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Broken Borders

Government, Foreign-Born Workers, and the U.S. Economy

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September 2013

The Independent Institute

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ISBN 13: 978-1-59813-169-7

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By Benjamin Powell and Zachary Gochenour

Abstract

The U.S. government interferes with the market for foreign laborers by restricting the number and mix of immigrants and setting tight quantitative limits on foreign-born guest workers. This has created a mismatch between the demand for foreign workers from U.S. businesses and their supply, directly leading to the illegal immigration situation we confront today. The current system inefficiently limits the gains that our economy could achieve from employing larger numbers of foreign workers, and it disproportionately harms small U.S. businesses. The economic fears associated with increased guest workers or immigrants are unfounded. The current Senate immigration reform proposal would be a marginal improvement but does not go far enough. Red Card, an alternative guest worker proposal, would better coordinate labor markets. Ultimately, an immigration market free from government limitations and interference would be the most efficient solution.

Introduction

Immigration policy is one of the most economically significant and politically divisive policy issues worldwide. A quota system that attempts to balance a country's labor-demand needs with concerns about the negative economic and cultural effects of immigration is current policy in most Organisation for Economic Co-operation and Development (OECD) countries. This study discusses the current U.S. quota system and evaluates its effectiveness in meeting the economy's labor needs for skilled and unskilled workers. It also investigates how different types and sizes of firms adjust their practices in light of these quotas and what policy reforms could lead to better economic performance.

The United States has had a surge of immigration since the 1960s, and immigration accounts for about half of the country's population growth. In 1965, the United States eliminated its country-of-origin quota system that, in some form, had existed since the Chinese Exclusion Act of 1875. A quota system was put in its place for various types of immigrant visas. As of 2013, the quota for family-based green cards is 226,000; for employment-based green cards, 140,000; a green card lottery for 55,000 people; and quotas for non-immigrant visas: 65,000 specialty occupation visas (H-1B) and 66,000 temporary or seasonal workers (H-2B) with an additional 20,000 advanced degree holders who are exempt from the cap.[1] The U.S. immigration quota is the largest in the world,[2] but the demand for visas far outstrips the available supply under the current quotas. Although the total number of accepted immigrants is larger than in other countries, the United States accepts immigrants only at about half the rate of other developed countries when measuring the proportion of immigrant applicants admitted. Employers of both high-skill and low-skill workers often complain that the current quota system is inadequate to meet their labor needs.

The United States began one of the largest guest worker programs in the world in the 1940s with the creation of the Bracero program, which attracted more than 4.6 million Mexican laborers from 1942 to 1964.[3] The program was extended several times at the behest of American farmers, citing ongoing labor shortages. European countries also experimented with guest worker programs, usually giving foreign workers temporary status, or relatively free border crossing within European Union (EU) member states.[4] Yet even with these programs, developed nations have far more willing workers waiting at the border than their public policies have allowed in, and in many sectors and regions demand for labor far exceeds available laborers under the current quota system.

A literature has developed in labor economics that seeks to find the optimal quota for various employment categories that will meet the labor demand but have a minimal impact on native wages. This literature affects the policy discussion,[5] and many policy proposals use the language of economics to lend themselves gravity. But what does it mean to be optimal? Is the idea of an optimal number even meaningful? How are the current quotas actually determined? How well does the U.S. quota system meet labor demand?

This paper analyzes the current U.S. immigration quota system to find out how effective the current quotas are at meeting labor demand and how the labor market might be better coordinated. Although family preference is a cornerstone of U.S. permanent immigration policy, there is a substantial fraction of the labor force living in the United States on renewable temporary work visas. Our focus in this study is on worker immigration programs, not citizenship or paths to citizenship. Our analysis is presented in four sections. "Migrant Labor Supply and Demand in the United States" shows the mismatch between employer needs and current immigration quotas, demonstrating a severe imbalance of supply and demand for migrant labor. "Differential Effects on Big and Small Businesses" discusses how the quotas affect small and large businesses differently, and analyzes how the quotas distort the market for labor. "Options for Reform" discusses policy reform options such as the recent U.S. Senate proposal, Red Card, and open immigration and how well each of these options would improve existing imbalances. "Would More Immigration Have Negative Economic Impacts?" considers whether greater immigrant flows from any of these reform options might have negative economic consequences for the native-born population.

Migrant Labor Supply and Demand in the United States

Existing immigration policy in developed countries reflects some concern for the needs of employers who want to hire migrant laborers. Several countries identify occupational shortages and use them as criteria for determining quota levels. The United Kingdom began a program in 2002 targeting low-skilled workers in particular sectors, such as hospitality and tourism.[7] Australia's government gives special consideration to immigrants in "required sectors."[8]

In the United States, guest workers must be sponsored by an employer to be eligible for a visa, and most of these employers are in high-skill sectors such as computer systems, academia, software publishing, and management and technical consulting.[9] Research in several OECD member countries indicates some severe labor shortages[10] for both high- and low-skilled labor.[11] Several European governments have undertaken studies to determine labor needs across various sectors, and have used the results in their immigration policy prescriptions. In each case, the method by which labor shortages are measured differs. We look at the magnitude of shortages in the U.S. labor market and how well the quota system matches supply and demand.

Migrant Labor Supply

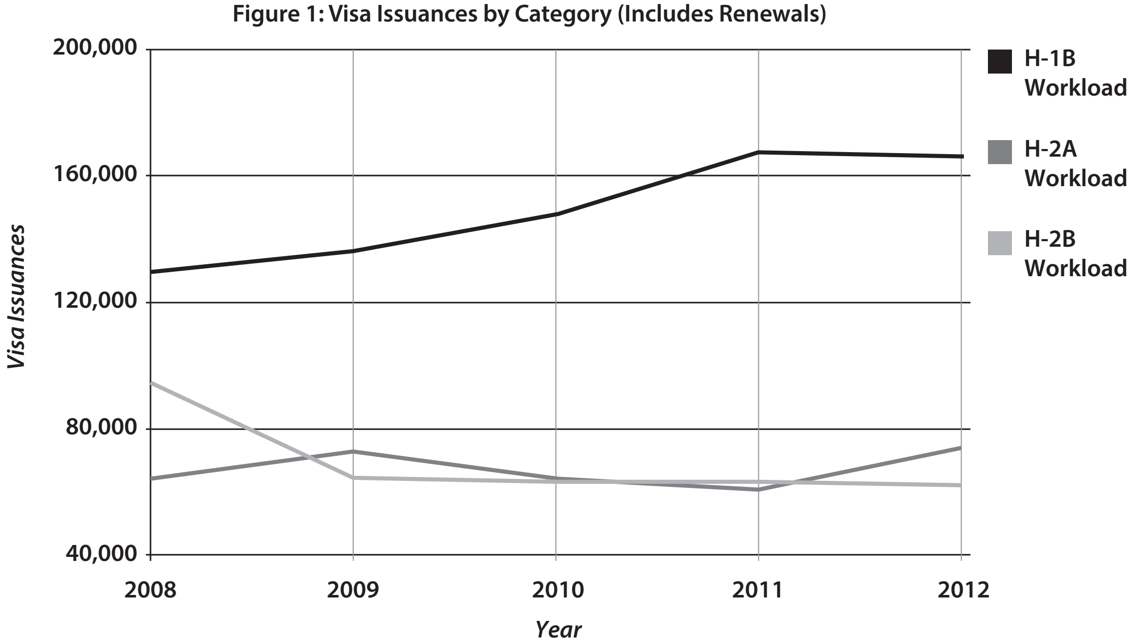
For employers unwilling to unlawfully hire undocumented immigrants, the supply of immigrant labor across categories is approximately equal to the number of visas issued, including renewals. Figure 1 shows the recent quantities of U.S. visas issued by category.

The most quantitatively important nonimmigrant visa categories are H-1B (specialty occupations, 165,524 workers)[12], H-2A (temporary agricultural occupations, 73,387 workers) and H-2B (temporary nonagricultural occupations, 61,901 workers). The number of issued H-class (guest worker) visas has remained relatively stable for the past decade, averaging about 300,000 issuances per year when accounting for H-4 class (immediate family members of H-1B visa holders).

The supply of visas is fixed through political channels and does not adjust dynamically to market conditions. Large firms with significant political capital may be able to secure exceptions for their industry, but most firms lack any ability to influence these channels directly. If employers want to hire foreign workers after the quota has been filled, their options are to hire illegally or relocate some aspect of their businesses to foreign soil.

There are approximately 11 to 12 million undocumented workers in the United States.[13] Many have been denied visas of any kind and decided to come to the United States to work anyway; others may have never applied because they did not know the procedure or because they recognized that the chances of being selected for any of the categories, especially for permanent status, were slim. Since the cost of illegally crossing the border is now so high (about $4,000[14] in 2009), it seems

Figure 1: Visa Issuances by Category (Includes Renewals)



Source: USCIS

reasonable that a much larger number of foreigners would be seeking work in the United States if the cost of doing so was lower.

There is little doubt that the supply of labor is severely depressed by the quota system and border enforcement. Each year, the cost of border crossing increases. Many growers, particularly large industrial farms, are moving more of their food production overseas. Skilled workers suffer from the same problem: interest groups for the technology industry, and some companies like Facebook, have expressed concerns about a shortage of competent domestic workers for Science, Technology, Engineering, and Mathematics (STEM) jobs.

Migrant Labor Demand

Estimating the demand for nonimmigrant visas is not easy. Many potential applicants do not bother to apply because they believe their chances of receiving a visa are low, or the cap has already been reached, and therefore looking at the number of total applications will not give a good estimate of the demand for work visas. Still, there are rough measures that will elucidate the mismatch between supply and demand currently plaguing the labor market.

One measure of demand we can use is the date on which the nonimmigrant visas reach their annual quota. Technically, the application process is year-round and decisions are made on a rolling basis; in practice, the quota is usually met soon after the first day applications are allowed. In 2013, the cap was reached on April 5, just five days into the application season for the next fiscal year, which begins on October 1. Table 1 shows the dates for the past several years that the quota cap was met.[15] The U.S. Citizenship and Immigration Services (USCIS) begins accepting applications on April 1 each year, six months in advance of the coming fiscal year when these visas will be valid. The Government Accountability Office has stated that demand perpetually exceeds the cap for H-1B visas.[16] While in some years demand is greater than others, demand exceeds supply even in recession years; typically, the cap is reached before the fiscal year begins. This makes it particularly hard for businesses to plan ahead for their upcoming year's labor needs.

TABLE 1[17]

Fiscal Year	H-1B Cap Reached	H-2B Cap Reached (First Half / Second Half)
2014	April 5, 2013	Not met
2013	June 11, 2012	Not met
2012	November 22, 2011	Not met
2011	January 26, 2011	Not met
2010	December 21, 2009	Not met
2009	April 7, 2008	July 30, 2008 / January 16, 2009
2008	April 3, 2007	October 1, 2007 / January 2, 2008
2007	May 26, 2006	December 15, 2006 / March 27, 2007
2006	August 10, 2005	December 16, 2005 / April 6, 2006
2005	October 1, 2004	Not met
2004	October 1, 2003	Not met

The demand for visas increases during economic expansions. In some sectors, such as computers, the disparity has been getting even worse. For instance, the number of U.S. college students graduating with computer science degrees in 2013 has declined by 43 percent since 2004,[18] but labor demand in the computer software and information technology (IT) sectors is robust.

H-2A visas are not included in the table because there is no statutory limit on the number of temporary agricultural workers that can be brought in under the H-2A visa program. However, visa issuances are limited by the application process that requires potential employers to engage in the costly task of demonstrating that no native workers will be displaced by this plan. H-2A regulations require employers to hire any U.S. worker who applies, even if it means displacing migrant workers. There are currently about 30,000 workers in the United States under the H-2A visa program, only a small fraction of the total agricultural labor force.[19] In this case, a better method of estimating demand is simply to ask the employers directly. The Western Growers Association, an advocacy group for California farmers, reported a 20 percent drop in farm labor in 2012. Average wages have risen considerably, forcing many growers to abandon crops or make inefficient investments in labor-saving machinery. Only 5 percent of the U.S. agricultural labor force is currently employed under the H-2A program, which allows workers to stay for one year only and does not allow them to change jobs. The Western Growers Association also estimates that 80,000 acres of fruit and vegetable production have moved out of California because of the labor shortage. Farm crews have been operating at less than 70 percent of their pre-2001 size, when border enforcement toughened drastically.[20] Growers estimate the shortage to be at least 20 percent of the size of their current labor force.

How to Balance Supply and Demand

Many countries, including the United States, find it is much easier to get political support for expanding high-skilled immigration rather than that of low-skilled workers. Although high-skilled jobs (such as those in STEM fields) may be the fastest growing in percentage terms,[21] the *volume* of job openings indicates that some of the biggest labor market needs are in low-skilled sectors. Only about 5 percent of U.S. jobs are classified as STEM jobs, for instance.[22] Most illegal workers are low-skill, but low-skill workers account for only a fraction of the total number of visas issued each year.

Another problem with the current quotas is that they do not respond to regional needs because visa holders aren't free to migrate throughout the United States while changing jobs. The United States harnesses market forces to determine optimal interstate migration for domestic citizens. One of this study's authors recently moved from Massachusetts to Texas. He weighed the value he could create in Texas (measured by the salary he was offered) against the value he could create in Massachusetts, while also considering cost of living differences and other factors. Market forces dictated that he could, on net, create more value in Texas. No government planning or quota system was necessary to make this determination. Unfortunately, worker visas that tie employees to employers before they even get here do not allow them the opportunity to continue to re-sort to find where they can create the greatest value in our economy. But absent the market's process of discovery, no visa planner can know in advance where prospective workers best fit.

The sorting mechanism that is best fitted for finding where immigrants should locate and what they should produce is the free market. In that setting individuals and businesses contract voluntarily, and wage rates balanced against the cost of living provide incentives to distribute the workforce efficiently, both geographically and by sector. When labor mobility and wages are tightly controlled, shortages are the likely result. Strict state laws or sporadic immigration law enforcement crackdowns may amplify the problems in particular regions.

It is important to consider the question of whether policymakers could possibly know the "right" or "optimal" quota level. Knowledge of labor market conditions is dispersed throughout the economy and government planners do not know the specific circumstances of time and place that entrepreneurs and workers "on the spot" know.[23] Central planning of economic activity has a dismal track record, and the labor market is not fundamentally different from other markets that are impossible to plan. Market conditions are changing constantly, and any quota that might seem appropriate for one time and place will not work in another. The prices and quantities of labor, just like other goods and services, need to be continually discovered anew by decentralized bidding between workers and employers.

No one knows the right quantity of labor in any given sector absent this process.

Before considering policy reforms that would help better coordinate migrant labor markets, it is worth considering how differently the current quota system impacts large and small businesses.

Differential Effects on Big and Small Businesses

Immigration restrictions affect small businesses disproportionately compared to large multinational businesses. Restrictions reduce the overall supply of labor, thus raising the economic cost of hiring labor as an input into a firm's production process. Large firms respond to these restrictions primarily in two ways: by increasing the number of outsourced or offshored to jobs in places with lower labor costs, and by lobbying the government for privileges and exceptions. Small firms, which do not operate at the scale necessary to hire overseas labor and do not have seats at the political bargaining table, are left with fewer options.

Multinational firms often do not need to offshore their jobs in order to access high quality foreign workers. L-1 visas are available only to foreign employees of international companies with offices in the United States and abroad. Companies can use the L-1 visa to bring workers from a foreign site to the United States for a period of seven years. Small businesses with limited or no international presence are not able to use L-1 visas to help mitigate labor market restrictions.

The visa application process itself favors large businesses, who can afford the large fees: official H-1B filing fees exceed $1,500, although small businesses of fewer than twenty-five employees pay a nominally smaller amount. Petitioning for employees often requires the assistance of a lawyer; while many large firms have in-house counsel well versed in immigration law, small firms usually do not, as these lawyers charge an average of $3,000 per applicant. The problem is even worse in low-skilled sectors like agriculture: H-2A visas last one year only and demand applicants to pay filing fees and go through complicated petitioning processes. Many would-be H-2A sponsors cannot afford the fees, which represent much larger fractions of the total labor cost for these lower-skilled workers than they are for higher-skilled workers.

Companies outsource in order to avoid certain types of costs, including the high cost of labor in the United States. Marginal labor productivity is much lower outside the developed world, owing to many factors, such as a lack of human and physical capital or, more importantly, an absence of strong property rights institutions that incentivize investment. Despite the low productivity of these workers, multinationals find it profitable to set up their manufacturing facilities and other enterprises in the developing world where labor supply is much greater and wage rates are lower. Worldwide employment by U.S. multinational corporations is increasing, accounting for 34 million jobs in 2012.[24] Furthermore, the proportion of U.S. jobs that are "offshorable" is increasing.[25] Large companies can afford to bear the large fixed cost of maintaining at least part of their manufacturing processes internationally, which allows them, in a sense, to circumvent immigration restrictions. The jobs move when the people cannot do so. Immigration restrictions sometimes can even be beneficial to large businesses because the restrictions disproportionately hurt their small business competitors, who are less able to negotiate their way around them through offshoring.

Only a small fraction of small businesses are able to offshore any of their labor directly, although many will elect to import materials they would otherwise produce themselves. Small businesses often do not have the resources, such as personnel with foreign-language skills, travel budgets, and the ability to deal with international legal bureaucracies, to conduct much business overseas. Small businesses usually lack in-house legal counsel, and their lawyers typically do not know about international regulations. Therefore, small businesses disproportionately need local labor in order to thrive. When the costs of engaging in international business are too great and small businesses can't access foreign workers who wish to move to the United States, they find themselves investing in economically inefficient labor-saving alternatives or ceasing production completely.

Another difference between small and large firms is their ability to lobby successfully for exemptions and policy changes. Although it is difficult to estimate the magnitude of the effect, it is clear that large industries or industry organizations are in better position than smaller ones to influence Washington. The expansion of the H-1B program in the 1990s was due partly to the lobbying efforts of big Silicon Valley firms. The latest (2013) immigration reform bill in Congress contains more than 400 waivers, exceptions, grants of discretion, and exemptions.[26] For instance, the hardship exception in Section 245D states that "the Secretary may adjust the status of a registered provisional immigrant to the status of a lawful permanent resident if the alien . . . demonstrates compelling circumstances for the inability to satisfy the requirement." There are no bright-line criteria for what qualifies as "compelling circumstances," but big businesses and lawyers with more experience with the system will be best positioned to demonstrate this hardship. Another exception, dubbed the "Facebook exception," applies to any company that applies for permanent residency for its overseas foreign workers and allows these companies to avoid new paperwork and wage requirements. Small businesses simply do not have the political capital, or the foreign labor force, to take advantage.

Although the current immigration quota system starves both big and small businesses of needed workers, it is the small businesses that are hurt disproportionately. Big businesses are more able to move the jobs to laborers overseas than small businesses are, and they are better at securing favorable treatment from a government which allows them more opportunities for bringing foreign workers to the United States.

Options for Reform

Immigration reform holds an important place in U.S. politics nowadays, and it was a major issue in the 2012 U.S. presidential election. Although many people agree that there is a need for reform, there is far less agreement on what reforms would be beneficial. We will analyze how a few options would affect economic efficiency and address the disparity between large and small businesses.

Expanding Existing Quotas: 2013 Senate Bill

Perhaps the simplest reform is simply to adjust the immigration quotas in order to augment the supply of foreign labor. The 2013 Senate Bill[27] essentially does this, expanding existing visa categories and creating some new ones. For instance, it increases the cap on new H-1B visas to 65,000 to 110,000 in the first year and to as high as 180,000 in future years. The bill creates a new government bureaucracy, the Bureau of Immigration and Labor Market Research (BILMR), which is responsible for collecting market data and setting new caps. Increasing the total number of immigrants across the board undoubtedly will help alleviate the labor shortage, but what is the right number? If we reject the idea that government bureaucrats can determine the optimal number of immigrants in various industries, sectors, or regions, then simply tweaking the quotas will not solve the fundamental problem.

The 2013 bill proposes to create a new visa category, the W visa, which would start out at 20,000 per year and increase gradually to 200,000. The number would fluctuate based on market conditions like wages and unemployment as determined by the BILMR. Under this category, foreigners with low skills would be able to apply for jobs in the United States. Registered employers, who must apply to participate in the program, will be allotted a certain number of visas each year. These visas would be issued on a three-year basis, renewable for another three years. The number of visas would be capped at 20,000 the first year and increase to 75,000 by the fourth year, at which time the annual cap would be based on a to-be-determined formula that would consider the number of new job openings, the number of unemployed U.S. workers, and the number of W visa applications. Such a plan, although likely an improvement over the current system of hard caps, would be subject to the above criticisms of centrally planning the labor market. Monitoring labor market conditions and setting new quotas every year would be a costly endeavor. Furthermore, the Senate bill calls for quotas to be broken down by industry, and many of the proposed quotas are completely out of line with existing market demand. For instance, construction visas were limited to 15,000 per year, a drop in the bucket for the construction industry, which now employs 5.8 million people.

In order to make the Senate bill appealing to anti-immigration groups and voters, a number of onerous controls were included. For instance, "agricultural equipment operators" are to be paid exactly $11.30 an hour, while crop harvesters make $9.17. But the government doesn't know the correct price for these types of labor any more than any other price, and market conditions surely fluctuate. These price controls, like all other price controls, will cause needless shortages and surpluses in these labor markets.

Furthermore the bill mandates the use of E-Verify nationwide, a database system that enables employers to verify employee information in state Department of Motor Vehicles databases. The system has a relatively high error rate.[28] For example, when Arizona's 2007 immigration law mandated the use of E-Verify for all hires, MLC Enterprises, which owns 24 Burger Kings in the state, reported that 75 percent of its foreign workers were rejected by E-Verify but all were later cleared for legal employment.[29]

This bill does nothing to address the disparity between large and small businesses, since there is no reduction in the fees and fixed costs for hiring migrant labor. By expanding current programs, those companies who currently enjoy an advantage because of their ability to deal with the bureaucracy should expect to continue to do so. Simply expanding the number of visas, although an improvement, falls short of the needed degree of reform.

Red Card

Red Card[30] is a policy proposal that would greatly expand the role of the guest worker programs in the United States. Private employment agencies would open offices in foreign countries to facilitate the process. The agencies run background checks, link specific workers to specific jobs, issue smart cards and track workers, and would be responsible for compliance with all U.S. laws. Each worker would carry a card that digitally stores information about that worker and his or her current job: the employer, location, and duration of that worker's stay.

This system has several advantages. The major one is that it does not limit the number of guest workers that could come to the United States. A second major benefit is that, with the quantitative limit removed, the government doesn't have to try to manage the immigrant labor supply across industries. Instead, market forces would be harnessed to dictate the quantity and distribution of guest workers, across industries, geographic space, and time.

As a political matter Red Card has some appeal to immigration critics as well. It is a guest worker program, not an immigration program with a pathway to citizenship. By creating a guaranteed method of accessing available U.S. jobs legally, it should also dry up the demand for today's illegal immigrants, thus encouraging them to return home to apply for legal status without any major

U.S. enforcement efforts. The system would enable the U.S. government to monitor and track movements across the U.S. border more effectively, because it would reduce the incentive to cross the border illegally. Furthermore, the use of smart card technology, which links each worker to a particular job, will reduce the costs of monitoring and enforcement, although it is possible that this could suffer from some errors as E-Verify does.

Red Card would also help to eliminate the disparity of treatment between large and small businesses. Small businesses could especially benefit because many of the fixed costs of hiring guest workers would be reduced or eliminated by this program. By allowing for relatively unrestricted cross-border labor mobility, Red Card would eliminate the need for companies to relocate jobs to outside the United States due to domestic labor shortages and would allow small businesses to hire locally without special privileges to secure more workers by opening foreign offices. Small businesses would also feel more secure in hiring Red Card holders than migrant workers under the current system, because the technology allows for simple, uniform enforcement.

Concerns about immigration often revolve around the problems of providing a "path to citizenship." But solving the mismatch of labor supply and demand does not necessarily imply granting permanent residency, citizenship, or voting rights. Red Card is politically viable precisely because it separates these issues by allowing as many guest workers as employers are willing to hire while not favoring these workers by offering a faster path to permanent residency or citizenship than would be available to any other would-be immigrant living abroad. Although this feature is a political strength of Red Card, it is also a limitation to the good Red Card can achieve because it leaves a large class of workers who desire to reside and work in the United States permanently with no legal way of doing so. For them, a more radical reform is needed.

Free Immigration

A radical solution, given today's political climate, would be a transition to completely free immigration, eliminating the need for guest worker programs entirely. Although radical sounding today, it was the norm for the United States during its first century. Until 1875, the United States had virtually open borders, and immigration peaked during the late nineteenth century and was accompanied by historically high economic growth. As the world's primary destination for immigrants, the United States enjoyed a rapidly expanding labor policy, which allowed businesses to hire as many workers as they wanted. This same dynamically adjusting labor policy could help drive the modern U.S. economy just as it helped fuel the growth of the nineteenth century. Free and open immigration is superior to the other options discussed here in terms of cost of administration and ability to adjust dynamically to changing market conditions. Free immigration is an idea met with strong resistance from across the political spectrum, but as a practical matter it may be the most economically sensible solution.

Instead of creating new bureaucracies, opening the border could eliminate entire bureaus, lowering the costs to U.S. taxpayers considerably. The United States could better maintain border security because the guards could focus on keeping out violent criminals rather than peaceful people attempting to cross the border for work illegally. Free immigration would eliminate the costs associated with guest-worker permits and applications, and it would level the playing field for big and small businesses and lower costs for those employers.

Most importantly, free immigration is the only solution that does not distort any market signals. Many labor decisions for both employers and employees are best made on the spot, so any process that needs to be started months in advance or does not let employees easily switch between jobs once they are in the United States is inefficient. Free movement of labor is the only way to ensure that labor demand is being met: in a free market for labor without artificial controls, there is no such thing as a labor shortage, as wages will adjust to meet the changing market conditions, and workers will flow in and out depending on the quality and quantity of opportunities.

The economic gains associated with adopting this policy truly could be enormous: a 2011 study[31] estimated a one-time gain to world GDP of 50 to 150 percent if a free immigration policy were adopted worldwide, with most of the gain coming from workers who currently live in low-productivity countries moving to high-productivity countries such as the United States.

Much of the resistance to unlimited guest worker programs or limitless immigration to the United States is based on fears of negative economic consequences that are largely unfounded.[32] It is worth considering some of the more prominent of these myths.

Would More Immigration Have Negative Economic Impacts?

Contrary to many popular fears, immigrants improve the economic welfare of the native-born population. Free trade in labor, like trade in goods and services, frees workers to exercise their comparative advantage. In fact, the basic economic case for free trade in labor is not fundamentally different than that for trade in goods and services.

Trade barriers for goods and services have fallen considerably since the establishment of General Agreement on Tariffs and Trade (GATT) in 1947. Support for free trade in goods and services commands more consent among economists than virtually any other issue. In fact, free trade has been a core issue for economists ever since Adam Smith's *An Inquiry into the Nature and Causes of the Wealth of Nations* (1776).

The basic case for free trade builds on the fact that different people, in different places, have different abilities to produce goods and services. If governments allow them to trade freely, market forces naturally will push each person (and country) to produce those goods and services that they can produce at the lowest relative cost and import those goods and services that they could produce only at greater expense. As a result, market exchange creates more wealth than would be created in the absence of such exchange.[33]

Substitute labor mobility for the mobility of goods and services and the process works in the same way. Given his or her abilities, interests, and costs, each laborer moves to where he or she can create relatively more value for others. If capital, natural resources, and goods and services were all perfectly mobile, labor mobility wouldn't be as economically important as it is.

But barriers to trade in goods and capital flows remain; some services must be provided in person, and, by definition, many natural resources are in a fixed, geographical location. Thus, labor mobility remains crucial for our prosperity. In fact, gains from increasing labor mobility would greatly dwarf the gains that could be achieved through further removal of barriers to capital flows and trade in goods and services.

Economist Michael Clemens has documented that completely eliminating global barriers to immigration would result in net gains of $30 trillion to $90 trillion for the world's economy (50 to 150 percent of world GDP).[34] Even a smaller migration of 5 percent of people from poorer parts of the world to wealthier parts would exceed the wealth gains that could be had by eliminating remaining trade and capital flow barriers.

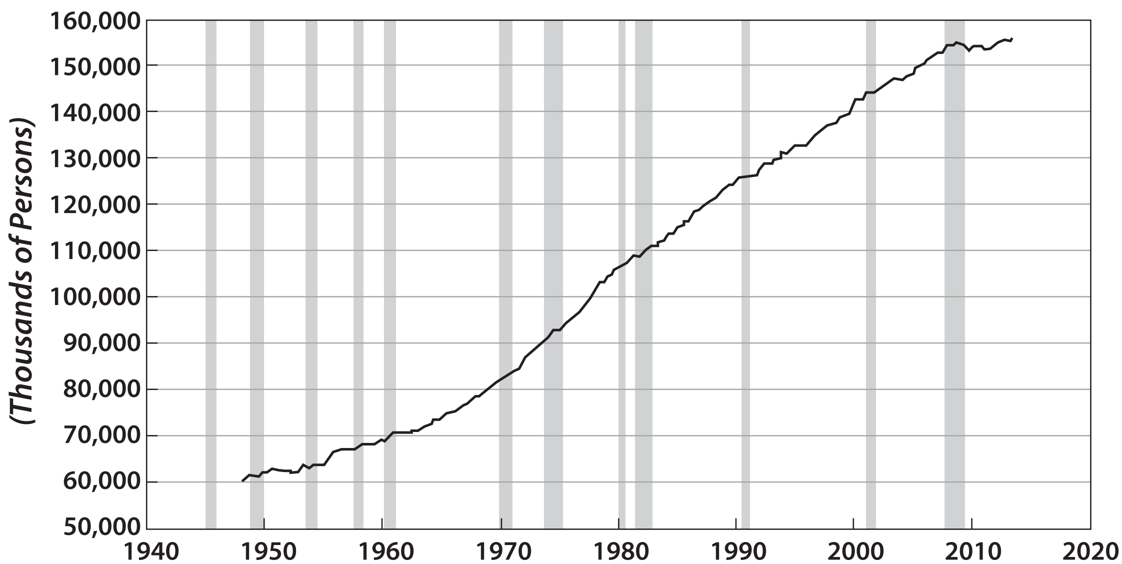
Of course, many of the benefits Clemens estimates would go to the immigrants themselves. What about the net benefit of immigration to the native-born population? Harvard economist George Borjas is probably the most widely known academic critic of unfettered immigration. But even he admits that immigrants create net benefits for the native-born and, in the *Concise Encyclopedia of Economics*, puts this gain at $22 billion a year.[35] Using his method of calculation, and updating for more recent immigrant flows, puts the number at approximately $41 billion.

Relative to the $15 trillion U.S. economy, $41 billion is rather small. Other methods of calculating the net benefits of immigration lead to larger numbers, though all remain modest as a percentage of our economy. However, it is important to keep in mind that the current level of benefits that natives derive from immigration is related directly to the U.S. government's restrictive immigration policies. Obviously, more immigrants would increase our gains. Also, as we've documented above, the current immigration quota system does a horrible job of letting immigrants work in economic sectors in where they would be the most beneficial. However modest the net gain to the entire economy might be, the important point is that economists have wide agreement that immigration, like free trade, brings net benefits to the existing native-born population.

That immigrants "take our jobs" is probably the most repeated and most economically ignorant objection to immigration. It's a classic example of Bastiat's "broken window fallacy" ("what is seen and what is not seen").[36] Everyone can see when an immigrant takes a job that was held by a native-born worker. But not everyone sees the secondary consequence of the new jobs that are created because native-born labor has been freed up for more productive uses. In the market's process of creative destruction, jobs are created and destroyed all the time.

If immigrants really did, on balance, take jobs, from existing native-born workers without new jobs also being created, the same should be true any time we add more workers to the economy. Is it? Since 1950, there has been massive entry of women, baby boomers, and immigrants into the work force. As Figure 2 shows, the civilian labor force grew from around 60 million workers in 1950 to more than 150 million workers today. Yet there has been no long-term increase in the unemployment rate. In 1950, the unemployment rate was 5.2 percent, and in 2007, the year before the recent economic downturn, the unemployment rate was 4.6 percent. As more people enter the labor force, more people get jobs.

Figure 2: Civilian Labor Force (CLF16OV)



Shaded areas indicate U.S. recessions.
2013 research.stlouisfed.org

Source: U.S. Department of Labor: Bureau of Labor Statistics

Immigration advocates often argue that "immigrants do the jobs Americans won't do." Critics of immigration often reply that if the wages were higher, Americans would be more willing to do the jobs. However, this reply overlooks the fact that if wages were higher, many of the jobs simply wouldn't exist. Approximately one-third of all garment workers in the United States are immigrants. If wages needed to be higher to get Americans to take the jobs, many of these jobs would have gone overseas. Examples abound of farmers deciding that it was better not to produce than to pay higher wages. In Arizona, for example, only 30 percent of the 2004 lettuce crop was harvested; the rest was left in the ground to rot. Losses amounted to nearly $1 billion. Farmers certainly could have paid higher wages to get the crop harvested, but the losses would presumably have been even greater.

This leads to the third, most common economic objection to immigration. Any student who has taken an introductory economics course would think, quite plausibly, that if the supply of labor increases, more workers will be employed, but the wage rate will fall. The first part is true: as noted above, more workers are employed. However, the second part is not: wage rates don't fall. A survey of the economics literature on immigration concluded that

> [d]espite the popular belief that immigrants have a large adverse impact on the wages and employment opportunities of the native-born population, the literature on this question does not provide much support for the conclusion.[37]

More research has been done since that survey was written, but the general conclusions remain much the same. Economists find no evidence of widespread declines in real wages. The debate on the effect of immigration on wage rates of native-born workers has mostly narrowed down to the effect on wages of high-school dropouts.[38] Estimates range from slightly positive to, at worst, an 8 percent fall.

How is this possible? Don't the laws of supply and demand dictate that wages would fall? Not when other things change at the same time. Those immigrants who add to the supply of labor also demand goods and services, causing the demand for labor to rise. This means that the effect of immigration on wages shifts from being a theoretical question to being an empirical one.

Second, immigrants don't simply shift *the* supply of labor. Labor is heterogeneous. When immigrants have skills that differ from those of the native-born population, they *complement* the native-born rather than serving as substitutes for them. Many of the immigrants to the United States are either extremely highly skilled or very low skilled. Yet most native-born labor falls somewhere in between. The native-born population makes up around one-third of adults in the United States without a high school diploma. A large percentage of new Ph.D.s is awarded to foreign-born people. To the extent that immigrants are complementing domestic labor, they can increase, rather than reduce, the wages of the native-born.

Third, even for the unskilled, there is the issue of price sensitivity. If the demand for workers is perfectly elastic in the relevant range, then there also need not be any effect on wages.[39] Finally, as Adam Smith pointed out centuries ago, specialization and the division of labor are limited by the extent of the market. Bringing more immigrants into the United States expands our market and allows for greater specialization. That makes each of us more productive and able to earn higher real wages.

Another common fear is that immigrants are a fiscal drain on the U.S. government's budget. Immigration historically has produced more federal tax revenue than immigrants have consumed in federal benefits over the long run.[40] However, some people legitimately may be concerned that future immigrants might differ in various ways from those at present, or that changes to immigration policy might upset the public's budget balance. But because economists agree that because net economic gains flow from immigration, any budgetary imbalances should be solvable by changes to fiscal policy.

Currently, noncitizens consume 6.7 percent of welfare spending while they make up 7.1 percent of the population.[41] But what if a dramatic increase in immigration from one of the policy reforms analyzed above were to materialize? Milton Friedman famously declared, "You cannot simultaneously have free immigration and a welfare state."[42] Many people take this to mean that we should limit immigration. However, the obvious alternative is to not allow immigrants access to the programs that comprise today's welfare state, including taxpayer-financed public education and healthcare programs. When Milton Friedman was asked about that alternative, he commented: "I haven't really ever thought of that system." Luckily, a recent policy study by Alex Nowrasteh and Sophie Cole has.[43] They argue for building a wall around the U.S. welfare state rather than a wall around the United States. They specifically suggest eliminating noncitizen access to Temporary Aid to Needy Families, Supplemental Nutrition Assistance Program, Supplemental Social Security Income, and Medicaid. Those reforms would immediately generate $29 billion in additional fiscal surplus for the U.S. government from immigrants and would limit the desire of any future immigrants to come here for access to the U.S. welfare state. None of the three policy reforms analyzed above need be a fiscal drag on the United States when rules limiting immigrant access to welfare are implemented.

Conclusion

There is a serious mismatch between labor demand and supply in the U.S. economy that could be alleviated by expanding the role of immigration in growing the U.S. labor force. The problem only promises to get worse in the absence of reform; the aging baby-boomer population and declining fertility rates mean that population growth in absolute terms for working-age Americans is moving toward a historic low. The need for reform has never been greater than it is now.

This study analyzed the current immigration and guest-worker quotas in the United States and found that they fail to meet domestic employers' labor demands. The speed at which guest worker quotas are reached was given as evidence for the severe shortage, as well as reports coming directly from employers unable to meet their labor needs. The mismatch is a systemic problem that cannot be solved by better technique: it is simply not possible for government central planners to know what the right level of immigration should be without letting decentralized market forces work.

Multinational businesses are the institutions best prepared for dealing with immigration restrictions, both practically and politically. A wide variety of visa options and work arrangements are available to corporations with offices and employees abroad, such as the L-1 visa and visas for temporary business travel. Multinational corporations are also able to hire labor overseas if they are not able to meet their labor demands with domestic labor. Small businesses are at a serious disadvantage, as they do not have the expertise, scale, or capital to overcome these challenges. Furthermore, small businesses lack seats at the political bargaining table, the availability of which would allow them to shape policy or secure favors and exceptions as large businesses are able to do.

The market for foreign workers in the United States is broken and needs reform. The current U.S. Senate proposal is a mild step in the right direction. It raises immigration caps, but leaves in place the fundamentally broken system of command and control. Red Card, an alternative guest worker proposal, is a much better solution for temporary workers because it lets market forces determine the numbers of admissible guest workers. Ultimately, the United States would be better served by moving to unrestricted migration for both guest workers and those who want permanent residency.

Notes

1. Organisation for Economic Co-operation and Development (OECD) (2013a).
2. OECD (2013b).
3. Cohen (2011).
4. Martin & Widgren (2002).
5. Mayr (2008).
6. OECD (2006).
7. Dench et al. (2006).
8. Miller (1999).
9. North American Industry Classification System (NAICS) (2012).
10. OECD (2008).
11. We should treat employer-reported shortages somewhat cautiously because they can be conflated with other labor market problems (such as recruitment difficulties and not labor shortages per se).
12. U.S. State Department (2012).
13. Passel et al. (2012).
14. Roberts et al. (2010).
15. Data is from the U.S. Citizenship and Immigration Services (USCIS) annual reports, 2011–2013.
16. Government Accountability Office (GAO) (2011).
17. The H-2B cap is split so that half of the permits are available in the first half of the year, and half are available in the second half of the year. This is done because these permits are for seasonal agricultural workers and the government is trying to spread permit availability across different growing seasons.
18. Computing Research Association (2013).
19. U.S. Department of Labor (2013).
20. During the 2000s, the number of law enforcement guards on the U.S.–Mexico border more than doubled.
21. Bureau of Labor Statistics (2013).
22. Carnevale, Smith & Melton (2001).
23. Hayek (1945).
24. Bureau of Economic Analysis (2012).
25. Blinder & Krueger (2009).
26. See Munro (2013)
27. S.744, passed June 27, 2013.
28. Nowrasteh (2011).
29. Nowrasteh and Radia (2011).
30. Krieble (2011).
31. Clemens (2011).
32. It is beyond the scope of this policy study to examine the political and cultural impacts of increased immigration. However, preliminary evidences suggests that immigration has no impact on a country's level of economic freedom (Nowrasteh 2013). See Alvaro Vargas Llosa (2013) for an extended treatment arguing that greater immigration is not detrimental to culture.
33. Ricardo (1817).
34. Clemens (2011).
35. Borjas (2009).
36. Bastiat (1848).
37. Friedberg & Hunt (1995).
38. For a couple of classic examples in the conflicting sides of that debate, see Borjas (2003) and Card and Shleifer (2009).
39. See Bryan Caplan's (2005) discussion of the contradiction within David Card's work on this point.
40. Smith & Edmonston (1997).
41. Nowrasteh & Cole (2013).
42. Brimelow (1998).
43. Nowrasteh & Cole (2013).

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