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## The Mobility Challenge for Growth and Integration in Europe

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## **The Mobility Challenge for Growth and Integration in Europe**

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Policy Paper No. 69  
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## **ABSTRACT**

### **The Mobility Challenge for Growth and Integration in Europe<sup>\*</sup>**

Open and flexible labor markets foster growth, development and integration in Europe. The single European labor market is still a vision, however, whereas the core challenge is a lack of sufficient mobility. The presentation discusses the value of labor mobility for economic prosperity and its determinants. Labor migration and not welfare migration dominates reality and supports economic equality. It does not depress wages or take jobs away. A brain drain for sending countries does not have to happen. Diaspora economies provide potentials for economic and political collaborations. Europe will face in the future a much higher level of circular and permanent migration.

JEL Classification: D61, F15, F22, F55, F66, J15, J61, J71

Keywords: migration, labor mobility, welfare migration, diaspora economics, circular migration

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## **1. Introduction**

It is a great honor and real pleasure for me to be here today. I feel deeply honored to have been chosen as the inaugural winner of the EIB Prize. This is not just a reflection of my own work, but that of a considerable number of co-authors and investigators as well as of the entire team at the Institute for the Study of Labor (IZA) in Bonn and at Bonn University. Together, we have worked hard, through many rounds of research, to move the needle dynamically on a proper understanding of the challenges and opportunities shaping European mobility, migration, integration and growth over the years. Without this entire team, I would not have been able to successfully undertake the research and communications efforts over the last nearly two decades.

I am especially grateful for the decision of the prize committee headed by Professor Christopher Pissarides. I also want to acknowledge by name the support of some of my colleagues who are here with me today: Professor Amelie Constant, George Washington University, Temple University and Program Director, Migration of IZA; Dr. Corrado Giulietti, Research Director of IZA; and Professor Martin Kahanec, Central European University in Budapest and IZA.

The four of us had the opportunity to present the first International Handbook on the Economics of Migration yesterday to the Warsaw scientific community at the Polish Academy of Sciences. This new book, just published by Edward Elgar, presents frontier research on the causes and effects of migration for the economy and society at large. The volume has been the output of hard work over half a decade and is written to be easily accessible to a wider readership.

## **2. The key message of my talk**

Open and flexible labor markets foster growth, development and integration in Europe -- and they increase welfare. We all have to realize, however, that the single European labor market which has been a European objective for long is still a vision. The core challenge we face remains a lack of sufficient labor mobility. My presentation today will analyze the value of labor mobility for economic prosperity and its determinants.

At the outset, it is particularly important to highlight that it is labor migration – and decidedly not welfare migration – that dominates our current economic reality. This migration also supports

economic equality. How so? Because migrants do not depress wages -- nor do they take jobs away. Rather, they foster employment and innovation and make natives more productive. A brain drain, sometimes much feared by sending countries, does not have to happen.

This applies even to the so-called diaspora economies, ethnic groups living away from home. They provide potentials for economic and political collaboration. This is an especially important finding for Europe. As we all know, our continent will face broad-based population decline in many countries not just in the future, but already now. Given that, it is a virtue, not some kind of horror prospect, that we will see a much higher level of permanent and circular migration. This is especially true because, if we allow the filter of the labor market to work, there usually is a quite remarkable form of self-selection: Generally speaking, people who migrate guided by economic conditions are dynamic and eager to work.

### **3. The global context**

With the inescapable progress of globalization, and in particular given the advances in human mobility, labor markets are bound to become more integrated. The impending demographic disruptions I mentioned before will set in with full force in the coming years in many countries.

Climate change, natural disasters and the rise of the BIC countries (Brazil, India and China) will pose additional labor market challenges. Ethnic diversity will continue to rise in importance – as both an opportunity and a threat. The rise of resources available to the developing world and the strong increase in human capital will generate more opportunities for global mobility.

All of these factors will eventually require a global reallocation of resources. This will force international and domestic labor markets to undergo major adjustment processes. The strong demand for skilled workers -- along with the fight against extreme economic inequality, the creation of 'good' jobs, as well as the increased employment of specific groups (such as the young, older, female, low-skilled and ethnic minority workers) -- will need scientific monitoring and evaluation. There is nothing "academic" about it. It is the only way to make sure at the political, economic and social levels that we will be able to initiate the necessary adjustment processes and labor market programs in time.

That is the key reason why migration economics is a fast growing and exciting research area with very significant and rising policy relevance. And that is why I hope you will consider it time well spent to let me highlight some of the key insights from that ever more important field of research and policy advice.

We all know that free trade and open labor markets are determinants of economic welfare. In his legendary 1981 book, the U.S. population economist Julian Simon claimed humans and human capital to be – in his words – “The Ultimate Resource.” He was also a strong proponent of open and free labor markets. While Simon died much too young in 1998, his vision is still very much alive. Indeed, in this age of information and knowledge capitalism, human capital has become the key driver of economic growth. And, here is the important point to remember, it can be optimized globally through migration if and when it is well-conceptualized and not badly managed.

In a recent article, entitled “Open Borders” and published in the Review of Economic Dynamics, John Kennan uses a simple static model of migration costs to show that the net gains from lifting mobility restrictions around the world would be enormous. Next, China’s strong role as a magnet in the global market for human capital will soon challenge the position of the United States leaving it to Europe to strengthen its strategy in accessing the ultimate resource to not falling behind in the race of nations. This is the finding in another recent study which was published in the Journal of Contemporary China. It is co-authored, among others, by IZA Program Director Amelie Constant and me. The goal of this article is to further stimulate the debate on the optimal use of human capital – and to explore some surprising horizons of research.

It was Professor Pissarides in his famous article with Ian McMaster on "Regional Migration, Wages and Unemployment" published 1990 in the Oxford Economic Papers who has cautioned us against too optimistic expectations from this vision. He had studied "the extent to which regional disparities in economic prosperity are removed over time by the working of the 'market system'. (p. 812)" Flexible wages and labor mobility could achieve "that an equilibrium with only compensating differentials will result" (p. 812). But his data for the UK lead him to conclude that while the market forces are at work, the processes of adjustment were very slow and "a regional policy that moved jobs to depressed areas - in contrast to relying on the movement of people to jobs - could save society considerable adjustment costs." (p. 828) The challenge outlined in this article has been a research program for me and many of my colleagues in the European context: To understand the determinants of the labor market forces and their proper regulations.

#### **4. The beneficial effects of labor mobility**

Everybody is aware that labor mobility is desirable because, in economic terms, it contributes to an optimal allocation of resources – and thus plays a crucial role in generating higher output and welfare. Such mobility ensures a quick adjustment of labor markets, especially at the regional level. Migrants have to be able to be and to stay different with their talents and abilities to be able to increase their target economy's growth potential. The societal fetish of assimilation or the melting pot metaphor are misleading concepts.

It is, therefore, vital to realize that it is not cultural assimilation, but cultural integration that is good in an economic context. Now, you may ask yourself whether that's not just a semantic difference or whether I am glossing over some potential political pitfalls. I suggest that this is not the case.

Cultural “integration” refers to a much more dynamic blending of the identities of the migrants, both of their home country and their arrival country. In a globalized world, such an active blending is bound to increase human linkages – and hence economic opportunities. In contrast, the old standby of “assimilation” captures a far more passive way of combining cultures – primarily by just focusing on blending in.

The key to it all is to focus on the migration of skilled people. This not only fosters economic efficiency, but it creates additional jobs for the unskilled as well as what we would call the differently skilled. It is also good to promote more equality, as research I did with Martin Kahanec published in the Oxford Handbook of Inequality has shown.

Hence, we find that there is no negative trade-off between efficiency and equality. Empirical evidence suggests that migrants neither take jobs away nor depress wages, and labor migrants do not typically come to take up welfare benefits. However, social tension between natives and foreigners may arise if sufficient integration opportunities are not available -- or the integration efforts fail.

This points not only to the particular future importance of research in this arena, but also to two more requirements: First, on the part of the scientists, to the need to make this research directly policy-relevant. And second, on the part of the policymakers, to consider these researchers a very



active partner to manage the future – and not some kind of fig leaf or cleanup brigade after policymaking has resulted in a near-complete mess.

## **5. The challenge of labor immobility**

Labor inflexibility has long been seen in the last few decades as the major determinant of the European employment crisis and the persistent slump of economic growth in Europe. That is why an increase in the geographical mobility of labor has been suggested as a strong instrument to foster faster economic adjustment and growth. So not too much labor migration, but too few mobility of workers has been the core of the European migration challenge.

While geographical and internal mobility can be beneficial when employed in a balanced way, migration across regions within a country and between countries within Europe has been in decline over the last decades, at least in some periods. Interregional migration has played a much smaller role in adjustment in Europe than in the United States. This suggests that interregional migration has been an important component that has driven the relative success of the American economy for many years. It is only recently, that Europe has become more flexible while the US labor market became less flexible.

Despite everything I have said so far, I realize that, in our globalized world, migration is a controversial and challenging issue. An estimated 3.0% of the world's population is currently considered to be international migrants. There is no time for me in this talk to deal with this issue properly. However, I should stress that the world is the flexibility reserve of Europe - but only in a very limited sense.

All developed economies face a strong and increasing excess demand for skilled labor. This is brought about by technological change, population aging and, in our European case, by a substantial decline in the future native European workforce. These upcoming needs clearly cannot be satisfied sufficiently by the local labor force or the educational system in the particular countries.

Europe as a whole is more and more drawn into a competition to provide the institutional settings for its companies to attract international skilled labor to fill the gaps. However, unlike traditional immigration countries such as the United States, Canada or Australia, Europe has no standing on the international labor markets for high-skilled people. That is why for us Europeans, concepts like

migration, return migration, onward migration and circular migration are the new challenges and phenomena we will rapidly need to learn to deal with in this phase of the internationalization of the labor market.

## **6. Causes of Regional Immobility in Europe**

In 2008, I directed IZA research for the European Commission. The research team including Holger Bonin, Werner Eichhorst and Kostas Tatsiramos (all at IZA at the time) found that the lack of mobility in Europe results from rising female labor market participation and less mobile double-income households, an increase in the homeownership rate, still existing barriers to the transferability of social security entitlements, insufficient recognition of formal qualifications, insufficient transparency of the European job market and online search engines, persistent long-term unemployment which leads to increased relevance of social networks for the individual, lack of language skills (main reason) and cultural barriers.

The study identified a low European annual interstate mobility (1%) in comparison with the United States (3%) and Canada (2%). The following policies to minimize labor market frictions at the national and the trans-national levels were suggested: (i) Strengthening the institutional preconditions of mobility on the labor market, (ii) Developing mobility-friendly educational policies, (iii) Creating effective information and social networks, (iv) Easing mobility barriers stemming from the diversity of national social protection and qualification systems, and (v) Extending the knowledge base and evaluating mobility-related policies.

Low European regional mobility has been considered to be a major challenge when the Euro was created. The recent so-called Euro crisis reminded me about my lecture on the Economics of Europe I gave at Dartmouth College in Summer 1997, which made the point that clear and effective rules to ensure fiscal stability and sufficient labor flexibility within a unified European labor market would be necessary to make the Euro a success for growth and welfare.

## **7. New Freedom of Movement for Eastern Europe**

Research teams lead by me and Thomas Bauer in the beginning, (now at RWI in Essen) and later by me and Martin Kahanec (now next to IZA also at the Central European University in Budapest) have early on studied the expected size of migration and the impact on natives, migrants and the

welfare take up. In various journal articles and in a book published with Springer Verlag involving also Anzelika Zaiceva (University of Modena and Reggio Emilia) and Benjamin Elsner of IZA, we found that the labor market effects on the natives were negligible.

It was only on May 1st 2011 when Germany finally opened its labor market to workers from those Eastern European countries that had joined the European Union back in 2004. After this much too long transition phase, full freedom of movement has reached Germany at last. At the time, I was here in Warsaw at a conference and observed the debate in the media which predicted another emigration wave of Poles to the West. But as you know and many of my fellow migration researchers and I had expected, the predicted large emigration did not occur.

Instead, Polish workers did Europe at large a big favor. They increased the number of circular labor migrants who were readily looking for work -- and not for welfare. These motivated people helped make European labor markets more flexible.

I want to give you two small real life examples beyond the mystical Polish plumber about Polish workers in Western Europe:

- In Germany, outside Bonn where I live and teach, the high-end vineyards employ Polish workers. When visiting such a winery just last week, the owner told us that he takes great care of his grapes and uses only handpicked grapes for his wines. When asked, he said that Polish workers are coming every fall to do this delicate and important job, and then they go back.
- In Greece, in the southern part – in Mani – the government decided to preserve the old look of the stone-built houses. And yet, apparently it was only Polish workers who still know this technique to build the stone houses. So Greeks invite Poles every time they need to build a house in Mani.

With the benefit of hindsight, we now know that Germany's policymakers have done their country no favor with their fears of overburdening the German labor market during the transition period of EU East Enlargement. High-skilled workers, who are urgently needed in many sectors of the German economy, voted with their feet and instead moved to countries such as the UK, Ireland or

Sweden. The economic message is clear: There are unassailable benefits to opening up one's labor market as early as possible for skilled labor.

Meanwhile, having lost out on the dynamic end of the market due to short-sightedness, the German government had to contend with plenty of older and low-skilled workers from Eastern Europe. They still continued to migrate to Germany through other channels such as illegal migration or self-employment.

Germany's closed-door policy pursued since 2004 therefore produced a double negative effect. Fears of Eastern European workers flooding the labor markets of Germany and other Western neighbors were completely unsubstantiated. Meanwhile, the high potentials from Eastern Europe long moved to other attractive regions of the world. That's like scoring not just one, but two own goals, to use some football language.

## **8. Immigrants in the Welfare Hammock**

Some myths never die... like the one about migrants who only come to use our welfare state as a "hammock." This stereotype persists despite numerous studies to the contrary, including an international IZA study recently prepared for the European Commission. The key finding, which was also published in the *International Journal of Manpower*, is that the generosity of welfare benefits has no substantial impact on migration in the European Union.

The team of authors (including Corrado Giulietti and Martin Kahanec) analyzed for 19 European countries from 1993 to 2008 whether national differences in unemployment benefits influenced individual decisions to migrate. The result could not be clearer: Such benefits had no impact whatsoever on intra-EU migration – the correlation was zero. Instead, the study showed that the skill level among EU labor migrants is remarkably high. While in some cases migrants are more likely to be unemployed than natives, this is rather due to ill-designed immigration and integration policies than to generous public benefits.

Moreover, recent studies show that taxes and social security contributions paid by foreigners in Germany exceed per capita expenditure on welfare benefits for the same group by about 2,000 euros annually. One of the main reasons is the favorable age structure of immigrants. This is also

why we should offer job prospects to skilled young people from Greece, Spain and Portugal, as well as from the reform countries of the Arab world.

The only thing that ought to matter is their readiness to fill the labor shortages that many German employers are experiencing. After all, that is what an advanced, globally integrated economy with a declining population ought to be doing. Never mind that empirical evidence also shows that the employment of each high-skilled immigrant creates up to three additional jobs in low-skill sectors, such as household services.

Why then do these objective facts still generate such emotionally charged opposition? What causes those strong sentiments against immigration even though the economic benefits of (properly controlled) immigration are obvious? As American and British researchers have shown, the widespread resentment is not just about the fear of losing one's job to a foreigner. It is also about a deeper-seated fear of negative changes in one's cultural and social environment.

Whether these worries are real or imagined does not really matter. If we fail to address these concerns adequately, the gap in the minds will widen – up to a point where the term “integration” might evoke a negative connotation.

## **9. Europe's Lost Generation**

There is no bigger challenge for labor economics and society at large than the profound economic crisis in Europe which has led to a situation where more than seven million young people under the age of 25 in the European Union are now NEETs – as in not in employment, education or training. This is more than a socially explosive situation. If the young generation turns away in despair from the “European idea,” the entire European project would be at risk of disintegration.

Against this background, Europe's top policymakers have rightfully put this issue at the top of their agenda. However, many of the quickly proposed remedies are ill-suited to bring about sustainable solutions. The “Youth Guarantee” scheme, which seeks to provide all young people under the age of 25 with a job or training opportunity within four months after registering as unemployed, is certainly a well-intended idea. But it would be an illusion to believe that this guarantee will amount to much more than a mere extension of the present dead-end strategy. New jobs are not created at the push of a button, nor by emergency action programs passed during political summits. The

billions of dollars allocated by EU leaders to youth employment initiatives will result in great disappointment -- if policymakers fail to tackle the roots of the crisis.

After all, we should never forget that Europe's high level of youth unemployment is not a peculiarity of the crisis, the level rose in proportion to the overall unemployment level. Its dramatic scope is a result of the economic crisis in general, paired with the continued lack of structural reforms aimed at improving the labor market situation of the young.

What Europe needs is a common labor market that is characterized by mobility, flexibility and innovative entrepreneurship. But these are precisely the areas in which the European Commission lacks the power to force the member states to implement fundamental reforms. All the more importantly, each individual country must be encouraged to do their homework when it comes to solving country-specific problems. France, for example, has created enormous labor market entry barriers for unemployed youth by setting high minimum wages and maintaining strict employment protection. Spain, on the other hand, has lots of university students in the humanities but very few vocational trainees. In Greece, medium-sized enterprises that are willing and able to train young workers are practically non-existent.

Youth all across Europe need solid, practice-oriented training. Countries like Germany, the Netherlands and Austria therefore rely on a successful "dual training system," combining the attendance of vocational schools with hands-on experience in a firm. On the downside, as German firms regularly complain, the much-appraised dual model is also quite costly. This is why the vast amount of money poured into youth employment initiatives should be used primarily to promote investment among Southern European firms who, in turn, agree to create training positions.

At the same time, policymakers should provide further incentives to enhance cross-border mobility. Even if few young people actually choose to move to another EU country, those who do, and succeed in the labor market, will be the perfect proof that the "European idea" does offer great opportunities after all – also, and particularly, during the current crisis.

For all the progress that has been made in Europe in past decades, intra-European labor mobility still leaves much to be desired. In this sense, the current grave economic crisis in countries such as Portugal, Spain and Greece offers a blessing in disguise.

People living there, especially younger professionals and skilled workers, are certainly incentivized now to make a move. Does that imbalance those societies? In particular, do we have to worry about a brain drain that sucks these countries dry of skilled people and thus makes an economic recovery harder to achieve?

I would argue that we don't really have to worry about that for three main reasons: First, the people who are moving to other countries such as Germany hail, in most cases, from the ranks of the unemployed. All that we are witnessing in that regard is that supply and demand are no longer balanced just on a national basis, but on a Europe-wide one. That is a change definitely to be welcomed.

Second, people who leave their country of birth are by no means gone forever. In fact, the contemporary trend of migration, properly understood, is best thought of as "circular migration", implying onward or return migration. Think of the proverbial Polish plumbers or of young Polish professionals who worked in Ireland during that country's boom times. These people, for the most part, never intended to emigrate for good.

In fact, many – using discount airlines – flew in for certain periods and, when not at work or on a project, also continued to live back home. In other words, they never really departed and essentially lived in two countries.

That same phenomenon can also be witnessed in Mexico today. With that country's economy growing quite strongly, and the U.S. one still lackluster, many more Mexicans would return to Mexico for the foreseeable future -- if it weren't for one particular quirk.

Because of the very inflexible U.S. immigration laws, long in need of updating (a legislative process that is still stalled), many Mexicans living in the United States don't have an official resident status. As a result, if they returned to their home country, they would not be permitted back into the U.S. by authorities, which have become much more strict in securing their country's borders.

If, in contrast, the United States had a more open, demand-based labor migration policy, as is basically in place in Europe, these people would feel much freer to go back and forth, depending on where the labor demand really is. This is just one powerful argument in favor of "circular

migration." Perhaps an even more important one is that the concept of circular migration puts many of the usual concerns about brain drain to rest quite effectively.

In a world with many fluid and affordable transportation options, ever more people want to stay connected to their place of birth. They don't just want to go back for visits every five or ten years. The difference from a few decades ago is that now migrants can remain rooted in their place of birth. Better yet, the skills, job experience and contacts they gained in their last overseas deployment effectively travel back home or elsewhere with them. They are theirs to use and exploit for their own benefit.

In short, we live in a very different world now. If we really want more European, and indeed global, integration, then it is not just unavoidable, but downright desirable that many more people from different nations will populate the future Europe.

## **10. Poland and the Euro**

Finally, in Poland, there is currently an intensive debate whether the country should join the Eurozone -- and if so, when. Let me start out by saying that it was always assumed that Poland will join the Euro when it joined the European Union in 2004. Why? For two reasons: First, because it is in Poland's best long-term interests. And second, because it will strengthen the Euro, the Eurozone and all of Europe if Europe's best transformation economy joins "the club."

I realize that some in Poland now urge, as one can hear and read, to push back the date of joining the Euro well into the future. As a visitor, I should not interfere in this domestic debate. Definitely, the decision is up to the Poles and has to be respected by the other European partner countries.

However, as an economist and somebody who has long admired the forthrightness of many Polish economic policymakers, I would like to point out the following principle: The Euro will one day be viewed as a great success story, despite the current hiccups and various initial reasons for skepticism. In the past few years, during the major global economic turmoil, the Euro served as a shield. If it weren't for the Euro, some countries in Europe would have been much more exposed, for example, Germany.



The Euro is not a dead end. The current challenges are not rooted in a typical currency crisis; we rather face the failure of some member countries to effectively enforce the necessary structural reforms and consistently comply with the agreements and obligations in terms of fiscal stability and growth-oriented policies. However, the Euro provides the chances and the pressure to enforce the necessary reforms and become competitive and ready for growth.

It therefore makes sense – both from an economic point of view and in recognition of living in a more and more globalized world -- to continue on this path of integration. Integration moves yield positive results – as I hope the thrust of my entire talk tonight has shown. And such integration moves always challenge us to do better, to improve, and never to rest on what by necessity are at best our (temporary) laurels. In short, I see no alternative for any dynamic, growth- and future-oriented economy than to participate actively in developing the Euro into a factor of stability in international financial markets. This critically means that the Eurozone also includes the eastern part of Europe, provided that the Member States fulfill the inclusion criteria. And Poland clearly is the linchpin in that strategy. Therefore, Poland should join the Euro zone with self-confidence and trust.

## **11. Conclusions**

I hope that my journey through the world of migration economics and labor economics tonight has shown you that economic research plays a significant role in determining not just our shared European future, but our common human future globally. Let me express the hope that the most productive days of what economics can deliver to politicians and the people still lie ahead.

It is in that sense that I accept the EIB Prize for what it really is – an encouragement to the entire IZA team and global network to keep pushing ahead, ultimately for the betterment of humanity. There are critical things we have learned already --- and many more we still need to unearth.

In all of this work, I am guided by one maxim – that the economic opportunities are by far greater than the risks. It is this optimism that drives me forward in my research. With that, let me thank you for allowing me tonight to lay out this rather detailed picture of many of the real challenges the economics discipline faces in the future – and what it can and what it must deliver.

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