



The Economics of Immigration

By Andrew Brod
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America has a conflicted attitude toward immigration. Of course we're a nation of immigrants. Yet once one wave of immigrants is established here, it's often suspicious of the next.

Perhaps because of this, immigration policy has been something of a backwater in American politics. To be sure, some critics have long seen the relative ease of entry into the U.S. as evidence of a fundamental weakness of both American policy and will. But rarely has immigration dominated public discourse as it has recently.

The current immigration debate is mostly about legality and fairness, not economics. Some commentators emphasize that any illegal immigrant is by definition a law-breaker. Others claim that previous immigrants played by the rules and applied for citizenship, and they demand the same of current immigrants. President George W. Bush's plan to provide illegal immigrants with a path toward citizenship has been met by vehement opposition, mostly from his own party, which damns it as an amnesty program and hence inherently unfair.

But there are also economic aspects to the debate, centered upon the claim that immigrants drive down wages in this country. The claim has been repeated so often that it's accepted as fact. But is it? Let's take a look at this claim as well as some others that constitute the economics of immigration.

- **Demand-Side Economics:** When people assert that immigration depresses wages, they have in mind a supply-side effect: An influx of people increases the supply of labor, which exerts downward pressure on wages. But what these people ignore is that there's also a demand-side effect. The influx also increases the demand for labor, as immigrants engage in retail activity just like the rest of us. More spending on products and services means that more people are needed to build stores, give haircuts, change motor oil, and so on. The resulting increase in the demand for labor exerts an upward pressure on wages.

Therefore, because immigration has a demand-side effect as well as a supply-side effect on the labor market, it simultaneously depresses and inflates wages. Which effect wins? Economic theory can't tell us, but economic data can. There is an extensive literature of empirical research that suggests that the two effects roughly cancel each other out in the short run (positive effects are more likely in the long run). For example, a well-known study of the 1980 Mariel boatlift of Cuban refugees into Miami found essentially no effect on wages. In broad outlines, immigration appears to increase labor demand by about as much as labor supply.

To be sure, there is some evidence of small negative effects for low-skill workers, and that should be a concern for policy-makers. But in some places the effect of immigration on

wages has been positive. A University of Nebraska study describes a county in which the Latino population increased ten-fold during the 1990s. The study shows that instead of decreasing wages, immigration revived the local economy and significantly increased local wages.

- **Class War?:** A study by two Harvard economists finds that immigration from Mexico “has played a modest role in the widening of the U.S. wage structure by adversely affecting the wages of less-educated native workers and improving the earnings of college graduates.” The first thing to note here is that once again, the wage effect is modest. The second thing to note is that while immigration depresses low-skill native wages by a small amount, it inflates the wages of better-educated natives by approximately the same amount. Therefore, immigration is good for rich people, but only slightly.

- **They Have Skills:** An analysis by the federal Bureau of Labor Statistics confirms the conventional wisdom that low educational attainment is more common among foreign-born workers than among native-born workers. Foreign-born workers are approximately evenly distributed among low-skill, mid-skill, and highly skilled workers, whereas relatively few native-born workers fall into the low-skill category. But highly skilled workers are equally common in the two groups: just under a third of each group are college graduates. So while the conventional wisdom is correct to a degree, foreign-born and native-born workers are equally well prepared for the New Economy.

- **State Budget Impacts:** Do illegal immigrants place an inordinate burden on state and local governments? After all, immigration is governed by federal policy but its effects are often felt locally, as immigrant children attend public schools and immigrant households avail themselves of social services.

A recent University of Florida study found that when compared to native households in the state, immigrant households pay less in sales and property tax and receive more in services. They pay less federal income tax than native households, but they pay about the same payroll taxes and they receive substantially less Social Security. All told, the state and local fiscal burden in Florida is nearly \$2,000 per immigrant household per year. Therefore, the net cost of providing services to immigrants is about \$360 per native household. Florida has a high proportion of immigrants, which tends to raise the average burden on native households. The national average is closer to \$240 per year.

The Florida study has been cited widely as support for restricting immigration, but the authors warn specifically against that: “We do not conclude from our findings that the state should either discourage immigration or limit services to non-native residents. Even from a narrow, budgetary perspective, most immigrant households are net contributors. Our point is simply that Florida’s state and local governments need to account for the effect of immigration *in their budget planning*” (italics in the original).

A study by the University of North Carolina at Chapel Hill focused on Latino immigrants and calculated a smaller fiscal burden. Latino immigrants in North Carolina contribute an

additional \$756 million per year in state taxes but cost the state \$817 million. The net burden on the state budget is \$61 million per year, or \$102 per Latino resident.

Now, of course not all segments of the *native* community contribute more in taxes than they receive in services. And the UNC-CH report noted the extensive economic impacts of Latino immigrants in North Carolina: a consumer spending impact of over \$9 billion per year and spin-off employment of nearly 90,000 jobs. It's very likely that immigration into North Carolina has softened the blow of the textile industry's decline.

• **Just Say No?:** Most of the debate over federal immigration policy has been about hardening the borders, primarily with Mexico. The president wants to dispatch National Guard units to that border and he wants a large increase in the number of Border Patrol agents. Nearly lost in the debate is the role of economic incentives in hiring illegal immigrants. If the "war on drugs" has taught us anything, it's that none of these other proposals will work unless employers face a strong disincentive to hire undocumented labor.

Economic theory implies that the disincentive can be summarized by the *expected value* of the fine, which is the probability of being fined times the dollar amount of the fine. Increasing either number—the fine or the chance of getting caught—will discourage the hiring of undocumented workers. And yet the federal government has decreased the number of worksite inspectors and along with it the probability that a given business will be fined. In 1999 the government fined 417 businesses for hiring illegal immigrants; in 2004 the figure had fallen to three.

No doubt the president's supporters in the business community aren't thrilled by calls for more worksite inspections and more stringent enforcement of current laws. Neither are some immigrants' advocacy groups. But a balanced approach to immigration policy would combine vigilance on our borders with sensible policies that address the economic incentives of employers.

The strong emotions in the immigration debate are less about economics and more about ethical concerns regarding fairness and the rule of law. Immigration overall has enriched the American economy, and fortunately few voices on either side of the debate have claimed otherwise. However, there is an economic risk of letting strong emotions take over the debate. Overly tough policies could discourage the highly skilled immigrants who have helped keep the U.S. innovative and competitive. We may have already shot ourself in the foot by clamping down hard on visits by foreign-born students and researchers in the wake of 9/11. The American economy is wonderfully resilient, but let's not further undermine it with a macho immigration policy.

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