Immigration and the U.S. Economy

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Introduction

In my very brief comments I will touch on several key issues surrounding immigration and the economy. My goal will be to clear up some of the confusion that often clouds the immigration debate. In particularly, I will explain the difference between increasing the overall size of the U.S. economy, and increasing the per-capita income of Americans. Finally, I will touch on the issue of immigration's impact on public coffers.

Immigration and the Size of the U.S. Economy

Immigration increases the overall size of the US economy. Of this there is no question. In 2009 immigrants accounted for 15 percent of all workers. More workers and more people mean a bigger GDP. Immigrants are 15 percent of U.S. workers. They likely account for about 10 percent of GDP or more than a trillion dollars annually. However, this does not mean that the native-born population benefits from immigration. Basic economic theory shows that the overwhelming majority of this increase in economic activity goes to the immigrants themselves in the form of wages and other compensation. It is important to understand that the increase in the size of the economy is not, by itself, a benefit to the existing population. Moreover, immigrants who arrived in the last 10, 20 or 50 years are without question earning and living better on average then they would be had they remained in their home countries.

If the question is how much does the existing population benefit, then the key measure is the impact of immigration on per-capita GDP in the United States, particularly the per-capita GDP of the existing population. We can see the importance of per-capita GDP versus aggregate GDP by simply remembering that the economy of Mexico and Canada are similar in size. But this does not mean the two countries are equally rich because Mexico's population is roughly three times that of Canada's.

Benefits to Natives

There is a standard way of calculating the benefit from immigration, also referred to the as the immigrant surplus, that goes to the existing population. A 1997 study by National Academy of Sciences[1] which was authored by many of the top economists in the field, summarizes the formula for calculating the benefit (see pages 151-152). The NAS study updates an earlier study by the nation's top immigration economist, George Borjas of Harvard (see page 7) [2] In 2007 the President's Council of Economic Advisers (CEA) again used the same formula

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[1] Edmonston, Barry and James Smith Ed. 1997. The New Americans: Economic, Demographic, and Fiscal Effects of Immigration, Washington D.C.: National Academy Press. http://books.nap.edu/openbook.php?isbn=0309063566

[2] George Borjas. "The Economic Benefits of Immigration" *Journal of Economic Perspectives* Vol. 9, Num. 2, Spring 1995. http://www.hks.harvard.edu/fs/gborjas/Papers/Economic_Benefits.pdf

to estimate the benefit of immigration to Americans.[3] A blog by professor Borjas has a clear non-technical explanation of the calculation, from which I borrow heavily in this paper.[4]

The next gain from immigration can be estimated using the following formula:

Net gain from immigration as a share of GDP = - .5 * labor's share of income * wage elasticity * immigrant share of labor force squared.

"Labor share" refers to the percentage of GDP that goes to workers, which is usually thought to be 70 percent, the rest being capital. The immigrant share of the labor force is well known, and is currently 15 percent. "Wage elasticity" refers to the percentage change in wages from immigration increasing the size of the labor force by one percent. The size of the elasticity is a contentious issue. The NAS study assumed an elasticity of .3 and so will I in the calculation below. This means that each 1 percent increase in supply of labor caused by immigration reduces wages by 0.3 percent. Put a different way, if immigration increased the supply of workers by 10 percent, it would reduce the wages of American workers by 3 percent. Putting the values into the formula produces the following estimate:

0.24% =-50 * 70% * -0.3% * (15%*15%)

Thus the net gain from immigration is 0.24% of GDP. (Expressed as decimal it is .0024.) If GDP is $14 trillion, then the net benefit would be $33 billion. Three important points emerge from this analysis. First, the net effect of immigration on the existing population is positive overall, thought not for all workers. Second, the benefits are trivial relative to the size of the economy, less than one-quarter of one percent. Third, the benefit is dependent on the size of the wage losses suffer by the existing population of workers. Or put a different way, the bigger the wage loss the bigger the net benefit. Those who content that immigration has no impact on the wages of immigrants are also arguing, sometimes without realizing it, that there is no economic benefit from immigration.

The same model can be used to estimate the wage losses suffered American workers.

Wage loss as a fraction of GDP = - "labor's share of income" * "wage elasticity" * "immigrant share of labor force"* "native-born share of labor force.

Putting the numbers into the equation you get the following:

2.7% = -0.7 times -0.3 times 0.15 times 0.85

This is 2.7% of GDP or $375 billion in wage losses suffered by American workers because of immigration. This is not trivial. There is nothing particularly controversial about this

[3] "Immigration's Economic Impact" White paper June 20. 2007 http://georgewbush-whitehouse.archives.gov/cea/cea_immigration_062007.html
[4] "No Pain No Gain June 8 1997, http://borjas.typepad.com/the_borjas_blog/2007/06/index.html

estimate and its stems from the same basic economic formula as the one above. Think of it this way, labor is 70 percent of the economy, which is $14 trillion in total. If the elasticity is .3, and immigrants are 15 percent of the labor force, then wages will decline several percentage points (15 by .3). Thus the total wage loss must run into the hundreds of billions of dollars. If we are to accept the benefit that the model implies from immigration, then we must also accept the wage losses that the model implies.

The money that would have gone to workers as wages if there had been no immigration does not vanish into thin air. It is retained by owners of capital as higher profits or passed on to consumers in the form lower prices. The fact that business owners lobby so hard to keep immigration levels high is an indication that much of the lost wages is likely retained by them. Also, workers who face little or no competition from immigrants will not suffer a wage loss. In fact, demand for their labor may increase and their incomes rise as a result. For example, if you are an attorney or a journalist at an English-language news outlet in the United States you face very little competition from immigrants.[5] In fact, immigration may increase your wages as demand for your occupation rises. In contrast, if you a nanny, maid, bus boy, cook, meat packer or construction laborer, then the negative wage impact is likely to be large because immigration has increased the supply of workers in these sectors quite a bit. But overall, the gain to some workers, businesses and consumers is still slightly larger than the loss suffered by the losers; hence the tiny net benefit reported above.

Immigrant and Native Job Competition

Some may feel that there is no job competition between immigrants and native-born workers. The argument is often made, mostly by non-economists, that immigrants only do jobs Americans don't want. But analysis of all 465 occupations defined by the Department of Commerce shows that even before the current recession only four are majority immigrant. These four occupations account for less than 1 percent of the total U.S. workforce. Many jobs often thought to be overwhelmingly immigrant are in fact majority native-born. For example, 55 percent of maids and housekeepers are native-born, as are 58 percent of taxi drivers and chauffeurs, 63 percent of butchers and meat processors, 65 percent of construction laborers, and 75 percent of janitors are native-born. There are 93 occupations in which at 20 percent of workerss are immigrants. There are about 24 million native-born Americans in these high-immigrant occupations.[6] Thus, the argument that immigrants and natives never compete for jobs is simply incorrect. The real question is how have the poorest and the least educated American workers fared in recent decades as immigration has increased.

Deterioration at the Bottom of the Labor Market

There has been a long-term decline in wages, even before the current recession, among

[5] "Jobs Americans Won't Do? A Detailed Look at Immigrant Employment by Occupation" Center for Immigration Studies Memorandum. Steven Camarota, Karen Jensenius. August 2009 http://www.cis.org/illegalimmigration-employment

[6] "Jobs Americans Won't Do? A Detailed Look at Immigrant Employment by Occupation" Center for Immigration Studies Memorandum. Steven Camarota, Karen Jensenius. August 2009 http://www.cis.org/illegalimmigration-employment

the less-educated. Hourly wages for those who have not completed high school declined 22% in real terms (adjusted for inflation) from 1979 to 2007. Hourly wages for those with only a high school education declined 10% in real terms from 1979 to 2007.[7]

The share of less educated adults holding a job has been deteriorating for some time. This is true even before the current recession. From 2000 to 2007 the share of adult natives (ages 18 to 65) without a high school diploma holding a job fell from 54% to 48%. For those with only a high school education, the share employed fell from 73% to 70%. By 2009 it was down to 43% for those without a high school diploma and 65% for those with only a high school education. There is a huge supply of less-educated people available as potential workers. In 2007, before the recession, there were more than 22 million native-born Americans (18 to 65) with no more than high school education who were not working. By 2009 that number was 26 million.[8]

If there was a tight labor market and unskilled workers really were in short supply, then we would expect that wages to rise for the less-educated. We would also expect that the share of these workers holding a job would be climbing. But even before the current recession, this was not what has happening. The deterioration in wages and employment for the less-educated is the kind of pattern we would expect to see as a result of immigrant competition.

Fiscal Impact of Immigration

The impact of immigration on public coffers is not directly part of a discussion on immigration and the economy. But when thinking about the overall effect of immigration on our pocketbooks, the taxes paid and services used by immigrants is an important issue. It may be the most important issue. The previously mentioned National Academy of Sciences (NAS) study estimated that the net fiscal drain (taxes paid minus services used) from immigrant households in 1997 was $11 to $20 billion a year. At the same time, using the same formula discussed above, the NAS study estimated a net economic benefit of $1 billion to $10 billion a year from immigration. Thus, the estimated fiscal drain was larger than the economic benefit. (Today the economic benefit and fiscal drain are larger reflecting our larger economy and government.)

It also must be remembered that there is still of wage losses for less-skilled workers. The NAS study indicated that the wages of the poorest ten percent of American workers were reduced by 5 percent as a result of immigrant-induced increases in the supply of labor.

More recent analysis indicates that the fiscal costs of immigration remain large. Census Bureau data indicate that one-third of those without health insurance in the United States are either immigrants (legal or illegal) or U.S.-born children (under 18) of immigrants. One-four of children living in poverty in the United States has an immigrant father. In 2008, 53 percent of immigrant households with children used at least one major welfare program, primarily food

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[7] The State of Working America 2008/2009 by Lawrence Mishel, Jared Bernstein and Heidi Shierholz Economic Policy Institute. Table 3.16 page 166.

[8] All figures for employed are based on the author's calculation of employment and labor force participation from the public use files of the Current Population Survey in the third quarter of 2000, 2007 and 2009.

assistance and Medicaid.[9] These fiscal costs are incurred despite immigrant's high rates of labor force participation. Their high welfare use rates and the resulting fiscal drain they create stem from the fact that a large share have relatively little education. About one-third of immigrants who arrive as adults have not graduated from high school. The modern American economy offers limited opportunities to such workers. This fact, coupled with a welfare state designed to help low income workers with children, is the reason for the above statistics.

Conclusion

When thinking about immigration it is important to recognize that its impact on the size of the economy is not a measure of the benefit to natives. There is no question that U.S. GDP is significantly larger because of immigrant workers. However, a larger economy is entirely irrelevant to the key question of whether the per-capita GDP of natives is higher because of immigration. Efforts to measure the impact of immigration on the per-capita GDP of Americans, using the standard economic model, show that the benefit is trivial relative to the size of the economy. Perhaps most important, these trivial gains are the result of reduced wages for American workers in competition with immigrants. These workers tend to be the least educated and poorest already. If there is no wage reduction, then there is no economic gain. Finally, the tiny economic gain is probably entirely offset by the fiscal drain immigrants create on tax payers.

In the end, arguments for or against immigration are as much political and moral as they are economic. The latest research indicates that we can reduce immigration without harming the economy. Doing so makes sense if we are very concerned about low-wage and less-educated workers in the United States. On the other hand, if one places a high priority on helping unskilled workers in other countries, then we should continue to allow in a large number of such workers. Of course, only an infinitesimal proportion of the world's poor could ever come to this country even under the most open immigration policy one might imagine. Those who support the current high level of immigration should at least understand that the American workers harmed by the policies they favor are already the poorest and most vulnerable.

[9] Figures come from the March 2009 Current Population Survey, which asks about health insurance coverage and welfare use in the prior calendar year. It also asks where respondents' parents were born. Thus, indentifying the children of immigrant parents is a simple calculation.