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How Labor Market Policies Shape Immigrants' Opportunities

by Pia M. Orrenius and Genevieve R. Solomon

Labor regulations influence the level and flexibility of wages and can diminish new workers' chances of finding jobs by pushing up employment costs.

When it comes to unemployment and labor force participation rates, immigrants do better in the United States than in most other countries.[1] In 2005, for example, the foreign-born had average unemployment of 4.6 percent in the U.S., well below native-born workers' 5.2 percent. U.S. immigrants also had higher participation rates. The American experience stands in stark contrast to many other developed nations'. In France and Germany, for example, the foreign-born typically have jobless rates twice as high as native-born workers and lower participation rates.

What accounts for these differences? Most studies attribute poor labor market outcomes to the immigrants themselves—their education levels, language skills, inexperience, family composition and reasons for migrating. Immigrant characteristics surely matter, but so do the host country's labor market institutions and policies.

Labor market access is important because immigrants who can't find work are blocked from the first rungs of the economic ladder.

Table 1
Foreign-Born Share of Population
(Percent)

Australia	23.6
Canada	18.8
Austria	12.5
United States	12.1
Germany*	12.1
Sweden	11.8
Belgium*	10.7
Netherlands	10.6
Ireland	10.4
Greece*	10.3
France*	10.0
United Kingdom	8.3
Denmark	6.2
Spain*	5.3
Czech Republic*	4.5
Italy*	3.9
Hungary*	2.9
Slovak Republic*	2.5

NOTE: Data are for 2001 except as follows: Australia (2004); Denmark, the Netherlands (2003); U.S. (2005); Germany, Ireland and Sweden (2002); France (1999).

SOURCES: Migration Policy Institute; Organization for Economic Cooperation and Development (denoted by *).

Countries with less restrictive labor regulations typically provide more job opportunities for their immigrants. Employers have greater freedom in hiring and firing, and supply and demand largely determines the terms of employment, such as wages, benefits and length of the workweek. More restrictive policies, on the other hand, include centralized wage-setting, strict rules that inhibit laying off workers and ceilings on the length of the workweek, such as the 35-hour limit France imposed in 2000.

Labor regulations influence the level and flexibility of wages and can diminish new workers' chances of finding jobs by pushing up employment costs. In standard economic analysis, unemployment results when wages and benefits exceed the market rate. It can happen when wage floors and mandated benefits set compensation too high. It can also occur when compensation is fixed and cannot fall in response to increased supply or decreased demand for labor.

Studies suggest less productive and lower wage workers are more likely than others to find themselves without jobs when restrictive policies are adopted or when wages remain fixed in the face of an adverse economic shock. A 2002 study of 17 countries in the Organization for Economic Cooperation and Development (OECD) found that union wage-setting priced the young and elderly out of employment and pushed them out of the labor force, while it raised relative unemployment rates for females.[2]

There's little research on such regulations' effect on immigrants, but the issue is coming to the forefront. The OECD has preliminary work showing that higher minimum wages, generous unemployment benefits and higher taxes negatively affect labor market activity among foreign-born women and employment among foreign-born men.[3] Immigrants are often more vulnerable than natives because in addition to lower education levels, they are typically younger and lack host-country language skills and job experience.[4]

Labor market access is important because immigrants who can't find work are blocked from the first rungs of the economic ladder. In more flexible labor markets, employers can compensate for immigrants' initial liabilities by offering them lower starting wages—in much the same way businesses pay fresh college graduates less than experienced workers. Over time, as immigrants improve their skills and become more productive, they earn higher pay. In fact, studies of U.S. immigrants find that lower initial earnings are correlated with subsequent higher wage growth.[5]

Immigrants have a large and growing presence in many national economies. They make up 23.6 percent of the population in Australia, 18.8 percent in Canada, 12.1 percent in the U.S. and Germany, and 10 percent in France (*Table 1*). Policies that erect employment barriers can lead to unemployment, inactivity or segmented labor markets that relegate immigrants to temporary jobs or positions with few prospects for advancement. Better job opportunities for immigrants, on the other hand, can speed their economic assimilation and reduce their dependence on public assistance.

Comparing Immigrant Unemployment Rates

Labor market policies regulate what would otherwise be a private transaction—the buying and selling of labor. Examples include centralized wage-setting, job protection, minimum annual leave and employment taxes. Regulations may also require safe working conditions and prohibit discrimination based on age, gender and race. The level and duration of unemployment benefits and the generosity of social assistance programs can also influence labor supply. Although governments typically set labor market policies, collective bargaining between

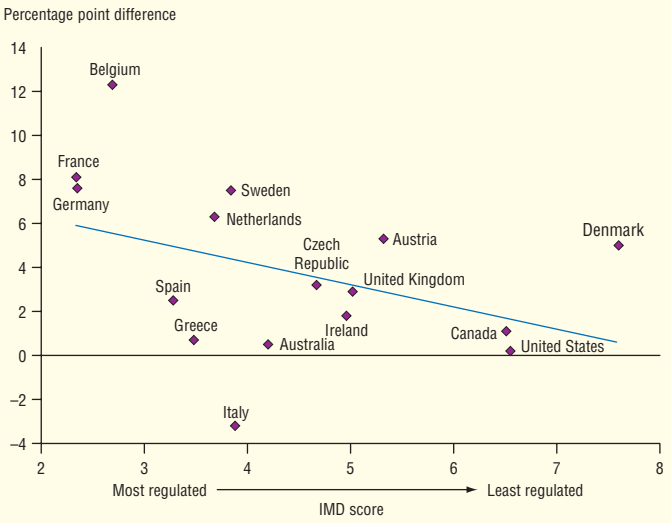
Table 2
Labor Market Regulation and Unemployment

IMD score	Country	Male unemployment rates: Native (percent)	Male unemployment rates: Foreign-born (percent)
2.3	France	7.3	15.4
2.4	Germany	9.3	16.9
2.7	Belgium	6.0	18.3
3.3	Spain	7.9	10.4
3.5	Greece	5.8	6.5
3.7	Netherlands	2.8	9.1
3.8	Sweden	5.2	12.7
3.9	Italy	7.0	3.8
4.2	Australia	6.0	6.5
4.7	Czech Republic	5.8	9.0
5.0	Ireland	4.8	6.6
5.0	United Kingdom	5.2	8.1
5.3	Austria	4.4	9.7
6.5	Canada	6.2	7.3
6.6	United States	7.0	7.2
7.6	Denmark	3.8	8.8

NOTES: Higher IMD scores reflect fewer regulations. IMD scores are for 2004; unemployment rates, for 2003.

SOURCES: *IMD World Competitiveness Yearbook*, 2005; *Trends in International Migration: SOPEMI 2004 Edition.*

Chart 1
Immigrants Fare Better in Less Restrictive Labor Markets
Difference between immigrant and native unemployment rates



SOURCES: *Trends in International Migration: SOPEMI 2004 Edition*; *IMD World Competitiveness Yearbook*, 2005.

workers' and employers' unions also plays a large role in many countries.

Every nation intervenes in its labor market to some extent. The International Institute for Management Development (IMD) produces annual surveys that compare the degree of labor market regulation among countries. Scores are based on questionnaires sent to top and middle managers of businesses in the 60 economies covered in the *IMD World Competitiveness Yearbook*. Respondents assess the competitiveness of their labor markets, assigning lower values when they think regulations hinder business and higher ones when they see few problems. The IMD then calculates an average value for each economy.

The scores range from zero for countries with regulations that present the greatest hindrance to business to 10 for nations with policies that cause the least. According to the IMD, France and Germany have the most regulated labor markets in our sample of OECD countries. The least-regulated labor markets include Denmark, the U.S. and Canada (*Table 2*).

By plotting each country's IMD score against the difference in jobless rates between foreign- and native-born men in the countries with data available, we can see how the degree of labor market regulation correlates with immigrants' relative unemployment rate. The unemployment rates, which come from the 2005 OECD report *Trends in International Migration*, represent the average for foreign-born and native men ages 15 to 64 in 2003.[6]

Immigrants in countries with more restrictive labor regulations have higher unemployment rates relative to natives than immigrants in countries with fewer such regulations (*Chart 1*). In France, for example, male immigrants had a jobless rate of 15.4 percent, while natives were at 7.3 percent—a gap of 8.1 percentage points, second only to Belgium's 12.3 points. With an IMD score of 6.6, the U.S. is less regulated and has a relatively small difference in unemployment rates—7.2 percent for male immigrants and 7 percent for natives. The trend line shows the overall tendency for unemployment differentials to be higher in more-regulated markets. In most European countries, these differences are even larger when we compare only immigrants from non-European Union countries to natives.

Some outliers are far off the trend line. Despite restrictive labor markets,

Studies show that young workers, as lower-productivity employees, often bear the costs of labor market regulations.

for example, immigrants in southern European countries such as Spain, Greece and Italy fare quite well. Until recently, immigrants to these countries were few but relatively skilled, compared with natives. Today, the Mediterranean countries have higher shares of employment-based immigration—including illegal immigration—and larger informal sectors than northern European countries. In Spain, moreover, opportunities for immigrants have been facilitated by rapid employment growth and a dual labor market structure.[7] The prevalence of fixed-term employment contracts, which bypass many regulations that apply to permanent positions, has meant that temporary workers make up a third of the Spanish workforce.

Denmark is another outlier, but in the opposite direction. Given the country's high IMD score, Danish immigrants should fare better than they do. Denmark, however, has very generous social assistance and unemployment benefits for low-income workers, which at least partly explains immigrants' underperformance.

Denmark's net replacement rate—the after-tax share of previous earnings paid by unemployment benefits upon job loss—is almost 80 percent for four years for a one-earner family making the equivalent of the average production wage.[8] In this case, the U.S. net

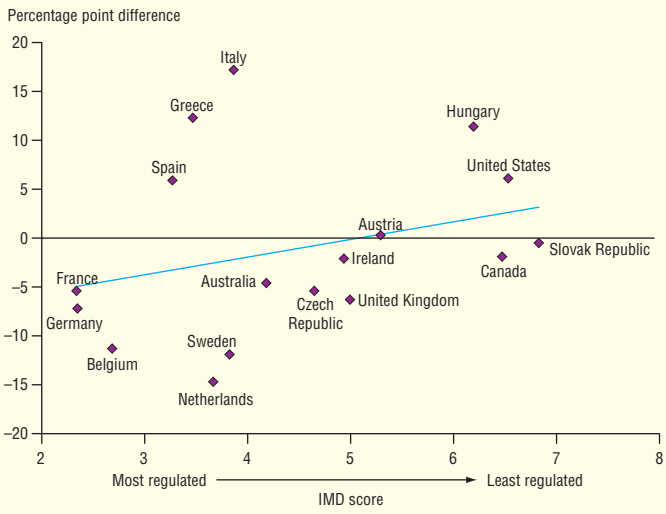
Table 3
Labor Market Regulation and Employment

IMD score	Country	Male employment-to-population ratios: Native (percent)	Male employment-to-population ratios: Foreign-born (percent)
2.3	France	69.8	64.4
2.4	Germany	71.3	64.1
2.7	Belgium	68.5	57.2
3.3	Spain	72.8	78.7
3.5	Greece	71.7	84.0
3.7	Netherlands	83.1	68.4
3.8	Sweden	76.5	64.6
3.9	Italy	69.2	86.4
4.2	Australia	78.7	74.1
4.7	Czech Republic	73.4	68.0
5.0	Ireland	74.7	72.6
5.0	United Kingdom	78.5	72.2
5.3	Austria	75.3	75.6
6.2	Hungary	63.4	74.8
6.5	Canada	79.1	77.2
6.6	United States	73.5	79.2
6.9	Slovak Republic	63.5	63.0
7.6	Denmark	79.4	58.2

NOTES: IMD scores are for 2004; ratios, for 2003.

SOURCES: *IMD World Competitiveness Yearbook*, 2005; *Trends in International Migration: SOPEMI 2004 Edition.*

Chart 2
Immigrant Economic Activity Greater in Less Restrictive Labor Markets
Difference between immigrant and native male employment-to-population ratios



SOURCES: *Trends in International Migration: SOPEMI 2004 Edition*; *IMD World Competitiveness Yearbook*, 2005.

replacement rate averages 55 percent for 26 weeks. Compared with natives, Danish immigrants are two to three times more likely to receive unemployment benefits or social assistance.

Generous, long-lasting benefits and assistance may lessen incentives to find work, increase both the incidence and duration of unemployment, and discourage people from joining the workforce. Because immigrants, particularly those from non-EU countries, face other challenges and are generally poorer, they're more affected than natives and other EU citizens by these policies.

Comparing Employment-to-Population Ratios

Unemployment rates tell us about workers who are actively seeking jobs. If immigrants are discouraged from even searching, they may remain outside the labor force altogether. Looking at the number of immigrants employed relative to their population provides a broader measure of immigrants' participation.

Among the countries with data available, the employment-to-population ratios of native- and foreign-born men differ markedly (*Table 3*). In 2003 in France, 69.8 percent of native men worked, compared with 64.4 percent of foreign-born men—a difference of 5.4 percentage points. Belgium, the Netherlands, Sweden and Denmark had differentials exceeding 10 percentage points. In the U.S., 73.5 percent of native males held jobs, compared with 79.2 percent of male immigrants, a gap of 5.7 percentage points in the opposite direction. Overall, countries with heavier labor regulation have a smaller percentage of their foreign-born male population employed than countries with fewer regulations (*Chart 2*).[9]

Labor market regulations aren't the only obstacle to foreign-born workers' employment. As mentioned above, public assistance programs and other social policies provide immigrants with an income and other subsidies. These programs may deliberately or inadvertently keep would-be workers out of the labor force. In addition, immigration laws, such as those applying to asylum seekers, often prohibit work outright. Undocumented immigrants aren't allowed to work, although in the U.S. and many other countries they typically do. Illegal immigrants, particularly men, have very high employment-to-population ratios.[10]

Are the Young Disproportionately Hurt?

Studies show that young workers, as lower-productivity employees, often bear the costs of labor market regulations, while prime-age, full-time workers reap many of the benefits. Do these regulations more heavily impact young immigrants, who possess relatively few skills and little work experience?

In many countries, youth unemployment is generally high, but immigrants tend to fare worse than natives (*Table 4*). Among workers aged 15 to 24 in the countries with data available, the average unemployment rates in 2002–03 for foreign citizens, including men and women, were 5.3 percentage points higher than they were for nationals.[11] This compares with a 3.8 percentage point differential for the overall male population.

Plotting individual countries' differentials against the IMD scores suggests that nations with more-regulated labor markets tend to disadvantage young, non-native workers (*Chart 3*). The trend line for youths is steeper than the one for males overall.[12] This indicates labor market regulations may affect young immigrants more than older ones.

In France, the unemployment rate for foreign youths was 34.2 percent in 2002–03, or 16.4 percentage points higher than national youths' unemployment of 17.8 percent. Only Belgium's differential is higher. The United States and most other less-regulated nations tend to have lower differentials between immigrants and the native-born. Young U.S. immi-

Generous, long-lasting unemployment benefits and social assistance may lessen incentives to find work, increase both the incidence and duration of unemployment, and discourage people from joining the workforce.

Table 4

Labor Market Regulation and Youth Unemployment

IMD score	Country	Youth unemployment rate: Nationals (percent)	Youth unemployment rate: Foreigners (percent)
2.3	France	17.8	34.2
2.4	Germany	10.0	16.3
2.7	Belgium	17.1	35.9
3.3	Spain	22.6	22.2
3.5	Greece	25.0	20.3
3.8	Sweden	13.1	26.8
4.2	Australia	12.8	17.0
4.7	Czech Republic	15.5	15.4
5.0	United Kingdom	10.5	14.8
5.3	Austria	7.1	9.7
6.5	Canada	9.7	14.3
6.6	United States	12.5	10.7

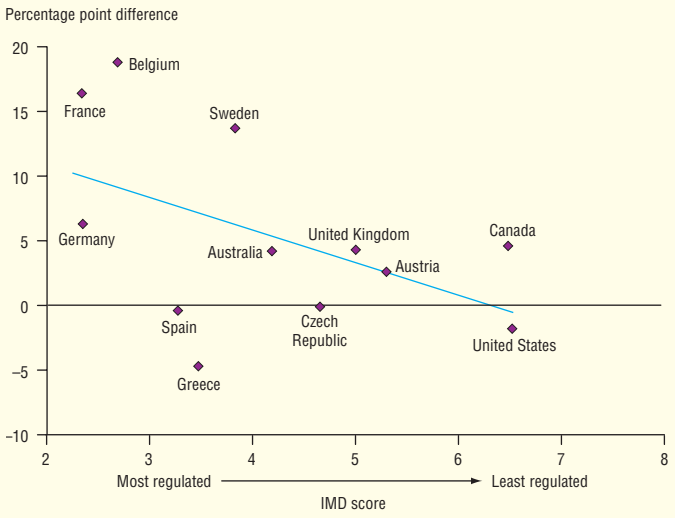
NOTES: Youth unemployment data refer to nationals and foreigners, except for the United States, Canada and Australia, where data are based on country of birth. IMD scores are for 2004; unemployment, for 2002–03.

SOURCES: *IMD World Competitiveness Yearbook*, 2005, *Trends in International Migration: SOPEMI 2004 Edition.*

Chart 3

Immigrant Youths Fare Better in Less Restrictive Labor Markets

Difference between foreign and national youth unemployment rates



SOURCES: *Trends in International Migration: SOPEMI 2004 Edition*; *IMD World Competitiveness Yearbook*, 2005

grants actually had a lower unemployment rate than natives—10.7 percent versus 12.5 percent.

Some policymakers have recognized that institutions are playing a role in high youth unemployment rates. France recently proposed reforms to make labor markets more flexible. The effort involved changes in the law that would allow firms to dismiss workers 26 years and younger during the first two years of their employment without having to give a reason. The intention was to encourage the hiring of younger French workers and reduce their unemployment rate. The virulent public response included protests by college-age youths, and the proposal was quickly shelved. Students and workers strongly resisted the removal of regulations they believe guarantee their job security.

Another concern is how poor labor market performance relates to foreign youths' educational outcomes. Results from international testing of foreign- and native-born 15-year-olds suggest that achievement deficits of foreign-born students are the most severe in the countries where immigrant labor market outcomes are the worst (*Table 5*). To measure achievement gaps, we used the average score difference between natives and immigrants on math literacy tests in the 2003 Program for International Student Assessment (PISA) for the countries in our sample.[13] U.S. students scored below the international average overall, but the achievement gap between natives and immigrants is relatively small. Generally, the gaps shrink when controlling for parents' socioeconomic status, including education level and occupational status, but they remain large and significant in almost every country.

Many factors beyond family background contribute to academic success, and immigrant students can be disadvantaged in myriad ways—from a lack of language skills to poor school quality in urban areas. Parents' labor market outcomes can also play a role by affecting the family's economic standing and the resources that are devoted to children's education. Students' perceptions of their own job prospects will also contribute to how much they invest in their human capital.

Immigrant Characteristics and Other Factors

Our data suggest a clear link between labor market policies and immigrants' job prospects. Immigrants in countries with highly regulated labor markets have relatively high unemployment rates and low employment-to-population ratios. Highly reg-

ulated labor markets with union-set wages and high tax rates can price newcomers and other less productive workers out of jobs.

Our analysis, however, by no means quantifies the size of the effect, nor does it explain all the differences in labor market outcomes between immigrants and natives. Indeed, many factors account for the relative performance of foreign workers across countries. We've touched on the influences of unemployment benefits, social assistance programs and dual labor markets. But systematic differences in the characteristics of immigrants across countries also underlie data patterns.

Immigrant characteristics can lessen or exacerbate the impact of labor market policies. Educated and high-productivity immigrants won't be as hurt by regulations that raise employment costs. Despite a fairly restrictive labor market, Australian immigrants do well relative to the native-born; the difference in unemployment rates between the two groups is close to zero. This is partly explained by immigrants' high education levels. In Australia, 57 percent of the foreign-born population has an upper-level education, compared with 44 percent of the native population.[14]

In France, 63.9 percent of foreigners have less than a secondary education, compared with 33.5 percent for nationals. In Germany, 47.1 percent of foreigners lack secondary schooling, while only 13.6 percent of nationals do. The OECD found that if foreigners in Germany had the same education levels as nationals, the unemployment gap would narrow by a third. Education's effect on the unemployment gap was considerably lower in other countries, however.

Immigrant characteristics that underlie economic outcomes are often driven by geographic, historical, political and cultural links between countries. For example, Mexicans make up nearly a third of the U.S. foreign-born population, largely due to their homeland's proximity to the United States. Historical ties with North Africa help explain why about a third of France's immigrants come from Morocco and Algeria.

Immigration laws and other public policies also matter. Countries like Sweden, which give priority to refugees and asylum seekers, may have immigrant populations that have worse economic outcomes in the near to medium term than countries like Canada and Australia, which focus policy more broadly on bringing in educated or employment-based migrants. Generous social assistance programs may result in self-selection of migrants, attracting those less likely to do well in the labor market.

Large numbers of immigrants without legal status—as in the United States, where about 30 percent of the foreign-born are undocumented—may contribute to low unemployment and high participation rates. Undocumented immigrants tend to migrate for work and send money back home. Once they're in the host country, they have strong incentives to continue working. Illegal immigrants lack a social safety net because they're generally ineligible for welfare and unemployment benefits.[15]

Countries that restrict legal immigrants' access to citizenship, as Germany has historically done, may inadvertently slow the assimilation process.[16] Research on U.S. immigrants finds a positive association between naturalization, higher income and fluency in English.

Table 5
Educational Achievement and Youth Unemployment

Country	Foreign-born achievement deficit	Foreign–national unemployment difference
Average, high-income PISA countries	45	—
Belgium	82	18.8
Sweden	61	13.7
France	54	16.4
Austria	51	2.6
Greece	44	–4.7
Spain	41	–.4
Germany	39	6.3
United States	35	–1.8
Canada	10	4.6
Australia	7	4.2

NOTES: The achievement deficit has been adjusted for parents' socioeconomic status. Youth unemployment is from Table 4.

SOURCES: "Variation in the Relationship Between Nonschool Factors and Student Achievement on International Assessments," by Gillian Hampden-Thompson, Jamie Johnston and American Institute for Research, *Statistics in Brief*, April 2006, National Center for Education Statistics; *Trends in International Migration: SOPEMI 2004 Edition.*

Balancing Costs and Benefits

Although the determinants of immigrants' success are many and complex, we can't ignore the role of labor market rigidities and their implications for the economy and society. Policies that keep immigrants out of employment contribute to higher unemployment and lower economic activity as well as slower economic assimilation. These regulations are often accompanied by extensive public assistance programs, which increase the tax burden associated with immigration. Such side effects can harden natives' attitudes toward immigrants. A report summarizing the difference between European and U.S. views found that a majority of Europeans favor stopping migration altogether, while a majority of Americans want to merely stop increases in migration.[17]

In market economies, immigration

increases economic growth and national income. The distribution of the gains can be uneven, depending on whether immigrants are low or high skilled—but on average, the host country benefits. Policies that restrict labor market access, however, detract from these gains. European labor economists have shown that when the host country is experiencing unemployment and wages are fixed, immigration of less-skilled workers results in a net loss to natives.[18]

At a time when population and labor force growth in many developed countries are increasingly driven by immigration, more attention should be paid to the perverse effects of some labor market policies. Nations should seek to structure a level playing field, on which the benefits of employment protections and other regulations are balanced against the costs, particularly where many of these costs are borne by the low-paid, low-skilled and inexperienced.

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Notes

[1] We use the terms *immigrant* and *foreign-born* interchangeably. *Native-born* refers to those born in the receiving country, while *foreign-born* are those born abroad.

[2] "Labor Market Institutions and Demographic Employment Patterns," by Giuseppe Bertola, Francine D. Blau and Lawrence M. Kahn, NBER Working Paper no. 9043, July 2002.

[3] "The Labor Market Integration of Immigrants in OECD Countries," by Sébastien Jean, 2006, www.oecd.org/dataoecd/25/14/36789352.ppt.

[4] In surveys, immigrants also cite a lack of social networks in the job market and difficulties transferring foreign qualifications as key problems they encounter in searching for employment. Discrimination could also be a factor.

[5] "Measuring Immigrant Wage Growth Using Matched CPS Files," by Harriet Orcutt Duleep and Mark C. Regets, *Demography*, May 1997, pp. 239–49.

[6] The sample of countries is based on the data available in the OECD report. We chose to focus on men (except in the case of youths) to abstract from differences across countries that drive foreign-born females' work decisions, such as country of origin, cultural and religious background.

[7] For additional information, see "Labor Market Assimilation of Recent Immigrants in Spain," by Catalina Amuedo-Dorantes and Sara de la Rica, IZA Discussion Paper no. 2104, April 2006.

[8] The example refers to 2002 data for a one-earner married couple with two children and no social assistance who earned the average production wage in the prior job. (See Figure 3.1a in *Benefits and Wages: OECD Indicators*, 2004 edition.)

[9] Denmark was excluded from this chart because it is a statistical outlier. Denmark has an IMD score of 7.6, but the difference in employment rates between the foreign- and native-born populations is –21.2 percentage points. For more discussion on immigrant outcomes in Denmark, see *Migrants, Work, and the Welfare State*, Torben Tranaes and Klaus F. Zimmermann, eds., Odense: University Press of Southern Denmark and the Rockwool Foundation Research Unit, 2004.

[10] More than 90 percent of illegal immigrant men in the U.S. are employed. See "Undocumented Immigrants: Myths and Reality," by Randolph Capps and Michael E. Fix, www.urban.org/publications/900898.html.

[11] *Nationals* are citizens in the receiving country, while *foreigners* denote those who are still citizens of the sending country. Because of restrictions on naturalization in some countries, such as Germany, it is possible to have second- and third-generation descendants of immigrants who are still "foreigners."

[12] The correlation coefficient in Chart 3 is –0.49, compared with –0.41 in Chart 1. In Chart 2, the correlation coefficient is 0.28.

[13] The average cross-country math literacy score was 500 for the native-born and 445 for the foreign-born; two-thirds of students scored between 400 and 600.

[14] Data on educational distribution of foreign and national populations are from Table I.12 in *Trends in International Migration: SOPEMI 2004 Edition*.

[15] Exceptions include emergency medical and maternity care.

[16] Germany passed an immigration law in 1999 that greatly eases the once-rigorous naturalization requirements. Previously, citizenship was largely based on ancestry or descent.

[17] *Immigration Policy and the Welfare System*, Tito Boeri, Gordon Hanson and Barry McCormick, eds., New York: Oxford University Press, 2002.

[18] "Looking South and East: Labour Market Implications of Migration in Europe and Developing Countries," by Thomas Bauer and Klaus Zimmermann, in *Globalization of Labour Markets: Challenges, Adjustment and Policy Responses in the EU and the LDCs*, O. Memedovic, A. Kuyenhoven and W. T. M. Molle, eds., Dordrecht: Kluwer Academic Publishers, 1997, pp. 75–103.

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