that is in any case likely to disappear rather than looking for other work.

There are also plenty of subsidies for inactivity. Generous long-term unemployment benefits, early retirement packages, paid study leave, childcare, subsidized career break schemes, and so on hardly serve to encourage people to look for work, and ultimately contribute to workforce immobility. Raising doubts about such systems — especially in Belgium but also in countries such as Germany and the Netherlands — is politically off-limits and it is very hard to discuss the validity of such systems, although there are numerous circumstances that ought to be prompting reflection and debate.

For example, the Netherlands — with one of the healthiest populations in the world — has over one million people who are "unfit for work" and who receive benefits under the WAO (Work Incapacity Act) system. A recent report by the Belgian National Employment Office shows that over one million Belgians receive unemployment benefit payments. Another example of subsidized inactivity is the Belgian early retirement system, which has produced the lowest proportion of working people aged 50 or over in Europe.

Finally, housing policy is often also a barrier to mobility. Home ownership is encouraged with tax breaks, interest subsidies, or premiums. Those benefits expire if one rents out one's home and takes a job elsewhere. In some countries — including Belgium — high indirect taxes on property purchases or sales are another disincentive to moving house. Again, excessively tight planning regulations or rent controls have brought about a housing shortage in some countries, making people think twice before leaving their homes.

Immobility is definitely one of the salient features of the EU labor markets. As deep-rooted traditions and acquired privileges are at stake, it may be unrealistic to expect this immobility to change much.

Wage-Base Determination and the Rhineland Consultation Model

The labor market is not a true "market" in the sense that wage and employment conditions are determined by the interplay of supply and demand. At market equilibrium, there is neither surplus nor shortage. If the labor market functioned this way, one would have a situation of full employment, or at least no involuntary unemployment.[6]

Of course, the labor market does not operate according to the rules of a competitive market with free price setting. Wage-base determination is heavily influenced by negotiations between organizations representing employers and employees respectively. In the so-called Rhineland consultation model,[7] employers' organizations and trade unions agree on pay and employment conditions. The Belgian model is a multi-step system. An interprofessional agreement between bosses and trade unions sets the framework for collective labor agreements at the sector level, which can be further refined (for larger companies) following negotiations at the business level. Concluded sectoral CLAs acquire — after they have been reported to the government — the force of law, and are binding on all companies in a given sector. As a result, the competitive mechanisms of the market are severely restricted. The unemployed cannot exert pressure on wage levels, and are unable to price themselves back into the market. An advantage of this approach to labor market organization is that anyone working is well protected, but a clear drawback is that, at the low productivity end, people are relentlessly priced out of the regular labor market.

The outcome of consultation depends on the relative bargaining power of employers' and employees' organizations. Trade unions negotiate wage and employment conditions that serve the interests of their members, that is, which protect and increase purchasing power, but that also take account of the increased likelihood that their members will end up losing their jobs if they go too far with their demands. Companies have "the right to manage" and determine the number of people they can profitably employ.

The relative power of the social partners — particularly in interprofessional negotiations — is affected by the government. Depending on the current makeup of the political coalition, the government will tend to throw its weight into one or the other side of the scales. As center - left coalitions prevail in Belgium, there is generally more acceptance of trade union viewpoints than for employer viewpoints. In the negotiating process between the social partners, an agreement is usually reached on the condition that tax or quasi-tax resources be released in order to provide some benefit for workers or companies. The government is thus maneuvered into a position in which it is forced to come up with tax money to ensure the success of the negotiations.

The outcome of interprofessional negotiations in Belgium about the "standard wage" — the increase in wages above the index during the next two years — and the details of

CLAs at sector and business levels are very important for employment, far more important than any effects of immigration.

In the medium term, the proportion of income from work in the total national income is more or less constant.[8] This implies that the overall wage sum that is available in an economy grows in step with the national income.[9] Pay increases above that rate of growth inevitably lead to decreases in employment. It could hardly be claimed that a policy of wage restraint has been conducted in Belgium over the past decades. Part of the destruction of jobs over the past decades is attributable to the prohibitive rise in wages and the cost of wages.[10] However, this is one of the taboo subjects in discussions about labor market policy. Blaming immigrants for the destruction of jobs is accepted more readily in public opinion and by opinion-makers than accusing social partners and government(s) of a lax, opportunistic, and populist income policy.

Globalization

Another factor that has considerable implications for employment in the EU is the globalization of the economy. The dismantling of trade barriers in successive GATT rounds, the creation of trade areas in various parts of the world (NAFTA, Mercosur, the EU), and above all the integration into the world economy of formerly relatively isolated societies (Comecon Block, China, India) combined with technological progress in transport, IT, and communication, have led to global markets. Worldwide markets create possibilities for specialization and more effective exploitation of economic opportunities.

Globalization also brings social costs and risks with it. Opening up markets — especially when this happens suddenly after a period of protection from foreign competition — is often followed by structural changes. Sectors in which there is no comparative advantage shrink back to their efficient core or vanish altogether, while other sectors that do offer a comparative advantage can expand.

Such processes of adaptation produce winners and losers. The losses are usually very obvious, and concentrated in a number of established sectors or large companies; the benefits, though real, are often spread out over numerous sectors, over small businesses or over families. Because the disadvantage incurred by the losers is far clearer than the benefits for the winners, the losers will be more motivated to organize themselves politically than the winners. The media, opinion leaders, policymakers, and public opinion, which are guided by this one-sided protest, will therefore be inclined to oppose globalization, even though its overall impact on society is favorable.

Globalization does make the labor market and the national economy vulnerable to external influences and shocks, however. It is therefore no coincidence that the internationalization of the economy is often accompanied by the development of an extensive network of social security and growing government interference. There is a marked positive correlation between a country's international openness on the one hand, and the government's share in the economy on the other. Among the wealthy OECD countries, the United States, Japan, Turkey, and Canada have the lowest trade figures compared with their national revenue, but also the smallest government share in the economy, whereas countries such as Belgium, the Netherlands, and Luxembourg, whose economies are very open, also have high government expenditure.

In an open economy, that part of the economy that is involved in international trade reacts to changes in competitiveness. The globalization of the capital market, given that investors are only interested in profitable companies and sectors, plays a particular role in ensuring the increased vulnerability of labor income. In global capital markets, national governments also lose their ability to tax capital. All of this increases the income risk for the workforce. As the internationalization of the economy increases, so do the income risk and the demand for a system of social insurance to cover that risk. Dani Rodrik, who has researched the mechanism in detail, calls "the social welfare state [...] the flip side of the open economy."[11]

Financing Social Welfare

The labor market is crucial for the financing of social welfare and solidarity in many European countries. All material prosperity has to be produced, and ultimately the means of production — labor and capital — are the sources of prosperity and solidarity.

The creation of economic prosperity presupposes a productive use of available resources. The workforce and the diversity of talents that are available can only be used efficiently if there are properly functioning labor markets. Wages and wage costs must reflect relative scarcity, so that they are good and reliable guidelines for companies' location and investment policies and families' decisions about participating in the labor market. When wages (and wage costs) — the result of historical developments such as institutionalized wage determination by inflexible consultation structures — no longer correspond to labor productivity, jobs are inevitably lost as are whole sectors and a loss of economic prosperity results. In regions with a large labor surplus but high statutory wages negotiated in agreements, new investors and companies are not attracted, meaning that families are doomed to unemployment, in some cases across multiple generations.

The cost of national solidarity is defrayed almost exclusively via the labor market. Although taxes are often collected by companies — corporate tax, value-added tax (VAT), social security contributions, and so on — every form of tax is nonetheless ultimately borne by the owners of the factors of production. The least mobile production factor bears the lion's share of the burden. Labor is all but internationally immobile, so that tax or quasi-tax charges can be made on income from labor at the national level on a long-term basis. With the exception of a few forms of capital such as land, property, etc., capital is very hard to tax or can only be taxed on a limited basis in the national context, because investors can search the world for a high expected return in the long term. Wage cost differences between regions and countries — either through differences in net wages or through differences in tax pressure — are able to persist because only a limited number of workers will decide to migrate. There is therefore little need for international coordination of labor costs and labor taxes to enable taxes to be levied on labor. However, investors react very quickly to differences in national returns due to taxation. Tax revenue on capital can only be generated by means of international agreements, harmonization, and the coordination of information. Solidarity is therefore essentially financed by the labor market.

The degree of solidarity in European countries varies somewhat, but on average, the amount of income redistributed by the government is close to half of the GDP of a country. The Scandinavian countries lead the field with total tax revenues of between 55 and 60 percent of GDP. Belgium, France, Austria, Germany, Italy, and the Netherlands lie between 45 percent and 50 percent. The United Kingdom, Ireland, and newcomers to the EU are on the low side (35-40 percent). There are also quite a few differences in the way in which taxes are raised. In some countries such as France, Belgium, Germany, and the Netherlands, much taxation is raised directly on labor income through social security contributions, whereas in others, it tends to be collected via personal tax (Denmark, Sweden) and indirect taxes. However taxes are raised, the system of solidarity between workers and non-workers is ultimately paid for by the immobile production factors, in other words, predominantly by labor.

The Shadow Economy

Such high levels of tax pressure — particularly when taxes are raised directly on labor via social security contributions and personal tax — constitute a considerable incentive for irregular and illegal employment. High taxes, coupled with compressed, uniform wages that take no account whatsoever of local conditions, make the gray and black markets particularly attractive to both employers and employees. For employees with low productivity — unskilled newcomers lacking experience — the shadow economy is often the only way of pricing themselves into the market. For the least profitable companies or sectors, the shadow economy is often the only way of surviving.

Despite the disincentives against the shadow economy — that is, the anticipated cost if one is caught and punished and the "psychological cost" associated with dishonest behavior — the volume of business and employment is substantial. The extent of the shadow economy in the EU is estimated at approximately 20 percent of GDP and employment within it is estimated at 12 percent of official employment. The extent of the shadow economy in Belgium is thought to be between one-fifth and one-quarter of GDP.[12]

Not all countries with high levels of taxation have an extensive shadow economy. Cultural differences and differences in the rate of detection and penalization account for differences of activity level. For example, the Scandinavian countries have a very limited shadow economy, partly for cultural reasons but also partly as a result of very tight social controls by both employers and unions.

Immigration and Labor Market Effects

In the economic literature, there are numerous studies measuring the effects of immigration on national unemployment and pay levels.[13] The majority of these relate to the United States, but there is also some European research, especially for the Netherlands and Germany due to the availability of sound data and databases. Various methods are used to investigate these labor market effects.

Natural Experiments

So-called natural experiments, such as the "Mariel Boatlift," the Algerian exodus to France in 1962, the return of Portuguese from Angola, and above all, the emigration of Russian Jews to Israel in the early 1990s are of particular interest in evaluating the effect of sudden migrations on the labor market.

In 1980 Fidel Castro decided that Cubans who wished to migrate to the United States could leave from the port of Mariel. In a short time, 125,000 mainly unskilled Cubans left Mariel for Miami. Half of these migrants settled there permanently. The Mariel Boatlift, as this sudden wave of migration is called, increased the working population of Miami by 7 percent and the number of Cuban workers by one-fifth. Research by Card[14] shows that negative effects (on wages and job opportunities) were mainly experienced by Cubans already living in Miami, but that there were no discernible negative effects on the other population groups — whites, blacks, and other Hispanics. The majority of these Cuban newcomers were completely absorbed after some time into the textile and clothes-making sector in the Miami region, without any particular consequences for the labor market.

As a result of Algerian independence, in 1962, some 900,000 relatively highly skilled Europeans departed for France. This meant a sudden increase of about 2 percent in the French working population. Most of these newcomers settled in the south of France. Hunt[15] found relatively limited effects on wages and employment for those regions that had experienced a high influx of newcomers. An increase in the working population of 1 percent in a region led to a 0.2 percent rise of unemployment among French-born workers and a fall in the same group's average wage level of 0.5 to 0.8 percent.

A similar study investigated the consequences of the settlement in Portugal of 600,000 Angolans when Angola gained its independence. Carrington and Lima,[16] who performed the study, came to the conclusion that this influx had scarcely any consequences for the labor-market position of those born in Portugal.

The migration of over 700,000 Soviet Jews to Israel in the period 1990-1997 is one of the most important natural experiments. Most of these migrants were highly skilled, and the influx increased the working population of Israel by 15 percent. Cohen and Hsieh[17] studied the short-, medium-, and long-term consequences. In the short term, real wages fell substantially, whereas real profits increased. In the medium term, the influx of newcomers led to an investment boom. In the long term, wages and profits returned to their pre-migration levels.

Econometric and Other Models

Such natural experiments are obviously rare. In many cases, immigration amounts to an influx of restricted scope that varies from year to year. Migrants also spread out geographically, so that there is also a certain variation in their influx across different regions, despite the fact that most migrants settle in urban areas. These annual and regional variations are used in econometric studies to check whether there is a link with variations in unemployment or wage levels among the native-born population as a result of the increased "competition" on the labor market.

The most common studies are area analyses, which investigate whether more migration in a given region leads to an increase in unemployment or a drop in real wage levels. Most of these studies are based on American data, but a number of studies have also been done for Germany.[18] Here too, it is often the case that very few effects are found, if any. The effects found in the United States are usually insignificant wage effects; in Germany, the wage effects are nil, but more immigration does have minor effects on unemployment.

Recent doctoral research by L. Okkerse into Belgian household data (PSBH [Panel Studie van Belgische Huishoudens, Study Panel of Belgian Households]) has produced similar results for Belgium. The effects of more immigration to a particular region (*arrondissements*) on wage levels are nil, but increased competition on the labor market does lead to a slight rise in short-term unemployment. The area analysis methodology can be used to check whether these effects are temporary or long-term. Investigations using a calculable general equilibrium model point in this direction.[19]

Another category of studies assesses the econometric production functions from which the demand for production — various sorts of labor such as native (higher) skilled labor, ethnic minority (lower) skilled labor, and capital — is derived. This makes it possible to estimate the degree of complementarity and subsidiarity of production factors, and, for example, to simulate the consequences of an influx of low-skilled immigrants.

Most (American) studies detect limited effects on the wage level among native-born workers, with greater effects on the wages of earlier migrants. Finally, there are also simulation models of various types. Partial equilibrium models look at the labor market alone, whereas general equilibrium models also take account of the interdependencies between the labor market and the rest of the economy. Such models are usually statistical, and enable the long-term consequences of different levels of migration to be assessed, whereas dynamic models attempt to establish the pattern of adjustments over time. For Belgium, a number of simulations have been performed on the basis of a standard growth model.[20] These show that relatively significant changes in the influx and quality (educational level) of migrants (from 10,000 to 65,000 per year) lead to very restricted effects on income per capita (-1.5 percent to 2 percent) and effective wages (-2.9 percent to +0.8 percent), even after several decades.

Looking through these studies, one arrives at the following conclusions. Firstly, no single research method is beyond criticism. Yet despite the differences in method, the results are often along the same lines, and the identified effects of migration on unemployment and wage levels are quite limited. In overall terms, the effect on prosperity is often positive. There is often also a redistribution effect. Those owning production factors that are complementary with migrant labor — such as capital owners and the highly educated — benefit from immigration while those possessing production factors that compete with migrant labor — the unskilled, and especially earlier migrants — lose out. In the short term, immigration usually has negative consequences — a rise in unemployment, wage pressure on markets with flexible pay, more welfare provisioning — but in the medium and long term, the influx of new labor contributes to economic growth.

Benefits of Immigration[21]

Immigration and Growth

As a rule, and if all other factors are equal, greater deployment of labor means more economic prosperity. It is no surprise that those countries that have admitted the most immigrants are among the wealthiest and fastest growing in the world. Traditional immigration countries such as the United States, Canada, Australia, and South Africa are examples of development and economic progress through immigration.

Economic prosperity needs to be maintained, and this presupposes the deployment of production factors — labor and capital — in an efficient manner. Technological progress, investment in smarter, more effective machines and production techniques, and investment in education and training increase labor productivity or the output per hour of work. But high labor productivity is not enough to keep the growth engine running. The number of working hours actually used is also of importance. More immigration — especially migrants of working age — means more hands and more growth, and growth is essential to maintain Europe’s welfare state.

The importance of the number of workers for economic growth is indicated by the developments of the last few decades. Until the late 1980s, there was a certain degree of convergence in economic prosperity per head among the wealthiest countries in the world. In the 1990s, that convergence came to an end. The income per head in the euro zone is now approximately 30 percent lower than in the United States. Despite this, European countries rate just as highly in terms of labor productivity or output per hour worked. They certainly concede no ground to the United States in terms of labor productivity. Belgium, incidentally, is the absolute leader in the rankings for GDP per hour worked. To an extent, these positive figures are attributable to the fact that only highly productive workers in Europe can stay in the labor market, while those with fewer skills and less knowledge are priced out of the labor market.

The big difference in total productivity is the result of differential participation in the labor market. The level of activity of the working-age population is considerably lower in Europe than in the United States, and within the EU, Belgium has one of the lowest rates of participation. Seventy percent of all women work in the United States; in the EU-15, that figure is approximately 60 percent.

The retirement of older employees is the main cause of the difference. In the United States, 62 percent of people between 55 and 64 work. In the EU-15, the proportion is just 45 percent. Belgium has the lowest participation rate with a mere 29 percent. Older citizens' low rate of participation in the European labor market may be partly the result of cultural factors and preferences, but it is largely because of policy. The generosity of the pension system, with its low retirement age, early retirement systems, long-term unemployment benefit payments, and so on make working unattractive for older people. The OECD recently calculated the "implicit" rate of tax on working after the age of 55, i.e., the substitute income one could receive "without working" expressed as a percentage of the average labor income one could earn "by working." These findings indicate that the average Belgian faces an implicit tax rate of 80 percent if he continues to work after 60. For the average Dutch person, the implicit tax rate is 90 percent.

Acquired privileges and habits are slow and difficult to change. Moreover, pegging back pension and other social benefits, even for newcomers, is especially politically unpopular. Although the "end-of-career issue" is on the agenda of virtually every European government, few calls are being made for the rate of participation of older citizens in the labor market to be increased. It looks as though the effective use of Europe's labor resources is unlikely to increase dramatically, and, despite productivity gains, this trend will continue to depress economic growth in Europe.

Nor is this state of affairs fully acknowledged or taken seriously in political debate. European governments often fail to address labor market issues head on by focusing on technological development and innovation, a more politically attractive agenda. This emphasis on R&D and innovation — which is supposed to solve problems such as ossification and stagnation like a deus ex machina — is often a pretext for not talking about Europe's real problems, namely low levels of activity and labor participation as a result of systems of welfare provision for which a very high price is paid in terms of forgone economic prosperity, underutilization of economic and human potential, and involuntary unemployment in particular.

Immigration — especially of people of working age — increases the potential workforce and can partly compensate for the low participation of the native population. More hands on deck ultimately means more economic growth and prosperity.

Labor Mobility and Immigration

As indicated earlier, workforces in the EU are immobile. If wages were flexible and adapted to market conditions, this immobility would not constitute a problem. In regions with a surplus of labor and substantial levels of involuntary unemployment, wages would fall to a level of full employment; in regions with a shortage of labor, wages would climb. Wage differences between regions would be an expression of the relative scarcity of labor. Companies would take this into account in choosing their location and selecting their investment policy, and as wages are a reflection of relative scarcity and productivity, this management process would take place efficiently.

To an extent, such an adaptation process can be seen within the enlarged EU. The hourly wages in Western European countries are five to ten times higher than in the new Eastern European EU Member States. Many businesses are relocating a number of their activities to the new Member States. In particular, industrial activities with low added value are now being outsourced to Central and Eastern European businesses. This is leading to the dismantling of industrial employment in Western Europe, but is also forging new possibilities for Western European companies to take on international competition — especially the new industrial giants China, India, and emergent low-wage countries in Asia.

Wage inflexibility and restrictions on hiring and firing workers are thought to account for the fact that job loss in Western Europe resulting from the shift in employment to Central and Eastern Europe is not being offset by other companies and sectors. At first sight, measures against dismissal and CLAs that make pay cuts virtually impossible appear laudable from the social viewpoint, but in many cases these protective measures lead to social disaster. Companies that are forced to adapt to a competitive market and that are unable to internalize these new conditions through rescaling or a gradual shift to activities with higher added value are often compelled by employment-related liabilities and employee protection into bankruptcy or closure, causing the entire business to go under.

At the national level, the immobility of the workforce, coupled with wage compression and uniform wages despite pronounced regional variations, lead to both persistent cores of unemployment in some areas and labor market shortages in others. Regional differences in unemployment between EU Member States, but above all within national Member States, are considerable. The compression of the wage range usually leads to wages going up on the bottom rung of the ladder, resulting in very high levels of unemployment among relatively unproductive workers, even in regions with a shortage in the labor market. Structural deficiencies and undermanned professions are not compensated for, because the level of wages stipulated by CLAs is insufficient to attract the right workers. In other regions, workers are unable to find work because the cost of wages is far too high compared with the productivity or added value that they can contribute. Such a situation leads to considerable loss of prosperity. There are economically viable jobs that are not taken due to labor shortages, and at the same time there are workers who are willing to work and who are potentially productive, but who are involuntarily unemployed: The jobs and the workers are both in the wrong location. No adjustment takes place, even in the long term, because the wages do not give the right signal to companies to relocate.

Immigration compensates for some of the rigidity of our labor markets and for the immobility of EU workers. Immigrants lubricate the wheels of the EU labor market, so to speak.[22] Non-EU citizens staying in the EU and immigrants are far more mobile than the rest of the EU working population. On the basis of European panel data on families, approximately 7 percent of non-EU citizens working in the EU seem to move house every year, whereas the total among EU citizens is just 0.6 percent. Immigrants are thus over ten times more mobile than EU citizens, and are thus really the oil in the machinery of the EU labor markets.

Non-EU citizens and immigrants also respond to shortages and surpluses in the labor market. Tito Boeri has documented the migration from Central and Eastern Europe to Germany in detail. His calculations show that migrants from these countries skip over the east German *Länder*, where unemployment is very high, and settle in western or southern Germany (Bavaria), where the job prospects are far better. It is widely known that immigrants prefer urban areas to more rural areas, as there are more job opportunities in an urban environment. Asylum seekers also move to countries and regions where unemployment among low-skilled workers is lowest, as is apparent from the correlation between the number of asylum seekers per 1,000 inhabitants and the level of unemployment among the low-skilled and young people.

The Use of Immigrant Labor

Many people believe that there is a fixed quantity of labor to be shared among a workforce of a given size. According to this view, work is given to one person at the cost of another. The specialist literature calls this assumption the "lump of labor fallacy." The same faulty logic is used by the advocates of shorter working hours, who hold that divvying out work is a way of getting more people to work. The labor market does not work in this way. Shorter working hours with the same weekly or monthly pay increases the unit cost of wages and reduces the total quantity of labor, which is precisely the opposite of what such changes intend to accomplish.

Each immigrant entering the country, as well as being a job seeker, also provides work to others because he or she is a consumer and user of all kinds of services and supplies. Each new citizen — whether born in an EU country or an immigrant — creates demand and hence work. There is no systematic connection between size or density of population and economic prosperity. The world's richest countries are in many cases among the most densely populated, and there is no reason to assume that more migration is damaging to economic prosperity. The quantity of work changes not just with the demand for goods and services but also with the cost price of labor — the cost of wages. The labor market has a dual character in many EU countries.

Many immigrants find their way onto the bottom rung of the primary labor market via the gray (or black) market, and their work creates opportunities for employees in the primary market. In Europe, a great many unskilled workers — day laborers, fruit-pickers, temporary workers, construction workers, cleaning staff, domestic staff, hotel staff, kitchen staff, and so on —find jobs in specific labor market regimes on the fringe of the official market or in irregular (illegal) regimes in the shadow economy. Such jobs — dirty, dangerous, and ill-paid — are often shunned by EU citizens. A wide range of factors, including a certain degree of over-qualification due to over-subsidized education, alternative income possibilities, and social prestige contribute to this phenomenon. Virtually all developed countries face a shortage of employees who are prepared to perform manual labor as construction workers, dockers, cleaning staff, and so on. Often, it is only newcomers who are prepared to take on these jobs.

This type of work is often complementary with many primary professions. For instance domestic staff, restaurant staff, and shop staff create opportunities for highly educated women to participate in the labor market. In many sectors, low-skilled labor is complementary to highly skilled labor. Low-skilled workers, often immigrants, are often required to sustain jobs for highly skilled workers. Especially old sectors subject to fierce international competition, such as steel, textiles, and basic chemicals, require cheap immigrant labor to maintain their competitiveness. Without this labor, companies in these industries are compelled to outsource or relocate internationally.

Here again, the institutional organization of the labor market is the cause of many problems. Wage compression, especially in the lower echelons, makes taking low-grade jobs unattractive and encourages a shadow market. Proportional social security contributions — without any exemption at the lower end of the wage scale — make even low-waged labor expensive and also do not help encourage legal employment among the low-skilled. The high cost of dismissal creates a considerable disincentive against new or temporary recruitments, and makes companies extraordinarily cautious about exploiting expansion opportunities.

Immigration as a Tax on Immobility and Inflexibility

Another outcome of research (although not always clear) is that non-EU citizens tend to settle in countries with more generous welfare systems, such as Belgium, Denmark, the Netherlands, Austria, and France. For example, there is a high correlation between the number of asylum applications per 1,000 inhabitants to EU Member States and the payments per capita in family and child allowances and unemployment benefits in the EU-15.

In most EU countries, non-EU citizens are also over-represented in unemployment benefits and family or child allowance payouts.[23] This does not necessarily indicate that immigrants see unemployment benefit or welfare provision as a cozy option. For instance, Dutch research has found that unemployment among newcomers falls after a few years from its initial high level to an average level comparable with that of Dutch people. The use of benefits by newcomers peaks some time after their arrival in the country, and subsequently falls to an average level. It takes less than five years before newcomers find their way from social welfare payments to the labor market.

On average, however, immigrants and non-EU citizens do make more use of the welfare provision, in the short term at least. Obviously, EU citizens are not happy about this tax burden, just as they have a dislike for most taxes for which they are unable to see an immediate return. Nevertheless, the returns on this extra expenditure caused by immigration are real. Immigration and the costs it gives rise to through a temporary increase in welfare payouts may be regarded as a tax on the immobility of European employees. It is the price EU citizens must pay for immobility and to avoid a slow-growing, sluggish economy due to a poorly functioning labor market.

Lessons for Immigration Policy

Immigrants play an essential role in the European labor market. They represent the only grease for coaxing a bit of movement into the creaky European labor markets. Some economists therefore, including this author, argue that the closed-door immigration policy operating in the EU should be repealed. The immigration policy that has been in place over the past two decades in many European countries is irrational and ineffective. The front door has been all but closed to authorized migrant workers, while at the same time the side doors have been left ajar through family reunion and the back doors have been wide open to illegal (or irregular) migration. Family reunion and illegal migration offer more opportunity for low-skilled people to immigrate; as a result, immigration has become unpopular, because when it consists of low-skilled workers it weighs more heavily on the labor market and the welfare system.

From the same viewpoint, there are calls from some quarters for a change in policy, re-opening Europe to authorized but selective labor migrants. Some argue in favor of a combination of restricted, conditional, and gradual access to the social security system, coupled with a selective migration policy comparable with the Canadian or Australian points system. At the same time, some urge shifting the responsibility for immigration policy from the national level to the European level. They expect that a supranational authority would be more resistant to pressure from public opinion, which is often manipulated by nationalistic populists.

Such proposals seem reasonable, but are of course not without their difficulties. Selective immigration with a points system that is primarily aimed at the highly educated inevitably leads to a brain drain effect, depleting poorer countries of essential human capital. Restricting access — even temporarily — to the social security system is discriminatory, and can result in serious minority problems. However, entrusting migration policy to the European authorities, who would then have to act as lightening rods for negative public opinion, is hardly conducive to promoting European cohesion and collaboration, and would further reinforce the European democratic deficit.

In any case, the restrictive policy presently conducted by the European Member States is not very effective. It is unrealistic to believe that illegal or irregular migration can be reduced or kept in check. In the EU — especially after its expansion — levels of tolerance for the unauthorized vary greatly. Effective border controls are enormously difficult to organize because of the length and variety of the borders. Moreover, the political will to maintain tough border controls varies greatly from one Member State to the next. A restrictive migration policy is therefore ineffective, and migration flows are determined by push and pull factors rather than by stricter border controls. Restrictive measures merely ensure that legal migration is replaced by illegal forms of immigration, and have far less effect than expected. Moreover, a restrictive policy has the effect of creating a market for criminals, who get rich from human smuggling and human trafficking.

A restrictive policy — virtually ineffective, but popular with large groups of European voters — is based on faulty perceptions of the scope of immigration. By historical standards, migration today is very restricted. Its absence from the contemporary process of globalization is conspicuous. In the early 20th century, migration flows were far more significant due to the convergence of capital-rich and capital-poor countries. Migration from southern to northern Europe played a key role in the process of European integration in the 1950s and 1960s. During these periods, migration was far more extensive than it is today, in both absolute and relative terms.

Sadly, this is not in line with public perceptions, which have become increasingly xenophobic. The sources of this increase in xenophobia make an interesting topic for research. One of the main causes is persistent, structural, rising unemployment, for which foreigners, immigrants, and ethnic minorities represent easy scapegoats. The true cause, however, lies in the ossification of the labor market in "old" Europe and the lack of political will to tackle this issue effectively. Reforms to the labor market, coupled with a more realistic system of social security, are indispensable if we are to avoid laying the cost of six million unemployed in Germany, one million in Belgium, and so on at the feet of the newcomers in European society.

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ENDNOTES

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2 Eurobarometer (2003), "Enlargement of the European Union — Flash Eurobarometer 140." EOS Gallup Europe (March), 85.

3 Eurobarometer (2007), "European Social Reality – Special Eurobarometer 273." TNS Opinion & Social, (February), 68.
http://ec.europa.eu/public_opinion/archives/ebs/ebs_273_en.pdf

4 Thalhammer et al. (2001), "Attitudes towards Minority Groups in the European Union."

5 Michael Burda describes Europe as " … a tribal mosaic … consisting of a great many individual sociological identities, peoples living alongside each other, identifying more or less exclusively with one of a great many parallel histories," in Tito Boeri, Gordon H. Hanson, and Barry McCormick, eds. (2002), *Immigration Policy and the Welfare System* (Oxford: Oxford University Press), 152.

6 Full employment does in fact include some unemployment, i.e., voluntary unemployment, where people voluntarily decline to accept a job at the current wage because, for example, they are looking for a better job or another job, or to take time to attend training, etc. Involuntary unemployment — the socially problematic form of unemployment — refers to a situation in which there are workers who would accept a job at the current wage, but cannot find one.

7 This term is often used to describe the organization of the labor market in Belgium, the Netherlands, and Germany, although there are considerable differences between these countries.

8 This amounts to a wage elasticity (in the medium term) of around -1: i.e., a 1 percent wage increase leads to a 1 percent fall in employment, all other factors being equal (ceteris paribus).

9 The growth of the Belgian economy's potential income is around 2 percent.

10 In 1996, the government of the time even decided to impose a wage policy by introducing a statutory standard wage. This measure was temporarily intended to prevent higher taxes and economy measures precipitated by the clean-up of public finances in the run-up to the introduction of the euro resulting in high compensating wage claims and leading to the destruction of jobs. Although this legislation has now been rendered redundant and is even counterproductive, nothing appears to be as permanent as a temporary measure.

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12 Friederich Schneider and Dominik Enste (2002), *The Shadow Economy: An International Survey* (Cambridge: Cambridge University Press).
13 For a readable overview see L. Okkerse (2003), "In Search of the Impact of Migration on the Labor Market," *Economisch en Sociaal Tijdschrift* 2: 163-189
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20 W. Nonneman and L. Okkerse (2002), "Migration and the Job Market," *Economisch en Sociaal Tijdschrift* (1): 3-31
21 A well-argued overview of the economic benefits of migration can be found in P. Stalker (2001), *The No-Nonsense Guide to International Migration* (Oxford: New Internationalist Publications), 63-99.
22 T. Boeri, G. Hanson, and B. McCormick (2002), eds., *Immigration Policy and the Welfare State* (Oxford: Oxford University Press).
23 For a recent study of the labor market position of immigrants in Belgium, see L. Okkerse and A. Termote (2004), "Hoe vreemd is vreemd op de arbeidsmarkt? Over de allochtone arbeidskrachten in België [How alien is alien in the labor market? On the alien labor force in Belgium]," Statistische Studiën nr 111, Nationaal Instituut voor de Statistiek.

About the Author

Walter Nonneman

Walter Nonneman is professor of economics at the University of Antwerp (UA), Belgium. He studied business economics at the Saint-Ignatius College (UFSIA) and obtained his PhD from UA in 1976. He has published in *The Quarterly Journal of Economics, Social Science & Medicine, Health Policy, Applied Economics, Economics of Education Review, The International Journal of Technology Assessment in Health Care, The Journal of Transport Economics & Policy*. He has held various administrative positions at his university (director, president) and in government (ministerial advisor, Chief of Staff of the Belgian Prime Minister). He is a non-executive board member of a financial holding company and several non-profit institutions. His current research interests are the economics of migration and terrorism.