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## Labor Mobility and the Integration of European Labor Markets

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February 2009

# Labor Mobility and the Integration of European Labor Markets

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## **ABSTRACT**

### **Labor Mobility and the Integration of European Labor Markets**

This paper outlines the importance of labor mobility for the improvement in allocating and distributing economic resources. We are faced with an increasing lack of skilled workers and a growing tendency of unemployment amongst the low-skilled. A central political objective for the future will not only be education policy but also the recruitment of high-skilled workers from international and European labor markets. Additional skilled labor increases well-being and reduces inequality. However, internal European barriers to mobility are difficult to break through. An improved transparency of the European labor market, a greater command of languages and a standardization of the social security system can strengthen mobility. The key to mobility is in promoting the integration of international workers in the European migration process, which can be strengthened through circular migration. The European “blue card” initiative and the opening of labor markets to foreign graduates who have been trained in Europe could set a new course.

JEL Classification: F22, J15, J61

Keywords: migration, migration effects, EU Eastern enlargement, free movement of workers

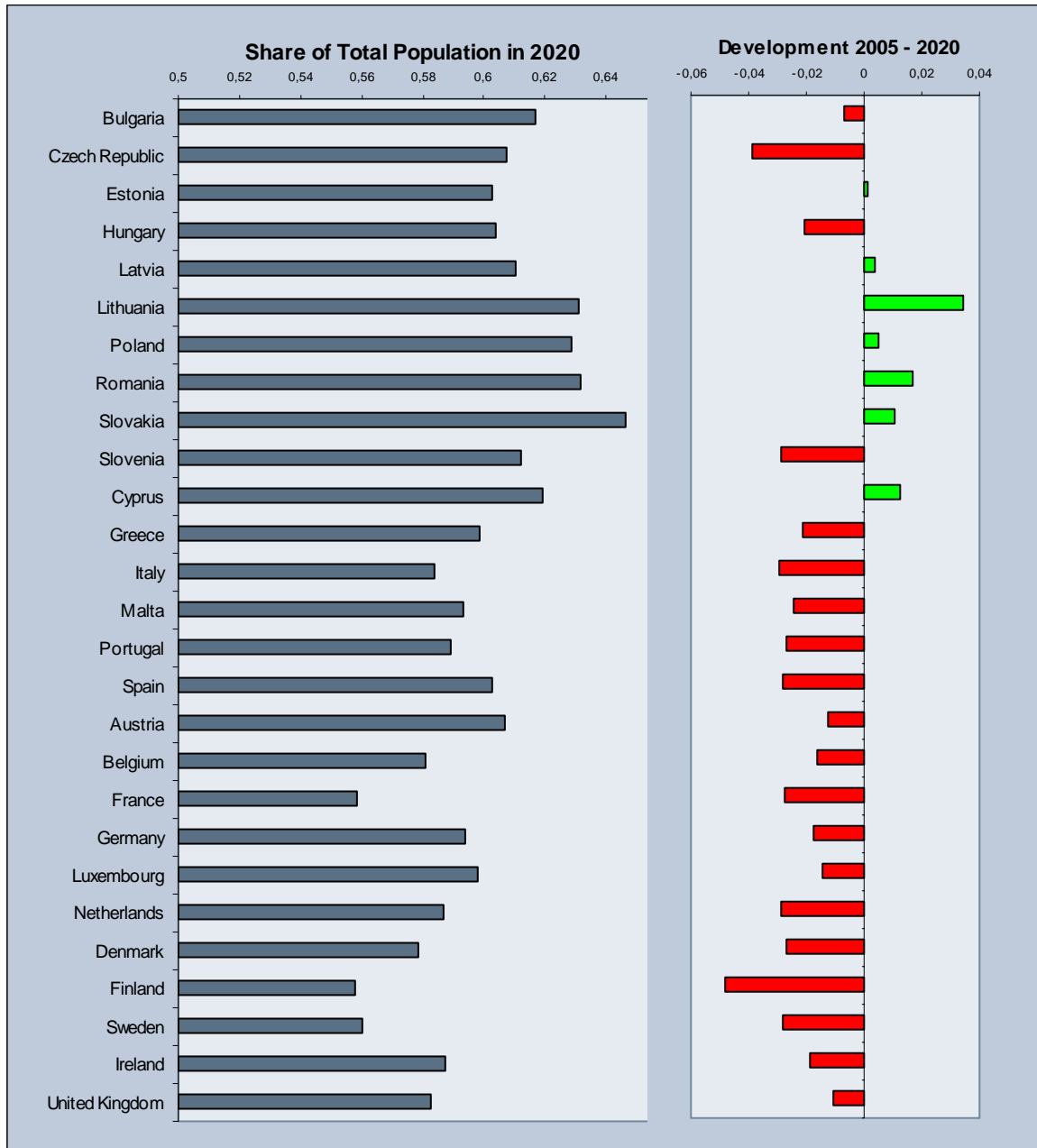
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## 1. Introduction

A globalized world and looming demographic shifts call for rapid adjustment of open economies. Due to the current global economic crisis European labor markets require new stimuli to avoid further economic decline, growing risk aversion or negative attitudes toward immigration. At the same time, demographic change presents nearly all of the old EU states with great challenges: ageing populations, scarcity of skilled labor, innovation deficits, and financial risks in social security systems. Growth, well-being, employment and social security are dependent on whether our reaction to the new challenges faced is flexible and innovative. At first glance, this will put particular demands on the factor labor, which as a provider of human capital acts as the main resource of a knowledge based society. Exchange rates and foreign trade policy have lost their significance as instruments of economic flexibility as a consequence of the euro zone and European integration. This has reinforced the importance of flexible labor markets. Past European stagnation has disciplined the manner in which wages are set, and the reality is that labor markets have become more flexible. Both real and human capital have also been more firmly embedded at the local level. In the long term, a lack of skilled labor will be the bottle-neck to expansion in developed economic regions. Human capital absorption through education and mobility policy is a key element to the future objectives of the European Union (EU) and its member states.

**Demographic Change 2005-2020**  
**Share of Working Age Population Will Decrease Across the EU**



**Source: Bonin et al. (2008) Geographic Mobility in the European Union: Optimising its Economic and Social Benefits. IZA Research Report No. 19 (Expertise for the European Commission)**

There is no indication that labor force mobility has increased in Europe. Current barriers in the form of e.g. non-transparent markets, the absence of cross-border recognition of professional qualifications and the non-transferability of social entitlements prevent not only mobility but also lead to potentially negative effects: As a consequence of these out-of-time restrictions, employment often occurs beneath the real level of qualification. Although the European Commission has already taken efforts and should continue to address obstacles in the field of coordination of national social security regimes, and transparency of qualification, the scope of intra-EU mobility in cushioning demographic ageing appears limited. Given that the share of old people relative to the working age population will increase inevitably, the demand for immigrants will increase especially within the EU-15.

**Demographic Change 2005-2020**  
**Share of Old People Relative to Working Age Population Will Increase**



**Source: Bonin et al. (2008) Geographic Mobility in the European Union: Optimising its Economic and Social Benefits. IZA Research Report No. 19 (Expertise for the European Commission)**



At the same time, the depiction of an inflexible Europe characterizes its own self-image and the image it projects to the outside world. Despite contrary efforts by the EU Commission for a European “blue card”, the EU still views itself as a fortress and not a migrant region. Therefore, it is not surprising that non-European migrants in Europe face mobility difficulties, and that the best skilled flock to the typical immigration countries of the USA, Canada and Australia. EU enlargement to the south and east has not brought about any fundamental changes. However, some key member states, like Germany and Austria, still hold on to the idea that Europe is a fortress. Ultimately, mobility both local and regional is still approached cautiously.

What are the empirical findings and causes for the immobility of the European working population? Is there an economic rationality behind this behavior? What will be the effects on well-being and distribution, and how will this affect concepts in policy which governs the economy, society and labor? We approach these issues in the following manner: first, we explain the economic framework for the effects of mobility on allocation and distribution i.e. well-being and equality. Then, we summarize what we already know about regional and international mobility in Europe. We conclude with recommendations for a European mobility policy.

## **2. Allocation and distribution of well-being and equality**

The migration of labor is typically associated with allocative, distributive and external effects (*Zimmermann, 2005a*). They generally contribute to a better employment of economic resources leading to increased production and greater well-being. One often

speaks of an improvement in allocation or an increase in social efficiency. Immigrants are especially useful in rapidly reducing imbalances brought on by the inability of native production factors to quickly adjust. However, the changes in the structure of production factors caused by this new labor also lead to a redistribution of the wages. Capital typically profits, while certain workers lose out. This can often result in conflicts regarding the distribution if unions are not prepared to accept a drop in wages as a result of immigration or less scope for wage increases. Immigrants can also stabilize social security systems with their financial contributions. They may also generate problems arising from unemployment, dependants who have come with them, or the increased burden placed on public services. Therefore, the parameters need to be kept in mind when evaluating the opportunities and risks of a migration policy. Overall, Europe has too little mobility and not too much.

This has been investigated in many studies, among them *Obstfeld/Peri (1998)* and *Faini et al. (1997)*. However, this immobility can also have positive sides (*Zimmermann, 2005a*). Internal and regional mobility of companies can replace interregional and international migration if firm or regional specific human capital plays a significant role. This human capital is lost when moving jobs, and it has to be rebuilt with the new employer. Employees typically value immobility: it enables them to form stable bonds in their social networks. Ultimately, every economy and society has to find its own balance between the utility from flexibility and its cost. Mobility can also be substituted with working at home or the internet. However, the process of moving work away from the office and to the house is proving to be difficult. Where this has taken place, however, has led to the same consequences as found with normal migration.

The effects of immigration on the native economy depend on the structure of the initial conditions and the composition of the immigrants (*Bauer/Zimmermann, 1997; Kahanec/Zimmermann, 2009a*). On the one side, the educational background of the immigrant plays an important role; on the other is the labor market situation of the receiving country. In a small open economy like Austria, flexible capital markets keep the level of interest rates constant when faced with immigration. If we at first turn to the situation of an homogenous labor market with full employment, then production increases with the employment of new workers. The wages of the native worker fall, and capital profits by the same amount the native work loses. Nevertheless, an expansion in production leads to a migration profit: were we to deduct the costs of the non-native labor force from the value of the additional production, we would yield an economic gain.

This example highlights the source of possible conflict between capital and labor in the discussion regarding immigration. This is all the more apparent when the labor market is clearly characterized by unemployment, and hence, exhibits an imbalance. Thus, unemployment would worsen with migration: in the worst case scenario, it would correspond directly with the number of immigrants. However, the competition caused by the immigration can also dismantle the rigid structure, loosen union minimum wages, raise mobility and improve the labor market situation. Even the economic lessons learned due to immigration tend to be positive. That can be easily explained considering immigrants often accept jobs which natives refuse to do or are not able to do because of a lack of qualifications. However, there is no assurance of this: social or political consequences may result from the possible economic upheaval. These considerations

frequently lead politicians to the implicit or explicit conclusion that immigration needs to be limited and controlled.

If realistic parameters are set, a completely different estimation can be arrived at. One such factor is that labor can be divided into trained and untrained workers (skilled and unskilled). Furthermore, the labor market for unskilled workers exhibits a surplus when the wages are too high; whereas the labor market for high-skilled workers is more characterized by a shortage. The three production factors of capital, skilled and unskilled labor are typically complementary: increasing one of the factors makes both the others more productive and results in better pay equilibria. If the shortage of skilled labor were to be eliminated, the wages of skilled labor would be lower and the employment rates of unskilled higher. Their wages may also increase as they become relatively scarcer.

In this situation, an influx of skilled labor is not only unproblematic but urgently required: the economic efficiency in the factor capital would rise with an increase in profits, and unskilled workers would also see their income rise while wages of the skilled would be moderated. As a consequence, there would be a reduction in inequality. (*Kahanec/Zimmermann, 2009a* show this in detail, both theoretically and empirically.) Therefore, qualified migration can lead to both more equality and better welfare. Conversely, the migration of unskilled labor is highly problematic because it raises unemployment and inequality.

Let us examine the flow of skilled labor more closely. If skilled labor has reached or is close to a labor market equilibrium, additional skilled labor may result in a drop in wages

with the complete absorption of the immigrants into employment. Thereby, unskilled workers become relatively scarcer; thus, they are in greater demand. This reduces their level of unemployment and reinforces a tendency towards higher wages. In turn, the increased employment of unskilled workers leads to a relative shortage of skilled labor. Therefore, the demand for skilled labor and their wages rise; this rise, however, tends to be lower than the previous drop. As a final consequence, unskilled employment and wages rise, whereas the aggregate wages of native skilled workers fall. The result is a reduction in the inequality between unskilled and native skilled workers.

### **3. Migration and mobility**

Since many parameters are changing globally, sustained growth, prosperity, employment and social security can only be safeguarded through a flexible market and the promotion of mobility. Labor migration leads to better deployment of economic resources and increases production. According to economic models, labor migration reacts strongly to differences in regional welfare (*Zimmermann, 2005b; Bauer/Zimmermann, 1998*). Differences in the following factors play a role: income, unemployment, cost of living, the availability of public goods and other state transfers. In contrast to this are the costs of change which arise, for example, not only through monetary costs from moving house or a loss of income in the transfer period, but also psychological costs which are incurred when a family is separated or other social networks in the country of origin are broken. According to the human capital model, the probability of older people migrating is lower than that of younger people, whose expected utility from the migration life-cycle is higher. Individuals with a better education

are more likely to migrate because they can not only expect a higher income, but they are also better at weighing up the risks of migration. They have at their disposal a greater ability of gathering and processing the relevant information. The risks and costs of migration typically grow with the distance from the destination country: information about distant labor markets is harder to obtain. Moreover, migrants circulate within familiar and ethnic networks. This leads to familiar and ethnic clusters of migration and the settling in the host country. The potential information transfer gained from this reduces the risks and costs for the migrant, thereby raising mobility.

The much criticized inflexibility of both national and European labor markets has a multitude of micro- and macroeconomic reasons. The rise in female participation in the work force results in double income households and makes the question of mobility more complex; therefore, a move is less probable. Recent years have shown the following causes for the persistently weak labor mobility: the increase in home ownership; limited transferability of social security systems; too little recognition of formal qualifications; a lack of innovation in Europe; a fall in available jobs due to low economic growth; the ageing of the working population; and an absence of transparency of European online employment exchanges. Faster trains and cheaper flights have an ambivalent effect: they can encourage a change of job to a more distant region, make commuting easier and promote a supra-regional presence without changing employment. Increasing unemployment has made the attachment to local ethnic and social networks all the stronger. Furthermore, poor language skills and cultural differences present the greatest hurdles to geographic mobility in Europe.

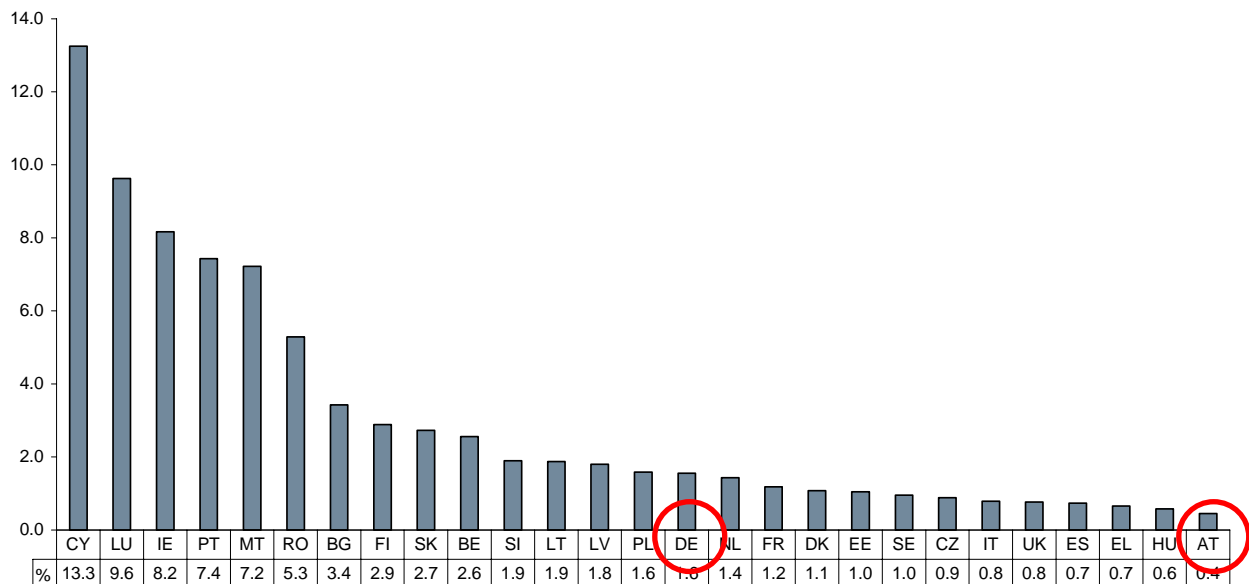
If mobility in Europe is to be measured and analyzed, a series of problems will be encountered: mobility is low, therefore hard to measure; macro-data on migration in the European Union is incomplete and contradictory; the international migration process can only be observed in segments at the micro-level; and who has migrated is compiled in the statistics of the receiving country, whereas the reference population is to be found in the data collection of the sending country. There is also a shortage of transnational surveys. Many statistics treat foreigners as migrants, neglecting their nationality, but include those belonging to the second generation with a foreign passport. Micro-economic migration studies readily fall back on individually compiled migration plans, which, admittedly, can overestimate the actual migration.

Despite these difficulties, *Bonin et al* (2008) were able to provide concrete data on European mobility. For European Union (EU) countries before eastward enlargement (known as the EU-15 countries), the share of active working age foreign-born (EU-27 or non-EU-27) is around 12.9%. The corresponding share for the new EU-12 member states is about 6%. As a comparison, about 18% of the labor force in Canada is foreign-born; 23% in Australia; and 18% in the US. Cross-border mobility in the EU-15 with regards to the population of the receiving country is 0.1% annually; whereas regional mobility is 1%.

Mobility rates and regional labor market performance are related: EU member states with higher rates of internal mobility experience smaller regional imbalances e.g. in unemployment rates. This indicates that increased geographic mobility could help to reduce regional imbalances on labor markets within the EU.

Additional data on mobile EU-27 citizens reveal low rates for all member states except for Luxembourg, Ireland, Portugal and Cyprus. The cross-border mobility rate for Germany and Austria is below 2%.

**Share of Citizens Living in Another Country  
Relative to the Population of the Country of Citizenship (2006):  
Low Rates Across the EU**



**Source: Bonin et al. (2008) Geographic Mobility in the European Union: Optimising its Economic and Social Benefits. IZA Research Report No. 19 (Expertise for the European Commission)**

Over the past 10 years about 10% of EU-15 citizens have moved temporarily or permanently to live in another country. This share decreases with age while increasing with better education. More than 30% of the citizens who have moved to another country are still living there, whereas the population share of high frequency movers is very small – only about 6.4% moved twice, 1.4% three times (*Bonin et al., 2008*).



Interestingly, job-related factors no longer seem to be the predominant factors influencing the decision to move in the EU-15, while almost 85% of the citizens in the new member states mention work and income as the core motivation for a potential move.

**Factors Influencing the Decision to Move (2007 Data):  
Striking Differences Between EU-15 and New Member States**

	EU15	NMS12	EU27
Reasons for Past Move			
Job-Related	40.5	58.6	42.3
Education-Related	14.7	12.2	14.5
Family-Related	32.2	16.6	30.6
Other	12.6	12.6	12.6
Factors Encouraging Future Move			
Work and Income	47.9	84.7	58.7
Social Network	52.8	37.3	48.3
Housing and Local Environment	71.2	57.0	67.1
Public Facilities	17.2	18.2	17.5

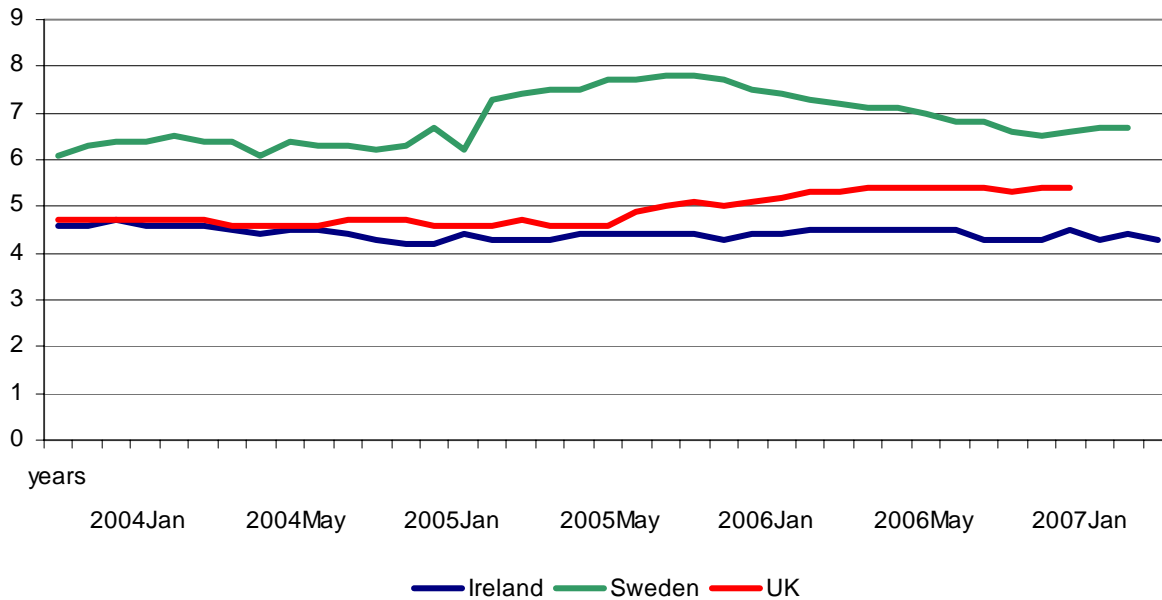
Percentage of respondents mentioning a certain factor. Regarding the reasons of the last move, job-related reasons comprise “found a new job”, “did not have a job but looked for a new one”, “were transferred by employer”; education-related reasons comprise “went to study, train, or learn a new language abroad”; family related reasons comprise “accompanying partner or family”, “went to be with family already living in new country” and “change in relationship/marital status.” Regarding factors encouraging future mobility, work and income related factors comprise “to have a higher household income”, “to have better working conditions”, “to have shorter commuting time”; social network related factors comprise “to be closer to family and friends”, “to meet new people” and “receive better support from family and friends”; environment related factors comprise “better local environment and amenities”, “better housing conditions”, “discover a new environment” and “better weather”; public facilities related factors comprise “better health care”, “access to better schools”, “better public transport”. Respondents are allowed more than one answer.

**Source: Bonin et al. (2008) Geographic Mobility in the European Union: Optimising its Economic and Social Benefits. IZA Research Report No. 19 (Expertise for the European Commission)**

Following the two stages of enlargement eastwards, which occurred in May 2004 and January 2007, it was especially Germany and Austria who decided to keep their doors closed for a transitional period. This was a reaction in defense of unemployment and the

feared “welfare tourism”. However, considerable inflows of labor migrants could be witnessed coming from the new member states to all European countries, with large numbers of migrants from Poland (for Germany, see *Brenke/Zimmermann*, 2007). Research, however, has concentrated on Sweden, the UK and Ireland.

**Free Movement of Labor After EU Enlargement 2004**  
**No Cause of Significant Rise in Unemployment in UK. Sweden. Ireland**



**Notes: Harmonized monthly unemployment rates 1/2004 – 1-3/2007 (seasonally adjusted)**  
**Source: Eurostat**

These three countries had already dispensed with entry restrictions at the first phase of eastern enlargement. As shown by *Zaiceva/Zimmermann* (2008), who summarized the hitherto research results for these countries, no negative effects for the labor market nor excessive use of the welfare system was able to be determined.

#### 4. Economic policy implications

To overcome the problems of lacking mobility in the EU labor markets, the EU has to follow a double strategy. First, initiatives have to be taken to mobilize the domestic market. Mutual recognition of professional qualifications and the full and transparent portability of social entitlements are not the only steps that should belong to the political agenda. The creation of a European online job exchange platform through a cross-linking of national agencies may help to stimulate mobility as well as a Europeanization of education policy programs. Obligatory stays abroad in the educational sector and a strong promotion of exchange programs will certainly be effective.

Secondly, while immobility can also be partially overcome through virtual networks and by providing extensive access to telecommuting, an active control of immigration is crucial to overcome the negative effects of restricted mobility. Thus, current barriers to freedom of movement for workers in the new EU member states must be abolished. A number of studies have shown that the positive outcomes of free movement of labor clearly outweigh any negative effects (*Kahanec/Zimmermann, 2009b*).

In the concept of the EU, free capital and product markets promote the integration of the European economic zone and deliver growth and well-being (*Zimmermann, 2005a*). The greatest can be expected from unrestricted labor migration, whereby initial adjustment costs cannot be ruled out from the outset. However, labor market integration and a controlled opening for skilled labor from abroad is only hesitantly gaining ground. But time is running out. Under the current economic depression, labor migration might

collapse, with detrimental long-term implications. The upcoming demographic contraction and ageing of the European labor force contrasts with the growing demand for skilled labor and the increased displacement of unskilled labor from production processes. This requires a greater internal flexibility of the labor forces within Europe and a rapid establishment of the EU as a migration destination for skilled international labor.

The world is facing a growing shortage of skilled labor, which will strike every economic nation in the long term and end in a battle for the most talented. Europe is not the first choice for the majority of highly qualified migrants. Since the EU has so far lacked a coherent common policy strategy for an active regulation of migration, it is not well positioned for the tasks ahead, but instead faces the danger of watching this on the side-lines, since the environment for labor migration has to be cultivated over time. Migration takes place in networks and builds up social infrastructures of people from diverse ethnicities. These networks need to be continuously invested into in view of the long-term, which is shown by the traditional migration countries. Otherwise, Europe will fall behind. It is not only the traditional policy of “Fortress Europe” which has outlived itself, but also the hesitant policies of making the labor markets more accessible, especially from the governments of Germany and Austria, following the latest European enlargements.

The EU commission has since then recognized and advocated more mobility within Europe proposing a “blue card” for highly qualified skilled workers. This would turn Europe into a continent of migration. Criteria for the allocation of “blue cards” should be

(i) a particular professional qualification; (ii) a contract with a business based in the EU; and (iii) an income of at least three times the level of the national minimum wage. If these criteria are fulfilled, the highly qualified worker should receive a work permit and residence visa. The “blue card” is supposed to enable the holder to work within the entire EU economic zone. This would open the possibility of strengthening cross-border mobility within Europe, which would otherwise be too difficult to achieve. This process could generate circular migration among international labor, which would help reduce regional shortages in the labor market. The path to European migration policy would then be open. National migration policies are not only superfluous in an open economic zone but dangerous. In light of the recent European history of migration policy, however, it is hardly a surprise that governments in Berlin and Vienna have voiced the loudest objections to the “blue card”. Of course, this initiative will only become compelling, once workers’ freedom of movement is achieved.

The economic contribution from immigrants can rise considerably with economic oriented migration policy (*Zimmermann et al, 2007; Zimmermann, 2005a*). Migration can be managed with the help of flexible and adjustable quotas for certain migration groups, and a selection system based on the personal characteristics of the immigrant (age, education, work experience, language skills, etc.). This would provide a larger economic welfare effect and increase immigrants’ integration skills without other migration reforms having to be modified. Economic-minded migration policy along the line of the “promote and challenge” principle can make the process more transparent, the public discussion more objective and create a basis for a broader acceptance of immigrants.

A selection process makes little sense if there is no guideline on the maximum number of permits issued. The setting for this level is for the politicians' responsibility. In the process, attention to both the long-term demographic trends and an effective determination of actual migration required are essential. The drop in population due to demographic changes and an ageing society make a steady migration of suitable groups sensible. However, the current labor requirements cannot be adequately covered by permanent immigration in cases of economic fluctuations or short-term demand bottlenecks, because these circumstances require a speedy and tailored response. This asks too much of the public authorities' ability to plan ahead and the responsiveness of migrants focused on the long-term.

Different short and long-term variations in demand require a correspondingly diverse reaction in policy in the form of a dual strategy. Permanent migration can be systematically regulated with a "points system" according to international proven models. Points are awarded with priority given to criteria like age, educational achievement, work experience or the presence of a job offer. From an integration perspective, previous stays and the presence of family in the receiving country should be weighted, along with whether they have come with children and how proficient their language skills are. In addition to this, appropriate integration offers would be made available, which would form the basis of a contract between the immigrant and the receiving country.

The most intelligent form of long-term migration policy lies in the education of qualified students who can stay in the country after their university degree if they find a job.

On the other hand, different factors need to be taken into consideration with temporary workers entering the country. Up until now, immigrants have entered the country rather randomly. The task which remains is to allow the entry of immigrants to selected segments in the labor market where there is a shortage of labor. Particular forms of temporary immigration should not be taken into account, for example workers of multinational companies or scientists, because there is no serious justification in state intervention. The actual required amount of immigrants could be “automatically” achieved by use of an auction, where a limited number of work permits and entry visas would be auctioned to interested companies. The market would react to this supply, and the activity of companies would indicate where the labor shortages are. A company would only take part in such an auction if the expected profit from employing an immigrant was greater than the costs of the auction and the search for personnel. This would only be the case if local labor supply could not meet demand. Such a method would be clearly superior to other conceivable options (fee-based scheme or levels at the discretion of government) because of the careful matching up of demand analysis and demand satiation. Furthermore, it would provide policy-makers with valuable information about current personnel bottle-necks, which could not be immediately tackled with education policy. The generated revenues from the auction could also be given to the education system.

In general, migration should be seen as a chance for new economic dynamism: Europe shall be better placed as a competitor for diminishing human capital. At the same time, imbalances due to maladaptation of native workers can be partially compensated through migration. Furthermore, migration of skilled workers produces greater social equality,

since the complementarity of high and low qualified workers provides employment and income advantages of the low qualified. To secure these positive effects, uncontrolled migration as well as low skilled labor migration has to be avoided.

## **5. Conclusion**

Despite opposing factors like multiple occupations within families, internet jobs or firm-specific human capital, the worldwide shortage of skilled workers and the importance of mobility for the acquisition and distribution of human capital have risen sharply. Hence, labor mobility is of crucial importance. Mobility contributes to an optimal allocation of economic resources that generates high output and welfare. In addition, mobility ensures a quick adjustment of labor markets, especially on the regional level. However, the rapid increase in the demand for skilled labor cannot be satisfied by EU natives only, even if mobility barriers could be overcome. The push and pull factors on the migration behavior of labor forces will once more gain importance. Specially qualified immigrants (skilled workers) are typically a considerable help in raising the welfare and distribution of the receiving country. More and more EU unskilled workers will remain unemployed unless more non-EU skilled immigrants help generate jobs for them. Even with an unchanged quantity of migration, the quality can and must clearly be raised. Therefore, economic immigration policy is absolutely necessary for future economic growth within the EU. Selective immigration is a key component of a sustainable European welfare policy. Europe needs open labor markets; an active migration policy with the help of a point system and the "blue card"; an absence of regional restrictions, also for non-EU immigrants; an active mobility policy within the EU; and intensified efforts towards



intercultural integration, which guarantees the preservation of ethnic diversity and the ethnic capital of immigrants. The governments of Germany and Austria in particular should begin to scale down their reservations towards an open labor market.

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