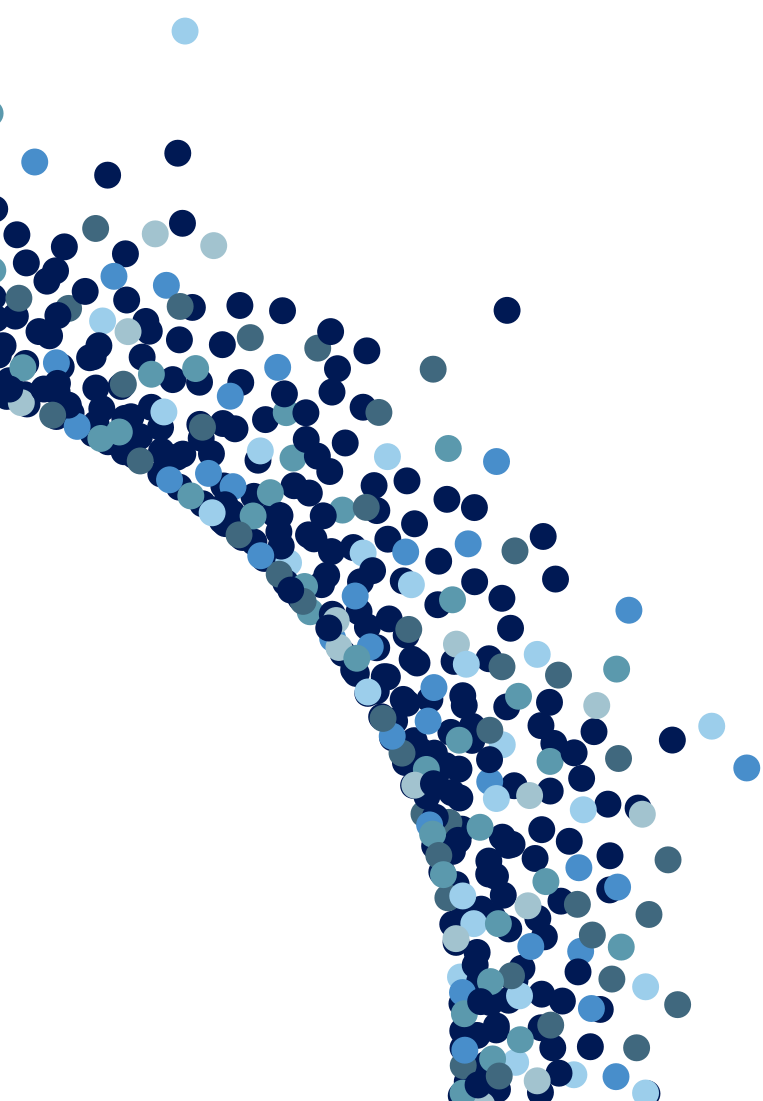




# BRIEFING

## The Labour Market Effects of Immigration



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## **This briefing discusses the impacts of immigration on the labour market in the UK, focusing on wages and employment.**

### **Key Points**

The impacts of immigration on the labour market critically depend on the skills of migrants, the skills of existing workers, and the characteristics of the host economy. Research evidence on the labour market effects of immigration is thus always specific to time and place.

UK research suggests that immigration has a small impact on average wages of existing workers but more significant effects along the wage distribution: low-wage workers lose while medium and high-paid workers gain.

The wage effects of immigration are likely to be greatest for resident workers who are migrants themselves.

Research does not find a significant impact of overall immigration on unemployment in the UK, but the evidence suggests that immigration from outside the EU could have a negative impact on the employment of UK-born workers, especially during an economic downturn.

For both wages and employment, short run effects of immigration differ from long run effects: any declines in the wages and employment of UK-born workers in the short run can be offset by rising wages and employment in the long run.

### **Understanding the evidence**

The outcomes of any study of the impacts of immigration depend on how “migrants” are defined. All available research studies on the labour market effects of immigration in the UK define migrants as foreign-born persons (for a discussion of alternative definitions, see the briefing ‘Who Counts as a Migrant?’).

It is important to distinguish between the effect of immigration on the average wage of all workers in the economy, and on the wages of different groups of workers along the wage distribution (e.g. low, medium and high-paid workers). It is possible, for example, that immigration leads to a rise in the average wage of all workers, but to a fall in the wages of some low-paid workers. Similarly, immigration may not affect the overall employment outcomes of existing workers, but it may impact on the employment outcomes of specific educational groups.

## **In theory, the impacts of immigration on wages and employment of existing workers critically depend on whether and to what extent migrants' skills are complements or substitutes to the skills of existing workers, and on how immigration affects the demand for labour**

The impacts of immigration on the labour market critically depend on the skills of migrants, the skills of existing workers, and the characteristics of the host economy. They also differ between the short and long run when the economy and labour demand can adjust to the increase in labour supply. The immediate short run effects of immigration on the wages and employment of existing workers depend particularly on the extent to which migrants have skills that are substitutes or complements to those of existing workers (e.g. Borjas 1995). If the skills of migrants and existing workers are substitutes, immigration can be expected to increase competition in the labour market and drive down wages in the short run. The closer the substitute, the greater the adverse wage effects will be. Whether and to what extent declining wages increase unemployment or inactivity among existing workers depends on their willingness to accept the new lower wages. If, on the other hand, the skills of migrants are complementary to those of existing workers, all workers experience increased productivity which can be expected to lead to a rise in the wages of existing workers.

In addition to expanding labour supply, immigration can also increase the demand for labour. Migrants expand consumer demand for goods and services. In the medium to long run, immigration can be expected to lead to more investment. Both effects result in greater demand for labour and thus increased wages and employment in the economy. In other words, the number of jobs in an economy is not fixed (the "lump of labour fallacy"). Immigration can increase competition for existing jobs but it can also create new jobs. The extent to which investment and labour demand respond to immigration depends on the characteristics of the economy. During an economic downturn labour demand may respond more slowly than during times of economic growth.

Changes in wages and employment are not the only ways in which an economy responds to immigration. There are at least two other adjustment mechanisms (see e.g. Dustmann, Glitz and Frattini 2008). First, immigration may change the mix of goods and services produced in the economy and thus the occupational and industrial structure of the labour market. For example, the immigration of low-skilled workers may expand the production (provision) of certain products (service) that use low-skilled labour intensively. The expansion of the sector will then increase demand and drive wages back up. Similarly, immigration may change the technology used for producing (providing) certain products (services). For example, the immigration of skilled workers may encourage innovation and the adoption of more skill intensive technologies which would again affect labour demand.

A key insight from these theoretical considerations is that the impact of immigration on the wages and employment opportunities of existing workers is always specific to time and place. This means that the results of empirical research always only apply to the time and place under consideration.

The impacts of immigration on the labour market in the UK were reviewed in two relatively recent government studies by the Department for Business, Innovation and Skills (Devlin et al 2014) and by the Migration Advisory Committee (MAC 2012).

## **UK studies find that immigration has small impact on average wages but more significant impacts along the wage distribution: low-waged workers lose while medium and high-paid workers gain**

Empirical research on the labour market effects of immigration in the UK suggests that immigration has relatively small effects on average wages but more significant effects along the wage distribution, i.e. on low, medium and high paid workers.

Focusing on the period 1997–2005 when the UK experienced significant labour immigration (see our briefing ‘Migrants in the UK Labour Market’), Dustmann, Frattini and Preston (2013) find that an increase in the number of migrants corresponding to 1% of the UK-born working-age population resulted in an increase in average wages of 0.1 to 0.3%. Another study, for the period 2000–2007, found that a 1% increase in the share of migrants in the UK’s working-age population lowers the average wage by 0.3% (Reed and Latorre 2009). These studies, which relate to different time periods, thus reach opposing conclusions but they agree that the effects of immigration on average wages are relatively small.

The effects of immigration on workers within specific wage ranges or in specific occupations are more significant. The greatest wage effects are found for low-waged workers even though those effects can be considered relatively small. Dustmann et al (2013) find that each 1% increase in the share of migrants in the UK-born working age population leads to a 0.6% decline in the wages of the 5% lowest paid workers and to an increase in the wages of higher paid workers. Another study focusing on wage effects at the occupational level during 1992 and 2006, found that, in the unskilled and semi-skilled service sector, a 1% rise in the share of migrants reduced average wages in that occupation by nearly 0.5% (Nickell and Salaheen 2008). They also find the same effect in an updated paper, in which they consider the period from 1992 and 2014, however in this extended period the average wage reduction for the unskilled and semi-skilled service sector is just under 0.2% (Nickell and Salaheen 2015).

The available research further shows that any adverse wage effects of immigration are likely to be greatest for resident workers who are themselves migrants. This is because the skills of new migrants are likely to be closer substitutes for the skills of migrants already employed in the UK than for those of UK-born workers. Manacorda, Manning and Wadsworth (2012) analyse data from 1975–2005 and conclude that the main impact of increased immigration is on the wages of migrants already in the UK.

### **Research does not find a significant impact of overall immigration on unemployment in the UK, but the evidence suggests that immigration from outside the EU could have a negative impact on the employment of UK-born workers, especially during an economic downturn**

Does immigration create greater unemployment or greater inactivity among existing workers? The first systematic study of this issue used data for 1983–2000 to analyse how changes in the share of migrants impact on employment, labour market participation and unemployment of existing workers (Dustmann, Fabbri and Preston 2005). It concluded that immigration had no statistically significant effect on the overall employment outcomes of UK-born workers. The study did, however, find statistically significant effects on specific educational groups of UK-born workers: immigration was found to have adverse effects on employment, labour market participation and unemployment of UK-born with intermediate education (defined as O-level and equivalent) and a positive impact on employment outcomes of UK-born workers with advanced education (A-levels or university degrees).

A separate study carried out by researchers at the Department of Work and Pensions (DWP) analysed the impact of labour immigration of A8 workers on claimant unemployment during May 2004–November 2005 (Lemos and Portes 2008). The study found little evidence of an adverse effect. There is some evidence to suggest that, just like the impact on wages, the effects of immigration on unemployment differ between the short and long run. An OECD study of the impact of immigration on the unemployment of domestic workers in OECD countries (including the UK) during 1984–2004 found that an increase in the share of migrants in the labour force increases unemployment for those with skills most similar to the migrants in the short to medium term (over a period of 5–10 years), but that immigration has no significant impact on unemployment in the long run (Jean and Jimenez 2010).

Two recent studies have provided additional insights on the impact of immigration on employment in the UK using a time period which includes the latest recession. Lucchino, Rosazza-Bondibene and Portes (2012) used National Insurance Number (NINO) registrations data from 2002 to 2011 to explore the impact of immigration on claimant

count rates (i.e. a proxy for unemployment) in 379 local authorities in England. The results suggest that there is no impact of immigration on the claimant count rate. This result holds even during periods of low economic growth or recession.

Research by the Migration Advisory Committee (MAC) studied the impact of migrants on the employment of UK-born people using data from the Labour Force Survey (LFS) for 1975–2010 (Migration Advisory Committee 2012). The study suggests that, overall, migrants have no impact on UK-born employment. However, the MAC also analysed the specific impacts of EU and non-EU migrants and also distinguished between two sub-periods: 1975–1994 and 1995–2010. It found that non-EU immigration was associated with a reduction in the employment of UK-born workers during 1995–2010. No statistically significant effects were found for EU immigration. The MAC analysis also suggests that the likelihood of a negative impact of immigration on employment of UK-born workers is likely to be greatest during economic downturns.

Devlin et al. (2014) replicated the MAC (2012) analysis with some minor adjustments. It found that the estimated effects on employment were similar if London is omitted from the analysis and when migrants are defined by nationality rather than country of birth.

### **Evidence gaps and limitations**

It is important to recognise that the analysis of the labour market effects of immigration faces a number of methodological challenges. For example, as migrants often go to areas that are experiencing economic growth and strong labour demand, immigration can be both a cause and consequence of changes in wages and employment. This makes it difficult to establish causality. Another problem is that international immigration into a certain area may cause some workers to leave that area and migrate to other parts of the country or abroad. Whenever this happens, the labour market effects in a certain area are dissipated across the country which makes correct measurement through local labour market analysis more difficult. There can also be difficulty in distinguishing whether migrants are actually impacting the wages of UK-born workers, or whether the figures for the average wage are being changed as a result of migrants growing as a proportion of the workforce whilst being paid less (or more) than non-migrants, without them necessarily affecting actual wages UK-born workers receive (Nickell & Salaheen (2015) address this problem in their analysis). A fourth methodological challenge arises from the questionable quality of data on migrants, and especially specific subgroups of migrants, which are often based on small samples of the population and can thus lead to significant measurement error.

Empirical research, including all the studies reviewed in this briefing, has employed various methods and econometric techniques to address these issues. Three broad types of methodological approaches can be distinguished: a 'spatial correlations approach', which slices the national labour market in sub-markets by geographical area, analysing wage changes in areas with different levels of migration (e.g. Dustmann et al 2005); a 'factor proportions approach' which involves simulation of the impact of immigration on the supply of labour and the consequences for wages and employment (e.g. Borjas, Freeman and Katz 1997 in the US); and a 'skills cells approach' which divides the national labour market by skills group rather than geographic area (e.g. Manacorda, Manning and Wadsworth 2012). Each of these approaches has different implications for the methodological challenges outlined above, but some difficulties and caveats usually remain.

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## Further Reading

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## The Migration Observatory

Based at the Centre on Migration, Policy and Society (COMPAS) at the University of Oxford, the Migration Observatory provides independent, authoritative, evidence-based analysis of data on migration and migrants in the UK, to inform media, public and policy debates, and to generate high quality research on international migration and public policy issues. The Observatory's analysis involves experts from a wide range of disciplines and departments at the University of Oxford.



## COMPAS

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