



# POLICY BRIEF

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**The consequences of the financial crisis on foreign workers and the labour market**

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## ABSTRACT

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The financial crisis has produced a fall in the economic activities and an increase in unemployment. All workers suffered from the downturn, but some actors in the labour market are more vulnerable than others. Given that the foreign workers are particularly exposed to the downturn, immigrant integration policies should be strengthened to avoid long-term labour market exclusion. This type of policies also benefits the host community as a scarce integration of immigrants brings social tension and unrest to the community itself.

Immigration policies tend to respond to the crisis, curbing the number of people allowed to enter through official channels. Policies that aim at excessively reducing the immigration flows should be avoided, as they risk to break the flexibility that the foreign labour brings. Strict hiring legislation against foreign labour damages not only the migrants but also the host economies as they will again demand migrants to meet their labour market requirements.

## Introduction

The financial crisis and the acute loss of confidence have produced a dramatic recession worldwide. This downturn is global in its diffusion, as all the economies have been drastically hit. From its core in the US the crisis spread and reached Europe, Asia, the emerging economies as well as Africa. The fall in the economic activities and the rise in unemployment have introduced a main concern for the well-being of movers and for the future implications on immigration. The migrants are particularly vulnerable with respect to the downturn, as they tend to be employed in highly cyclical occupations, they are granted with fewer guarantees compared to the native workers and they are often not entitled to benefits. Unfortunately, a clear inspection of the effect of the financial crisis on migration is premature, as up to date data is scarce and forecasts are only preliminary. However, the existing literature provides an important guide on what we should expect for the short and long run. Moreover, past recessions can teach relevant insights.

## What should we expect in Europe

The effective reaction of the movers to the financial crisis highly depends on the type of migration flow, as some groups will react more than others. As the literature emphasizes, emigration decisions are driven by pull and push factors, with the first being related to the economic conditions of the receiving countries, while the second being influenced by events in the origin countries, such as conflicts or famine. One type of flow is represented by skilled workers, who generally move within programmes designed for highly skilled movers. For example, UK developed the Highly Skilled Migrant Programme (HSMS), which attracts nearly five percent of total migration inflow. For this type of movers both push and pull factors matter, and for this reason an eventual reduction of the inflow is unclear. The contraction of the labour market in destination countries should ultimately depress the inflow, whereas the downturn faced by skill-rich origin countries, such as India, should increase pressure to migrate. Regarding the outflow, the final outcome is as well ambiguous. The young age and the absence of family ties at destination should make skilled movers very responsive to the crisis. However, this type of labour is very flexible, as they are better positioned to change

sectors or to engage in self-employed activities, and they are also willing to downgrade to less skilled jobs. The possibility to switch sectors and activities increases their chance to find new occupations, reducing the decisions to exit. This consideration is not true in case of prolonged depression, which will eventually trigger return migration. In summary, it can be expected that inflow may slightly decline, whereas noticeable outflows will be experienced only in case of long lasting recession.

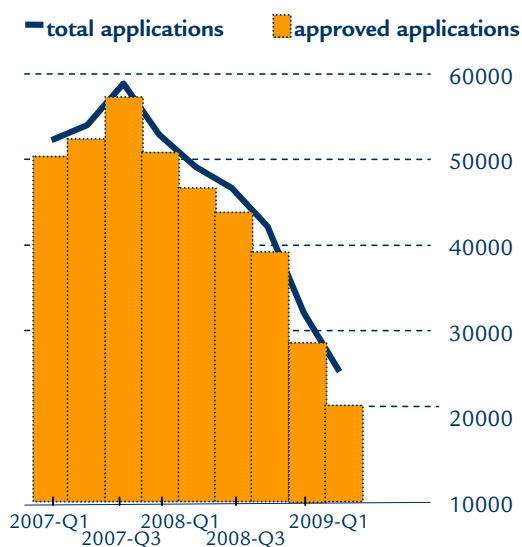
Work-permit migrants are a second type of flow. They contribute greatly to the overall flow, as they represent the second largest source of immigration, only after the A8 movers from the new EU accession countries of the Eastern bloc. Given that the immigration chance of work-permit migrants is attached to receiving a job offer, the downturn should importantly influence this type of inflow. The same is true for the outflow, as permits are tied to specific employers. The loss of jobs implies return to origin countries, unless the migrant finds a new employer willing to apply for his new permit. Work-permit migrants tend to be generally low skilled, and therefore they are more vulnerable than skilled workers during periods of recession. Low-skilled workers are more likely to lose their jobs, as employers discard workers that are more replaceable, and those with the lowest productivity.

A third type of flow is composed by unauthorised migrants. In UK, for instance, it is estimated that they represent about 10 percent of total migration. Unauthorised migration comprises foreigners who enter illegally the country, but also unsuccessful asylum seekers or those overstaying their visa become illegal migrants. Economic conditions in host countries are the main drivers for this type of flow, implying that high unemployment rates at destination should discourage illegal inflows. For example, the Department of Homeland Security in US reports a sharp drop in the number of migrants, who were caught trying to cross the Mexico-US border. The volume of arrests is the lowest since the 1970s. At the same time, border enforcements represent a deterrent to the outflow for those already settled in destination countries. Overall, it should be expected only a marginal reduction in the outflow of unauthorised migrants, while fresh inflows should decrease.

A fourth type of flow is represented by movers from A8 countries. In Europe, they constitute by far the largest flow of total migration. There is

reason to believe that these migrants are the most affected by the financial crisis and preliminary evidence for UK confirms this idea. A sharp decline in applications is registered in the Worker Registration Scheme (Figure 1). Moreover, the number of applications in the fourth quarter of 2008 and the first of 2009 was the lowest since 2004, when the EU enlargement was effective.

**Figure 1. A8 total and approved applications to work in UK**



**SOURCE: UK BORDER AGENCY. ACCESSION MONITORING REPORT (2009)**

Some motivations can be indicated for such a drastic drop. First, they are highly labour-motivated, implying that the depressed labour conditions discourage new immigration. Second, the absence of any visa requirement makes them very flexible in terms of both deciding the best time to arrive and opting for an early return to the country of origin. The crisis should influence the outflow as well. The possibility to move frequently back and forth is likely to produce a large increase in the outflow. Moreover, they are highly represented in some of the sectors most hit by the recession. For example, relevant declines in applications are registered in the manufacturing and in the construction sectors (Figure 2), which suffered the most from the downturn. Finally, A8 workers tend to have low family and social ties at destinations, and their permanence is designed to be only temporary.

**Figure 2. Changes in A8 applications by selected sectors. UK**



**SOURCE: UK BORDER AGENCY. ACCESSION MONITORING REPORT (2009)**

A fifth type of flow is represented by those moving for family reunification purposes. Given the permanent settlement of these individuals, their outflow should not be affected. Eventually, some delay in new inflows should be expected, as potential family migrants may decide to wait until the economic situation improves in the host countries.

Finally, humanitarian migrants tend to be little responsive to economic pull factors as they do not move for work purposes. On the contrary, they respond to conflict, which tend to increase as a consequence of global crises. For this reason it is unlikely that humanitarian migration inflows and outflows will sensibly change.

Overall, a massive outflow of migrants is quite unlikely, despite some categories of movers, in particular work-permit and A8 migrants, should be somehow affected. It should be noted that illegal migration will barely respond to the crisis, at least in terms of their outflow, for the motivations described above. This implies that a certain variation in the composition of movers in the destination countries is expected, with a reduction in the share of work-permit and A8 migrants and an increase in the share of illegal migrants. Moreover, even if for some categories the flows might decrease, this decline should only marginally affect the overall size of the total stock, being this contraction only few percent of the overall number of migrants.

## Migrants face high risks of unemployment

Rather than a large reduction of the stock itself, the more visible effect of the crisis will be a displacement of the existing migrants from the labour market. Migrants are more vulnerable than natives. They are highly represented in high-turnover jobs, and they barely own permanent contracts. They face language barriers which make them more disadvantaged compared to natives. Employers may choose to lay off migrants rather than natives for discrimination reasons or because during recession they prefer to invest in long lasting relationship with natives, than in short-term contracts with foreigners. For example, Dustmann, Glitz and Vogel (2006)<sup>1</sup> report that unemployment rates among immigrants are cyclical, in the sense that movers are dismissed more quickly than non-migrants during recession, and they gain employment more quickly during booms. Migrants are not entitled to benefits and this will deteriorate their welfare condition. Only the existence of a social network of conational can mitigate their welfare loss.

In terms of long-term implications of the crisis on the migrants, two considerations can be pointed. First, to respond to the crisis, an overall economic restructuring will be pursued, with some industries dying and other expanding. This in turn will bring a modification in the existing jobs and consequently some types of migrants will be ever redundant. Second, many migrants risk to remain detached from the labour market for a long period, breaking the information channel that typically spreads within the migrant network. Only after a prolonged period, the network will again be effective in passing on labour market information.

These problems highlight the need to address proper immigrant integration programmes, which are believed to be important generally, but are vital during periods of downturn, when the potential for migrants to integrate socially and economically is in great danger. Migrants who lose their jobs not only risk severe hardship during the downturn, but risk long-term labour market exclusion. This is because their skills deteriorate during unemployment, or because

their layoff is treated as a signal of low productivity. Retraining and reintegration schemes, in particular for low-skilled migrants, should be provided during time of recession. This will eventually limit the risk of exclusion from the labour market when the economy recovers. Targeted language supports can be an instrument designed to increase the productivity of immigrants, and reduce the risk of unemployment. Governments should also reinforce their effort against discrimination, in order to keep decent labour standards and protect the labour rights among foreigners.

It should be noted that integration policies do not profit the immigrants only, but their benefits spread to the host community as well. A scarce integration of immigrants brings social tension and unrest to the community, as migrants may be more inclined to channel into illegal activities and this is negative for the community.

Increased investment in community cohesion is also important, to limit tensions between movers and natives, gain good race relationships, diffuse diversity awareness among locals and eradicate an anti-immigrant sentiment. Finally, a rising xenophobia due to greater competition between natives and migrants for the limited jobs should be combated.

## The actual policies on migration

The analysis of past crises suggests that migrants are not always responsive to recessions. The link between migration flows and ups and downs in the host economies is not straightforward and changes in immigration policies hold sometimes a bigger role than the economic cycle in shaping the flows<sup>2</sup>. During the Great Depression, for example, US experienced a great decline in legal immigration, but a closer look at the data reveals that the drop started already in 1928, before the market crashed. This may indicate that the Immigration Act in 1924 had a certain responsibility for such a decline.

What we assist now is an unambiguous cut in the number of people allowed to enter through official channels. Spain reduced the quota for foreign recruitment from 15'731 in 2008 to 901 persons in 2009. Italy stopped the entrance of non-seasonal workers and plans to apply stricter requirements for residency permits. Australia

<sup>1</sup> Dustmann C., A. Glitz and T. Vogel (2006) "Employment, Wage Structure, and the Economic Cycle: Differences between Immigrants and Natives in Germany and the UK" CREAM Discussion Paper Series 0609, Department of Economics, University College London.

<sup>2</sup> Papademetriou D. and A. Terrazas (2009) "Immigrants and the Current Economic Crisis: Research Evidence, Policy Challenges and Implications" Migration Policy Institute, Washington D.C..



revised the number of skilled entrances from 133'500 to 108'100. Stricter conditions are set for employers willing to hire foreigners. Governments not only cut fresh flows but try to nick the existing stock, offering incentives to go home. The Spanish government grants some migrants from outside the EU with part of their Spanish benefits if they promise to go home and not to return for at least three years. In Czech Republic, migrants who have been laid off can obtain a free plain ticket to go home, plus 500 euros<sup>3</sup>.

It should be noted that an excessive reduction in official migration may produce the undesirable effect of increasing the illegal migration. For example, work-permit migrants may choose to switch to illegal migration if they are not allowed to renew their permission to stay. Constraining migrants to stay in their home countries for three years can damage the host economy if it recovers earlier than expected and the migrant is in demand again. Strict hiring legislation against foreign labour prevents the economy to gain from the flexibility that migrants bring.

Immigration policies tend to be cyclical, as they allow a greater number of immigrants when the economy is in expansion and a fewer number when it is depressed. However, a certain lag in the impact of the policy should be taken into account. Therefore a combination of cyclical and counter-cyclical policies should be envisaged. This guarantees a quicker response of the flows when the economy recovers in order to effectively meet the labour market requirements. Moreover, rather than curbing the number of entries tout court, the governments might operate a selection and target the admission towards movers who are most likely to integrate quickly. This also means that European countries should not try to attract only highly skilled workers, but certain low-skilled types of movers should be welcome, in order to fill in the labour shortages. Incentives to circular migration should be provided, through multiple entry visas for work-permit migrants. This allows movers to go home when the supply of labour is in excess and speed their return when the demand increases. Portability of social rights is another instrument which brings flexibility to the labour market. Movers will efficiently adjust to the economic condition, leaving the host country and returning when the situation improves.

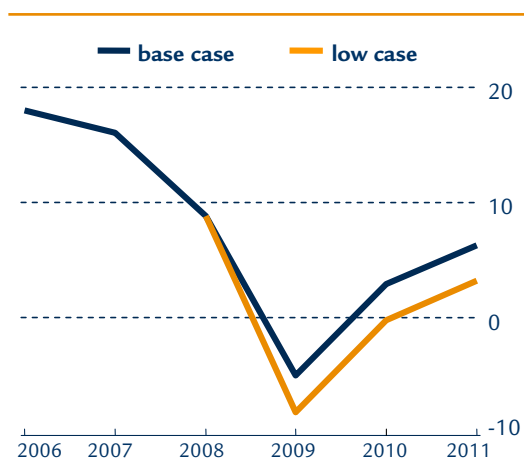
<sup>3</sup> The Economist (2009) "People Protectionism" 1st July.

## The effect on remittances

The financial crisis will undoubtedly bring a reduction in the flow of remittances. As migrants lose their jobs, the possibility to send money home is curtailed. A projection of the World Bank indicates a five percent drop in the outflow of remittances to developing countries for 2009. A more pessimistic projection sets the reduction rate to eight percent (Figure 3). These forecasts are supported by the early evidence provided by the balance of payments of the Central Banks in major host countries. For example, Banca d'Italia records a declining trend in the outflow of remittances, starting from the beginning of 2009 (Figure 4).

Such declines have negative consequences for the countries affected. Remittances finance large shares of consumption in recipient families and the down-turn will have drastic implications for the well-being of many families, which now risk to fall into poverty. Remittances represent important source of foreign exchange for many developing countries. In the current economic climate, the fall of remittances may be associated with a depreciation of the local currency, and consequently with an increase in the costs of imported goods, which is again detrimental for poor families. The advantage of a depreciation, moreover, may not be fully appreciated by exporters if demand in big markets like US and EU is depressed by the crisis. Moreover, the depreciation implies a greater cost of servicing the foreign debt.

**Figure 3. Changes in remittance flow to developing countries**



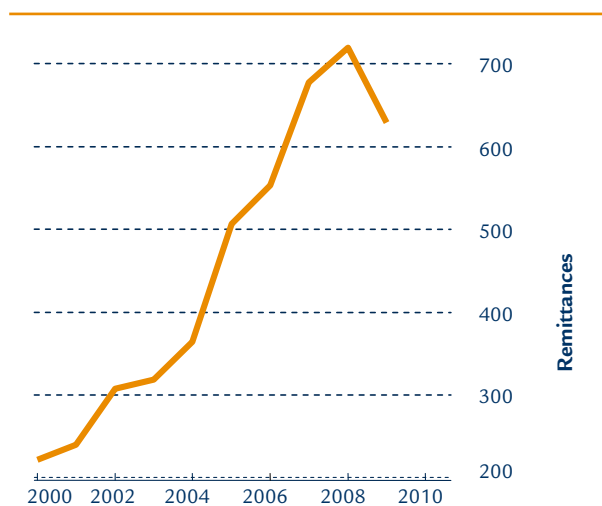
SOURCE: RATHA AND MOHAPATRA (2009)<sup>4</sup>

<sup>4</sup> Ratha D. and S. Mohapatra (2009) "Revised Outlook for Remittance Flows 2009-2011" Migration and Development Brief 9, The World Bank, Washington D.C..

These considerations highlight the risks that the crisis transmits through remittances to countries that were not hit from the beginning. In principle, the financial crisis should transmit primarily to those low income countries that display a high degree of financial integration. However, so far it appears that the direct financial transmission of the crisis has been minimal for these countries, whereas the reduction in trade, remittances, foreign direct investment and aid have produced the greatest impact<sup>5</sup>.

Even if the flow of remittances is expected to fall, the application of appropriate measures can boost the outflow of this private capital, even during time of crisis. For example, the reduction of remittance fees is likely to increase the incentive to send money home and at the same time encourages the use of official channels for sending the capital. At present, the cost for sending remittances through the official channels is not only high but also regressive, being the cost proportionally higher the smaller the size of the money sent. Easier access to banking and greater competition in the remittance industry should reduce the cost faced by migrants<sup>6</sup>.

**Figure 4. Outflow of remittances from Italy. Million Euro<sup>7</sup>**



SOURCE: BANCA D'ITALIA

<sup>5</sup> IMF (2009) "The Implication of the Global Financial Crisis for Low Income Countries" IMF, Washington D.C..

<sup>6</sup> Ratha D. (2007) "Leveraging Remittances for development" MPI Policy Brief. MPI, Washington D.C..

<sup>7</sup> The value of remittances includes the gross earnings of temporary migrants, recorded in the current account of the Balance of Payment, under the subcategory "income", and the monetary transfers of permanent migrants, recorded in the current account, under the subcategory "current transfers".

It should be noted that despite the predicted decline, remittances remain more resilient than other types of flows, namely private debt, equity flows and foreign direct investment. Given the limited possibility that low income countries have to address the financial crisis, donor supports should be strengthened rather than tightened. This will enable low income countries to attenuate the effects of the downturn on poverty. The crisis has clarified the limit of simply relying on remittances to eradicate poverty and under-development. Remittances have proved to be not ever-increasing and therefore more active initiatives from developed countries should be introduced.

### Policy lessons

The more visible effect of the crisis on immigrants is likely to be the displacement of the existing migrants from the labour market. Given that foreign workers are particularly exposed to the downturn, immigrant integration policies are essential. Retraining and reintegration schemes should be provided to displaced migrants, to limit their risk of exclusion from the labour market when the economy recovers. Increased investment in community cohesion is also important, to limit tensions between movers and natives, gain good race relationships, diffuse diversity awareness among locals and eradicate an anti-immigrant sentiment.

Immigration policies tend to respond to the crisis, curbing the number of people allowed to enter through official channels. However, policies that aim at excessively reducing the immigration flows should be avoided, as they risk to break the flexibility that the foreign labour brings. Incentives to circular migration should be provided, through multiple entry visas for work-permit migrants. This allows movers to go back home when the supply of labour is in excess and speed their return when the demand increases. The portability of social rights in favour of migrants is another instrument that brings flexibility to the labour market. Finally, the reduction of remittance fees should produce a greater incentive to send money home, ensuring that remittances do not drop dramatically during the recession.