

School of Economics FOCUS PAPER

Is a policy of free movement of workers sustainable?

by Tim Worrall

Since its inception, the European Union (EU) has aimed at implementing a policy of free movement of workers between member states (Article 45, EU Lisbon Treaty). However, some EU member states have been reluctant to implement this policy. Similar difficulties have emerged in other country associations such as the North American Free Trade Area, in which the free movement of workers is only allowed between the US and Canada. The main reason for this reluctance lies in the fear that inflows of migrant workers might depress local labour market conditions and lower the welfare of the host country's workers.

This paper studies the factors that help countries mutually agree on common policies of unconditional and uncontrolled movement of workers. For the countries to agree on such a policy, short-run costs must be outweighed by long-term benefits. While the costs lie in the congestion and adverse effects of terms of trade, the benefits considered here stem from labour market flexibility and consumption smoothing. Countries facing good productivity shocks incur short-run costs because they allow foreign workers to participate in their local labour markets, which reduces local wages and/or purchasing power.

By contrast, countries facing bad productivity shocks benefit from free movement of workers because they are able to invite their citizens to work temporarily or permanently in more prosperous countries. Such policies are less likely to be adopted when workers are impatient and less risk averse, when production technologies display decreasing returns and when countries trade a greater share of their products. Large permanent differences



in consumption levels prohibit the adoption of the policy. The presence of trade increases the costs of immigration but at the same time it mitigates the migration incentives. In the presence of both tradeable and non-tradeable goods, the policy of free movement of workers is more likely to be sustainable as fewer goods are traded. Finally, wage rigidities improve the sustainability of the policy, provided these rigidities are not permanent.

This analysis is designed to highlight the role of labour market flexibility and insurance in the adoption of uncontrolled and unconditional migration. It shows the importance of time discounting, risk-aversion, factor congestion, and trade. These are important ingredients in the decision of countries to adopt a policy of free movement of labour, and by considering the interplay of trade and congestion this paper offers new insights into these decisions.

The main contribution of the paper is threefold. As far as is known, this is the first paper to apply the methods used in modelling sustainable trade relationships to the issue of migration. Second, although the model abstracts from many important factors considered in the migration literature, it puts at the forefront uncertainty and intertemporal welfare. In this way, it helps to explain why some of the large potential gains from migration identified in other studies might be difficult to realise. Third, the paper contributes to understanding the interaction of trade and migration policy.



The model is stylized and many other important aspects of the problem are not taken into account. It takes as given that immigration always has short-run costs. This might not be true, or might only be true for particular sectors or skill groups. The model also considers only the case where migrants remain citizens of the origin country. Another important omission is the lack of skill heterogeneity across workers. With skill heterogeneity, there might be offsetting worker flows in response to productivity shocks. The issue of controlled migration is also not addressed here. However, such a policy is difficult to implement relative to a policy of free movement, even though it might have efficiency benefits by reducing issues caused by an excess agglomeration of labour. Equally, the analysis only considers the case of free trade. It does not consider how the adoption of trade and migration policies might be coordinated. These are all possible interesting directions for further research.

Information

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