Analysis

Public finance impact of immigration will depend on employment outcomes

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Immigration will bring about a favourable change in the age structure, as the majority of immigrants are young adults. The effects on the public finances will above all depend on the impact of population growth on the costs of various publicly funded services and on the labour market performance of the immigrants. While population growth increases the costs of some publicly funded services, not all the costs will grow proportionally with the population. The average employment rate for immigrants is lower than for natives but it can be influenced. Immigration does not appear to weaken the employment prospects for the native population.



Immigration affects the size and composition of the population

Although attitudes towards immigration are not shaped by economic factors alone, studies on immigration often highlight concerns about the impact of immigration on the wages and employment level of the native population and on public finances.[1]

Immigration has an effect on both the size and the age structure of the working-age population, as the majority of immigrants are young adults. For example, in its 2015 population projection, Statistics Finland foresees a reduction in the working-age population of Finland by 75,000 persons by 2030. According to the same projection, the Finnish working-age population would shrink by 300,000 persons if there were no migration.

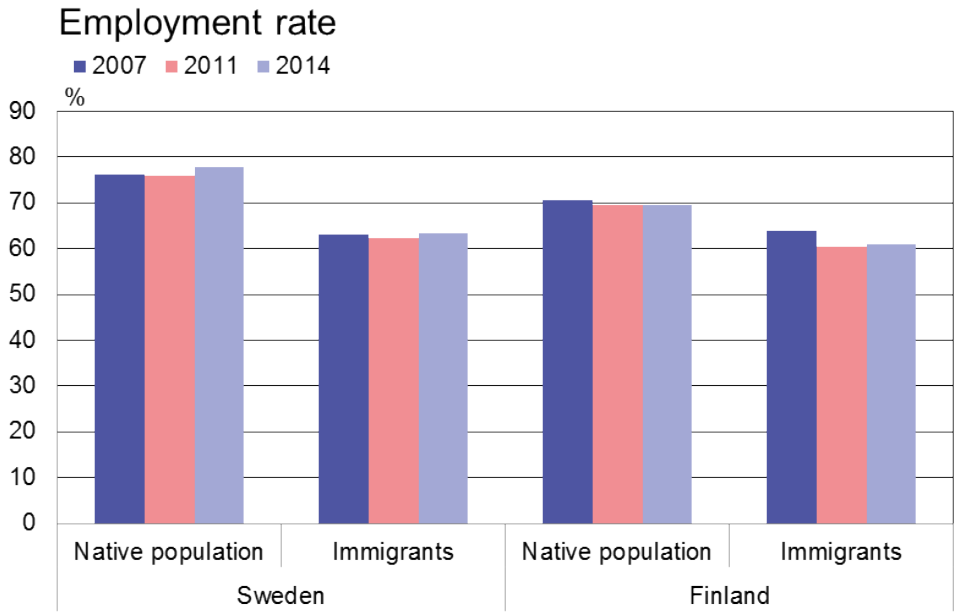
The age structure of the immigrants is the very reason why many ageing Western economies have looked upon immigration as a potential solution to the fiscal problems caused by a deteriorating dependency ratio.[2]

As the population increases, the costs of some public sector services (education, social welfare and health care services) will increase broadly in pace with the population growth. However, part of the public sector services are so-called collective services (e.g. part of infrastructure costs), the total costs of which are independent of the size of the population. The costs of these services per taxpayer will fall as the population increases.[3]

Population growth also means more taxpayers, which is reflected in tax revenue and income transfers. The magnitude of these changes depends on the labour market outcomes for immigrants, in particular.

Immigration carries with it a huge potential. Publicly produced individual services are mainly consumed by children, the young and the old, while especially the social benefits payable as old-age pensions are intended for those over 60 (Chart 1). Considering that the majority of immigrants are of working age, immigration has a favourable impact on the age structure in fiscal terms. However, fulfilment of that potential requires that sufficient numbers of the immigrants find employment.

Chart 1.

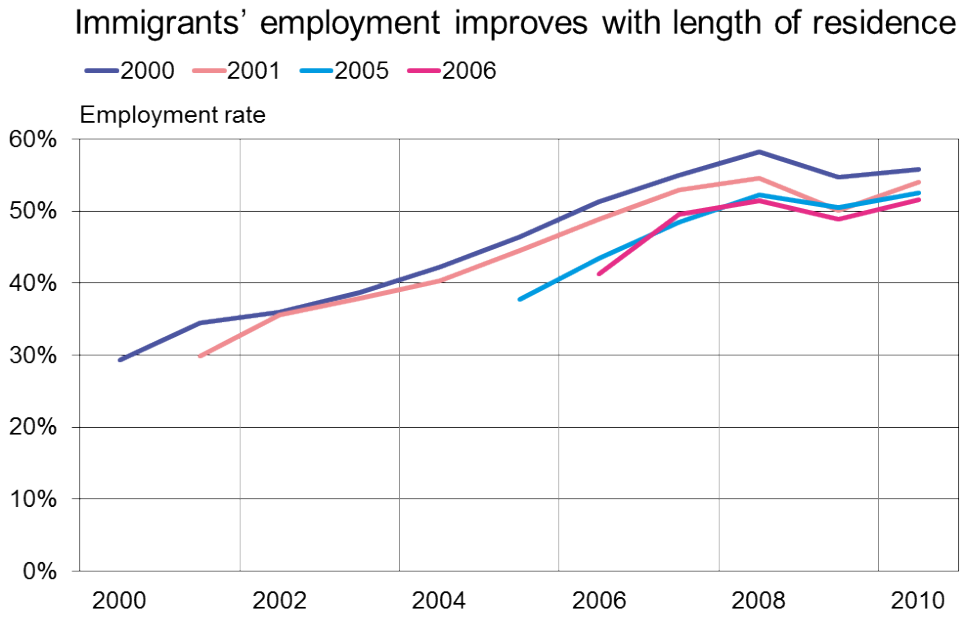


Source: OECD (2015).
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Employment rates lower for immigrants than for natives

In Sweden and Finland alike, the employment rate for non-native-born persons is just over 60% (Chart 2). The employment rate for the native population is slightly higher in Sweden than in Finland. In both countries, the unemployment rate is clearly higher among immigrants than among natives.

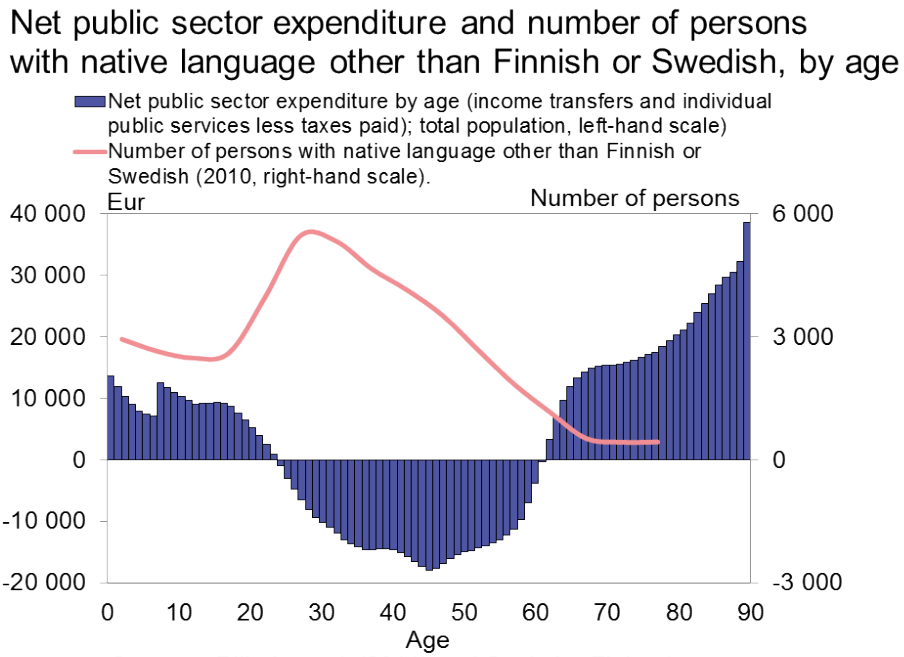
Chart 2.



Source: Eronen et al. (2014).

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Chart 3.



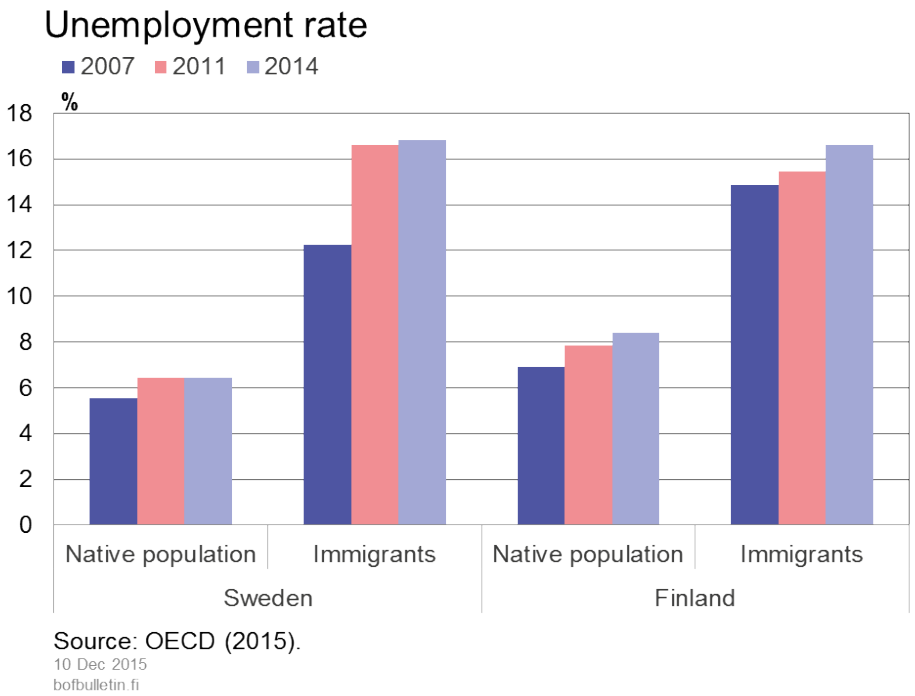
Sources: Riihelä et al. (2011) and Statistics Finland.

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An analysis of the employment situation of immigrants to Finland in age bracket 16–64, grouped

by year of immigration, shows that employment improves over the period of residence (Chart 3). In addition, immigrants who arrived in Finland in 2005 and 2006 have had better labour market outcomes than those who arrived in 2000 and 2001.

Chart 4.



Source: OECD (2015).
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Research results point to major differences among immigrants as regards employment rates, both immediately upon arrival and after a lengthy period of residence.[4] For example, male immigrants of OECD origin who migrated to Finland in 1990–1998 have attained the level of income of comparable natives, in contrast to female immigrants and male immigrants from non-OECD countries.[5]

Immigration has only minor effect on labour market position of native population

The impact of immigration on the labour market of the host country can manifest itself in numerous ways. We will outline one key mechanism. Immigration increases the labour force, causing some unemployment in the presence of wage rigidity. The increase in labour supply (and the rise in unemployment) will, however, create downward pressure on wages. Corporate profitability will improve, encouraging companies to invest and recruit more employees. The rise in labour demand will boost wages and employment. The final outcome will be a higher level of

employment without a change in average wages or the rate of unemployment.[6]

The labour input of less educated immigrants and that of the native population may also be complementary to each other. This may be important especially in an ageing economy like Finland with a steadily rising level of education, where the labour force participation rate for women is high. The demand for labour-intensive, low-education services is growing, while the number of persons willing to take these jobs is decreasing.[7] The educated workforce becomes increasingly specialized in high-productivity tasks, while immigrants are, at least initially, employed in low-productivity jobs.[8]

In such circumstances, immigration may have an effect on income distribution that is not reflected in average wages. The effect on the wages of natives competing for the same jobs with immigrants will be negative, while the effect on the wages of other natives will be positive.

The key challenge for empirical research comes from the difficulties of separating the impact of immigration on the employment and wages of the native population from other factors. There is as yet no Finnish research on this subject, but in light of foreign studies, immigration has only a minor effect on the unemployment and wages of the native population.[9]

Labour market rigidities and integration may influence the labour market outcomes for immigrants

The institutions related to the employment security or wages of employees, such as employment protection, unemployment benefits and minimum wages, are designed to protect employees against the risks of unemployment and loss of income.[10] The downside may be that immigrants will fall below the productive employment threshold. Instead of being employed in low-wage jobs, immigrants may experience a lower rate of employment.[11]

Research on the labour market institutions of European countries finds that the interaction of higher employment protection and barriers to market entry with immigration may have weakened the capacity of the economy to absorb new employees and reinforced the adverse labour market effects of immigration on the native population.[12]

Evidence from the German labour market indicates that while immigration had a negligible impact on the wages and employment of the native population in the 1990s, there was a rise in unemployment among earlier migrants. Greater labour market flexibility would have improved the capacity of the economy to adjust to labour growth.[13]

Research findings indicate that labour market institutions may play a role in determining what kind of immigrants get employed. Similarly, active labour market programmes may influence the labour market performance of immigrants. For example, the Finnish reform which introduced integration plans for non-working immigrants increased the earnings of the target group markedly, and so reduced social benefits.[14] In general, however, there is little research evidence as to what kind of measures are effective.

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Notes

1. See e.g. Preston (2014). ↑
2. The literature on the fiscal effects of immigration does not generally focus on refugees, but adopts a broader view on immigration. There are many special issues related to refugees and exceptional waves of immigration that fall beyond the scope of the present article. ↑
3. According to national accounts data, the general government individual consumption expenditure was around 17% of GDP in 2014, while collective consumption expenditure was around 8% of GDP. ↑
4. Pekkala Kerr and Kerr (2011) have conducted a survey of research on the wages and employment of immigrants. The survey also includes studies on Nordic countries, notably Sweden. ↑
5. Sarvimäki (2011). ↑
6. For more details, see e.g. Haavio et al. (2013). ↑
7. Ottaviano – Peri (2008). ↑
8. The readiness of immigrants and natives to accept job offers may differ, reflecting for example the more general entitlement of natives to earnings-related unemployment benefits. ↑
9. See e.g. Okkerse (2008), Longhi et al. (2005), Dustmann et al. (2007). The labour market may adjust to growing immigration also via channels other than wages and unemployment. Dustman argues that the output structure of the economy may change, while Peri and Sparber (2009) maintain that for example in the European countries the native population has been observed to move into more demanding tasks in step with growing immigration and competition for low-productivity jobs. ↑

10. These labour market phenomena (such as employment protection, the replacement rate of unemployment benefits, wage rigidity and barriers to market entry) favour the native population, not least because union membership is typically less frequent among immigrants, who are more often employed on temporary contracts or in the grey economy. See Angrist and Kugler (2003). ↑
11. See e.g. Antecol et al. (2006). ↑
12. Angrist and Kugler (2003). ↑
13. D'Amuri et al. (2010). ↑
14. Hämäläinen and Sarvimäki (2014). ↑

Keywords

employment, immigration, public finances