Immigrant Integration and the Welfare State

A Survey of Issues, Problems and Results

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Master thesis for the Master of Philosophy in Economics degree

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January 2011
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Trykk: Reprosentralen, Universitetet i Oslo
Abstract

Lower labor market participation and greater extent of welfare dependency among non-Western immigrants, compared to comparable natives, is common in Western welfare states. A first glance at immigrant-native employment gaps, suggests that the Central-European and Anglo-Saxon countries generally have smaller gaps than social democratic states such as Sweden, Denmark and the Netherlands. This thesis seeks to understand why there are such differences across welfare states present, and how the welfare state affects immigrant labor market integration.

In order to answer these questions, I provide a survey of the literature to find out if it is possible to say something general about welfare state organization and labor market integration of non-Western immigrants. I find a tentative pattern in the literature, that to some extent confirm the ruling perception: When observable characteristics are controlled for, the gap in immigrant-native employment is often larger in social democratic countries, than in conservative Central-European states and English-speaking countries. This is to some extent caused by the welfare organization, although many other factors contribute to this result. Within a welfare modeling framework, I argue that welfare states, with their different welfare organization, integration and immigration policies, and labor market structures, influence immigrants’ labor market integration.

The structure is as follows: Section 1 provides an introduction to the problems in question. Section 2 reviews some basic terminology and background topics. In section 3, the topic of how the welfare state affects immigrant labor market integration is surveyed: First, the welfare state can create welfare migration depending on the generosity of the welfare state and on immigration policies. Second, the labor market structure of the welfare state influences immigrant integration. Third, integration policies create different outcomes across countries. At last, I will look at two studies examining one immigrant group’s outcomes in two welfare states. In section 3, some further topics are addressed. These issues concern the importance of language skills, ethnic ties and self-employment.
Preface

This thesis marks the end of five years of study at the Department of Economics, first as a bachelor student and later as a master student.

During the last year, I have worked as a research assistant at the Norwegian Institute of Public Health, with a project concerning immigrant integration in Norway, Germany and the Netherlands. Results from this study do not yet prevail, but in the process I have had the chance to interview a number of immigrant families. The issues raised in these interviews motivated me to learn more about how the welfare state affects immigrant labor market integration.

I would like to thank ESOP- Center of Excellence for granting me a scholarship and office space, and for including me in activities. I also owe thanks to my supervisor and positive spirit, Kalle Moene, for valuable feedback and encouraging comments. In spite of his busy schedule, he found time to help me, especially in the later phases. Finally, I want to thank my friend and fellow student, Rasmus Bøgh Holmen, for proofreading the thesis.

I take full responsibility for any inaccuracies or errors in this thesis.
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1 Introduction

Over the last decades, Non-Western immigrants have generally entered the Western countries on humanitarian grounds, or to be reunited with family. These immigrants have lower employment rates than the native population in most Western countries, even after a substantial period of time. The poor labor market outcomes are reflected in extended participation in welfare programs. As employment is a corner stone in the welfare state construct, this has raised concerns regarding integration and welfare policies.

During the 1980s and in the beginning of the 1990s, immigrants’ labor market situation, relative that of natives, worsened in the US and in Europe (Borjas 2010, Ekberg 1999). In Sweden, for instance, where 11 percent of the population are immigrants, social assistance to immigrants accounted for nearly half of the country’s expenditure on social assistance by the middle of the 1990s (Hansen and Lofstrom, 2007). Both in Europe and the US, immigrants are more likely to receive welfare benefits than natives. Studies show that the differences generally remain even when observable personal characteristics are controlled for, although there are some exceptions, for instance in Germany. (Hansen and Lofstrom, 2007, Borjas and Hilton, 1996, Castronova et al.,2001). Furthermore, research find that recent immigrants in the US are more likely to receive welfare benefits than earlier arrived immigrants, and that the probability to receive benefits increases with the duration of stay (Borjas and Trejo, 1991). A common claim has been that immigrants will integrate better the longer they stay in the host-country. Even so, in Norway for instance, results indicate that immigrants drop out of the labor force and become welfare recipients after 10-15 years of residence (Bratsberg et al. 2011). This has raised concerns regarding integration and welfare policies, as it seem like immigrants are integrating into a welfare trap, by obtaining use of welfare assistance. These concerns have even caused some countries, for example the US and Germany, to restrict immigrant access to some welfare benefits (Hansen and Lofstrom, 2007). Other countries, like Switzerland, have sought to resolve this issue by blocking naturalization to immigrant welfare recipients, and by forcing unemployed immigrants to return to their country of origin (Koopmans, 2010).

Almost all immigrant groups in West-Europe and the US, and in particular newly arrived groups of refugees, have lower labor market participation than natives (Bevelander et al.,2010, Borjas and Hilton, 1996). The general pattern is that natives have the highest
employment rates, Western immigrants the second highest rates, while non-Western immigrants have the lowest employment rates (Bevelander et al., 2010). This immigrant-native gap has been relatively persistent in Europe through the last twenty years, though the US has seen some improvements (Borjas, 2009). However, there are large differences across countries. In Sweden, for instance, natives in the labor force have a participation rate of 0.75, while the rate for Non-Western immigrants is 0.54 (Koopmans, 2010). Other countries with poor immigrant performance are the Netherlands, Belgium and Denmark. The Central-European countries of Austria, Germany and Switzerland have the highest immigrant labor market participation rates. Numbers for Austria show that the native population has a participation rate of 0.68, while the Non-Western immigrants are not far behind with a rate of 0.66 (ibid.). A gap remains even when personal characteristics such as education, age, gender, experience and sector of activity is controlled for. A common claim is that differences in immigrant integration across countries, is due to welfare state organization.

The situation described above raises the motivating question of the thesis: Why does immigrant labor market integration vary across welfare states? And how does the welfare state influence integration outcomes?

To answer the motivating question of the thesis, I provide a survey of the literature, especially from cross-national studies. References from several disciplines within social sciences are utilized. The focus will be on the relationship between welfare states and immigrants’ labor market integration in the Western European countries and in the US.

The structure is as follows:

Section 1 provides an overview of the problems in question through this introduction.

Section 2 reviews some basic terminology and background information.

In section 3, the topic of how welfare states affect immigrant labor market integration is surveyed. I argue that states, with their different welfare organization, integration and immigration policies, and labor market structures, influence immigrants’ labor market integration. First, the welfare state can create welfare migration depending on the generosity of the welfare state and on immigration policies. Second, the labor market structure of the welfare state affects immigrant integration through several channels, such as labor market protection, the size of low-skilled sector and incentives in the benefit system. Third,
integration policies create different outcomes across countries. At last, I will look at two studies, each examining a specific immigrant group’s outcomes in two welfare states.

In section 4, some further topics are addressed. These issues concern the importance of language skills, ethnic ties and self-employment.

Section 5 gives a summary and concludes.
2 Background

2.1 Some Definitions

**Labor market integration:** The term integration includes a number of social and cultural features. The labor market part of integration is of great importance, because labor market integration is key to understanding a range of economic consequences (Jean et al. 2007). Labor market integration is defined as ‘convergence of migrants’ wages or (un)employment rates towards those of natives’ (ibid.). This thesis focuses on labor market integration, with weight on labor market participation.

**Human capital:** Human capital refers to the quality of labor. Three characteristics are mentioned in the literature (Weil, 2005). First, human capital is productive in the labor market- that is, it enables people to produce more output. Second, it earns a return by giving the worker a higher wage. Third, the production of human capital comes with a cost of time and resources. Human capital thus includes education, job training, medical care and acquisition of information and language (ibid.). Some types of human capital, such as language proficiency and cultural acquisition, are specific for the host country. Immigrants tend to have lower level of human capital specific to the host country at arrival, and the lack of such capital can be a disadvantage several years after immigration (Cusa and Jean, 2007).

**Welfare benefits:** Benefits involve monetary transfers from the government to people who are entitled to such benefits. A person may be entitled when he or she is unemployed, old, sick, on a low income, have dependent children, has a status as refugee etc. In addition, there may exist requirements related to work history and citizenship to be entitled to benefits.

**Welfare dependency:** Welfare dependency can arise when a person on welfare relays on welfare benefits, as an alternative for securing a paid job. When an individual is more likely to receive benefits for one period, given that he or she received benefits in the last period, the person is welfare dependent. Welfare dependency and labor market participation affect one another when welfare receipt functions as insurance of income outside the labor market.

**Welfare state generosity:** The generosity level of a state is commonly computed as ‘replacement rates’ for OECD countries. This is the ratio between income out of work
(welfare benefits) and average wage in the labor market. These calculations are done for different household types, with different incomes and with various degrees of unemployment.

**Multicultural policies:** The word ‘multiculturalism’ covers various forms of cultural diversity (Kymlicka, 1995:10). I use the term ‘multiculturalism’ as an expression relating to the policy approach of recognizing and supporting cultural differences, and providing immigrants with rights. This is consistent with several papers referred to in this thesis (see for instance Koopmans, 2010). In the Western world, the Scandinavian countries, the Netherlands, as well as the US and UK have traditionally been inspired by multiculturalist ideology, while countries like France, Germany and Austria have tend to rely on more restrictive assimilation policies.

### 2.2 Welfare State Typologies

There are several definitions of the term ‘welfare state’. One fundamental definition involves state responsibility for securing citizens with some basic welfare needs (Esping-Anderson, 1990). In general, what we call welfare state covers education, health care, social insurance, social care and poverty alleviation. By social insurance I mean public benefits, like insurance against illness and unemployment, and pensions. The welfare state offers insurance and redistribution of income in different amounts, depending on the policy design in various states. What welfare model countries cluster around can be of great importance to immigrants’ economic performance because different models supply immigrants with different entitlements to welfare benefits. Thus, the welfare model can help explain why immigrants’ labor market integration differs between countries.

The organization of the welfare state varies across countries. The literature tends to divide welfare states, or regimes, according to different characteristics and organization. One typology divides welfare states in two categories; universal state-centered welfare states (Beveridgean approach) and welfare states stressing social insurance and corporatist elements (Bismarckian approach) (Abrahamson, 2000). Another type of categorization divides welfare states in three regimes; the Scandinavian, the continental and the Anglo-Saxon (or Atlantic) tradition. Here, the Beveridgean model is subdivided into Scandinavian and Anglo-Saxon model. Lastly, welfare states can be divided in four institutional groups, making the Southern European countries a separate regime.

In the residual model of social policy, the ‘natural’ institutions where needs are met, are the market and the family. Only when these institutions fail to provide the needs of an individual, can social welfare institutions provide temporary support. The influence of this marginal social welfare system, based on liberal theory and belief in market forces, is still in place, for instance in Switzerland and the Anglo-Saxon countries (ibid.).

In the industrial achievement-performance model, the welfare state is a provider of education, social insurance and health services. This model is not universal; it is reserved for those contributing. Social needs are met on the basis of productivity, merits, work performance and achieved status differentials. The welfare state contributes to maintain social differences, and therefore it focuses on income substitution. The model is based on a conservative ideology of obtaining existing privileges. The continental countries, with Germany as prime example, are shaped by this model (ibid.).

The institutional-redistributive model of social welfare provides both universal and selective services outside the market. Universal services are available to all citizens, and social policy has a role as identity-creator, promoting integration and redistribution of resources. Oddly enough, the Scandinavian countries are not mentioned as an example, but Titmuss makes a reference to the ‘Ujamaa Villages’ in Tanzania (ibid.).

A well-known classification of welfare states is that of Esping-Anderson (1990). In his book *Three Worlds of Welfare Capitalism*, Timuss’s typology of welfare states regimes is renamed Liberal, Conservative and Social Democratic (Abrahamson, 2000). Esping-Anderson argues that the social democratic states have a high level of ‘decommodification’ of labor, which means that a worker can obtain a level of welfare without depending on the labor market (Esping-Anderson, 1990:37). The major emphasis is on support from the state, rather than from the family or the market. Social-democracies have the highest levels of entitlements to welfare benefits and the highest provision. In conservative corporatist regimes, the state plays a smaller role and the family a larger role, when it comes to support of individuals. Conservative states have intermediate levels of ‘decommodification’, while liberal states have
the lowest. In liberal regimes there is a low level of benefits from the state. The market is the dominant institution for individual support. The Scandinavian countries are typically social democratic regimes; Germany, Austria and France are examples of a conservative regime, while Great Britain and the US have characteristics of liberal regimes (Esping-Anderson, 1990).

Leibfried (1992) adds another category to Esping-Anderson’s three regimes, namely the ‘Latin Rim’ countries of Southern Europe. He divides welfare states in four regimes: The Scandinavian welfare states, the ‘Bismarck’ countries, the Anglo-Saxon countries and the ‘Latin Rim’ countries. The Scandinavian countries are ‘modern’ welfare states that emphasize work for everyone, with the state as employer of first resort. The ‘Bismarck’ countries, consisting of Germany and Austria, are ‘institutional welfare states’, with the state not as an employer, but as compensator of first resort. Right to social security, rather than work for everyone, is the main goal. The Anglo-Saxon countries, consisting of the English-speaking states, are ‘residual welfare states’, especially when it comes to income transfers. These states stress work enforcing mechanisms, meaning that entry into the labor market is forced, rather than subsidized. In contrary to the ‘Bismarck’ countries, the welfare state is a compensator of last resort. The Southern European countries that make up the ‘Latin Rim’ are ‘Rudimentary welfare states’, which do not even provide their citizens with welfare rights. They are similar to the Anglo-Saxon countries in the sense that labor market entry is forced and residualism is emphasized. Nonetheless, there are traditions for welfare (to the needy) stemming from the Catholic Church (Leibfried, 1992). It is important to be aware of, though, that during the last 20 years, the Southern European welfare states have developed. An aptly example is Spain, which has developed its social policy extensively.

The typologies are summarized on the next page.
### Table 2.1: Typologies of welfare states

<table>
<thead>
<tr>
<th>Types</th>
<th>Scandinavia</th>
<th>England and the US</th>
<th>Central-Europe</th>
<th>South-Europe</th>
</tr>
</thead>
<tbody>
<tr>
<td>**Bismarckian/</td>
<td>Beveridgean</td>
<td>Beveridgean</td>
<td>Bismarckian</td>
<td>Bismarckian</td>
</tr>
<tr>
<td>Beveridgian</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Titmuss</td>
<td>Institutional-redistributive(^1)</td>
<td>Residual</td>
<td>Achievement-performance(^2)</td>
<td>Achievement-performance</td>
</tr>
<tr>
<td><strong>Esping-Anderson</strong></td>
<td>Social democratic</td>
<td>Liberal</td>
<td>Conservative (corporatist)</td>
<td>Conservative</td>
</tr>
<tr>
<td><strong>Leibfield</strong></td>
<td>Modern</td>
<td>Residual</td>
<td>Institutional</td>
<td>Rudimentary</td>
</tr>
</tbody>
</table>

**Characteristics**

- **Bismarckian/ Beveridgian**
  - High degree of decommodification, goal of full employment, employer of first resort, universalist

- **Titmuss**
  - Institutional-redistributive\(^1\)

- **Esping-Anderson**
  - Social democratic

- **Leibfield**
  - Modern

- **Characteristics**
  - Low degree of decommodification, goal of full growth, compensator of last resort, work enforcement

The assumption that welfare states cluster around different welfare models has widely been acknowledged, although there have been discussions about problems and limitations (Abrahamson, 1990). The literature presents several attempts to categorize regimes according to other characteristics than those presented above, for example according to social insurance models, which look at transfers for sick pay and pensions. Besides, welfare state typologies have been criticized for neglecting families and networks as institutions of welfare provision. Also, critique has been raised for not taking women’s issues into account. Nevertheless, the typologies presented above have shown robustness (ibid.).

\(^1\) According to Abrahamson (2000), Titmuss does not mention Scandinavia, but the typology resembles Scandinavia to a great extent, and it is in accordance with later work on the field.

\(^2\) Except for Switzerland which is a residual state
Scruggs (2006) estimates decommodification scores, based on replacement rates and welfare program coverage, for several countries. The results are shown in figure 2.1. In line with Esping-Anderson’s reasoning, the same results apply for 2002. The Social democratic group of countries (Norway, Sweden, Belgium, Netherlands, Finland and Denmark) has the highest scores, the Conservative countries (Austria, Italy, Germany and France) have the second highest scores, while the Liberal countries (UK, US and Ireland) have low scores. In addition, Switzerland scores low, since it has elements from both conservative and liberal regimes.

Figure 2.1: Decommodification scores 2002

Esping-Anderson’s classification of welfare regimes according to the degree of ‘decommodification’, involves both welfare entitlements and the generosity level of provision of welfare benefits. The provision of insurance and incentives promoted by the welfare state, is of importance to immigrants’ participation in the labor market.

2.3 Migration Flows

According to the dictionary, immigration is to move from one place of residence to another with the intention of remaining for some substantial period of time. Immigration can be subdivided into three categories depending on the primary motivation for migration; labor immigration, refuge and asylum seeking, and family reunification.
Immigration can be legal or illegal, permanent or temporary. Legal migration covers labor migration, family unification and refugees\(^3\). Migration can depend on several factors, some being actual conditions and people’s knowledge of the conditions in origin and destination country, expectations about future conditions, risk aversion, home country preferences and network effects. Temporary migrants, for instance, move to seek asylum or work. Expectations about future conditions involve both income expectations, like wage potential, welfare benefits and social expectations, such as norms and acceptance in the host country. Migration usually leads to change in community affiliations and in the composition of labor supply.

In practice, the term ‘migrant’ refers to very different concepts, depending upon the country concerned. Some countries define migrants as those born abroad, while others define migrants as foreign nationals. The term ‘immigrant’ is also defined differently in countries’ statistical database. Some define immigrants as both the first and second generation of immigrants, while other countries define immigrants as only being the first generation of immigrants.

**Europe**

Immigration in Europe became significant after World War II. In the years between 1945 and the early 1960s, migration movements were influenced by post-war adjustments and post-colonial return migration. During this period, 20 million people displaced by the war migrated to Germany (Bauer et al, 2000). Great Britain, Belgium, the Netherlands and France, on the other hand, experienced inflows of workers and colonists from the former territories. In Great Britain, for example, every citizen of Commonwealth could enter United Kingdom unrestricted until 1962. Before 1955, more than 60,000 Indian had migrated to Great Britain after the independence in 1947. Another instance is that of the Netherlands, which experienced an inflow of 70,000 immigrants from Indonesia in 1946 and a second wave of 60,000 immigrants from Indonesia in 1950, after the country gained independence (ibid.).

From the early 1960s to the mid 1970s, economic growth induced labor migration. Excess labor demand, due to economic growth, lead to weakened immigration restrictions. Some European countries, for example Sweden and Germany, even established recruitment policies

\(^3\) A person who is outside his country and unable or willing to return because of (a well founded fear of) persecution based on race, religion, nationality, membership of a particular social group, or political opinion, is outside the country of his nationality, and is unable to or, owing to such fear, is unwilling to avail himself of the protection of that country (www.unrefugees.org)
for guest workers. In the years from 1955 to 1973, 5 million migrated from the less developed South-Europe to the northern European countries. Labor migration from Asia was substantial as well. For instance, immigration to Norway boosted after oil was discovered in the 1960s. Low skilled, male immigrants, mainly from Pakistan, migrated to work in the flourishing Norwegian economy.

In the early 70s, the economy was less successful in Western Europe, and the demand for unskilled labor decreased. Immigrants were in need of social benefits, and restrictions on labor immigration, as well as ‘immigration stop’, were implemented by Western governments. This put a stop to unskilled labor immigration. Nonetheless, immigration continued because of exemptions for certain groups. The resident countries allowed family reunification, and refugees and skilled labor were given entrance. Hence, after the mid 1970’s, family reunion and asylum have been the most common reasons for immigration to Europe.

From 1985 the flows of asylum seekers into West Europe increased. In the late 1980s Germany experienced an inflow of native German immigrants from Poland, Russia and Romania. Until the early 1990s, asylum seekers and refugees were mainly Asian and African. During this decade, the number of asylum seekers and refugees from the European countries increased, as a result of the fall of the Iron Curtain, the war in Yugoslavia and the conflicts between Kurds and Turks in Turkey (Bauer et al., 2000). Due to the more restrictive policies, the number of asylum seekers decreased in several European countries after 1992. In the UK, for instance, one experienced a flow of fewer asylum seekers, but this was also due to restrictions in welfare benefits to this group (SOPEMI, 1999, as described in Bauer et. al, 2000).

In 2002, immigration restrictions were implanted by European Economic Area (EEA), requiring education to immigrate to the EEA countries. Following the extension of EU in 2004, which opened for 10 new member countries, labor immigration from East to West Europe has increased rapidly. In 1995 there were 4,500 Polish immigrants in Norway, while the number had increased to 52,000 in 2009 (Statistics Norway: www.ssb.no/innvanding). Romania and Bulgaria opened their labor markets to EEA in 2007 by becoming members of EU, though some restrictions were imposed on the new members.
For the past 20 years, Southern European countries have become immigrant destinations, in contrast to being characterized by emigration due to weak economic performance in the 1960s and 1970s.

USA

On the contrary to European countries, which experienced immigration after the countries were developed, immigration to the United States was essential for founding and developing the country (Bauer et al., 2000). Immigration to the United States was fairly unrestricted until the 1920s, when a policy which favored some nationalities was implemented. In 1965 this national origin restriction was replaced by a policy that made family reunification the main criteria for immigration. Visas for family reunification are still in place, although visas are also being allocated on the foundation of labor market characteristics (ibid.). Today, Mexicans are the largest immigrant group in the US. There are large immigrant groups from China, Philippines and India as well.

The composition of reason for migration in 2007 is depicted in Figure 2.2 for some selected countries.

Figure 2.2: Composition of permanent-type immigration to OECD countries, 2007.4

4 Figure from Liebig(2009)
Immigration in terms of family reunification is especially a large part of total immigration in the US and Sweden. Portugal, UK and Italy have a large part of labor immigrants, while Sweden stands out in granting immigration on humanitarian grounds. All the European countries have a large part of free immigration in the composition of immigrants. This free movement is to a large extent characterized by immigration from East-Europe.
3 Why Does Immigrants’ Labor Market Performance Vary Across Welfare States?

Immigrants’ structural integration depends on welfare regime, labor market structure and integration and immigration policies. These institutional settings’ importance varies across time and societies, and the institutional elements are mutually dependent of each other (Reitz 1998, as described in Kogan, 2003). This chapter explores how the welfare state interacts with policies and labor market structure, and affects immigrants’ labor market performance.

Welfare state institutions may affect immigrants’ labor market integration before the time of migration, as well as after immigration. Pre-immigration effects may be caused by self-selection in response to welfare state generosity and immigration policies. Post-immigration impacts can be influenced by labor market structure and integration policies of the welfare state, which can work in favor or disfavor of labor market integration.

Comparing immigrant employment across welfare states, one finds that there are great differences across countries. Countries that apply the social democratic model, seem to have lower immigrant employment rates than countries that apply the liberal and conservative model. Norway is an exception with a relative high immigrant employment level. Employment rates for selected countries are depicted in table 3.1.
Table 3.1: Employment rates, per cent of population aged 15-64, averages 1999-2004

<table>
<thead>
<tr>
<th>Countries</th>
<th>Native-born</th>
<th>Non-Western born</th>
<th>Relative immigrant employment</th>
</tr>
</thead>
<tbody>
<tr>
<td>USA⁵</td>
<td>62,5</td>
<td>63,5</td>
<td>1,02</td>
</tr>
<tr>
<td>Austria</td>
<td>68,1</td>
<td>66,6</td>
<td>0,98</td>
</tr>
<tr>
<td>Norway</td>
<td>75,0</td>
<td>67,0</td>
<td>0,89</td>
</tr>
<tr>
<td>Germany</td>
<td>68,5</td>
<td>59,4</td>
<td>0,87</td>
</tr>
<tr>
<td>Switzerland</td>
<td>79,5</td>
<td>68,5</td>
<td>0,86</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>72,0</td>
<td>60,3</td>
<td>0,84</td>
</tr>
<tr>
<td>France</td>
<td>63,5</td>
<td>52,5</td>
<td>0,83</td>
</tr>
<tr>
<td>Belgium-Wallonia</td>
<td>56,4</td>
<td>45,1</td>
<td>0,80</td>
</tr>
<tr>
<td>Netherlands</td>
<td>75,1</td>
<td>57,8</td>
<td>0,77</td>
</tr>
<tr>
<td>Sweden</td>
<td>75,1</td>
<td>54,4</td>
<td>0,72</td>
</tr>
<tr>
<td>Belgium-Flanders</td>
<td>64,4</td>
<td>45,3</td>
<td>0,70</td>
</tr>
<tr>
<td>Denmark</td>
<td>77,0</td>
<td>53,5</td>
<td>0,69</td>
</tr>
</tbody>
</table>


These figures do not tell the whole story. When explaining these differences across countries (the institutional differences), it is important to be aware of the socioeconomic and demographic factors contributing to immigrants’ labor market participation. Several studies have aimed to isolate the institutional effects, in order to explain how the structure of the welfare state contributes to influence integration outcomes. It is common to control for age, gender, education, work experience and country of origin. The results from these regressions imply that there are indeed variations in labor market performance across countries and welfare regimes. Nonetheless, the picture may be different from that above. In Norway, for instance, high immigrant employment is partly due to a favorable composition of immigrants. When education is controlled for, Norway has a larger immigrant-native gap (Liebig, 2009).

However, comparisons that try to isolate the effects of welfare regime on integration are difficult to make, because integration may be influenced by a number of country specific effects, which cannot be controlled for with available data. One such effect is for instance immigration policy. In the following sections, I will give some explanations to how the institutional elements of the welfare state affect immigrant integration.

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⁵ Figures for the US include the whole foreign-born population, not just non-Western immigrants.
3.1 Composition Effects and Welfare Magnets

A relationship between welfare spending and immigration proposed by the literature is composition effects. These effects suggest that people with a low level of human capital will choose to migrate to generous welfare states with big safety nets and compressed wages. There will thus be an adverse selection effect to countries with a relative equal income distribution (Borjas, 1998). Such selections effects can affect immigrants’ observed and unobserved characteristics considerably.

It is possible that welfare benefits attract immigrants to states with big safety nets, or that the safety net discourages immigrants who fail to return to their country of origin. Borjas (1998) argues that immigrant welfare recipients in the US, in contrast to natives, should be located in the states with the most generous welfare benefits. He uses data on micro level from the 1980 and 1990 American Census to test the hypothesis that generous welfare states serve as welfare magnets to the immigrant population. Borjas investigates households that have received public cash benefits during the year prior to the Census. The cash benefits include Aid to Families with Dependent Children, Supplemental Security Income and general benefits.

Borjas develops a model and makes several prophecies. First, more generous welfare states are predicted to experience a greater clustering of low-skilled immigrants relative to natives. Second, immigrants are predicted to be more sensitive to changes in benefit levels than natives. This ‘benefit elasticity’ suggests that an increase in benefit level will increase welfare participation among immigrants more compared to natives.

In the study, California is mentioned as an example of an American state with relative generous benefits and with a large part of the immigrant population receiving benefits. In 1990, 37.6 percent of immigrants on welfare lived in California, compared to 11.5 percent of immigrants not receiving welfare benefits. The explanation could be that a large part of the immigrant population is refugees. California also has a large Mexican immigrant population that probably has chosen to settle down, not because of benefits, but due to the short distance to Mexico and ethnic network effects and family ties. Borjas therefore leaves out refugees and Mexican immigrants of the analysis. Nevertheless, the results show that immigrants on welfare are more clustered in California. These results indicate that when an income maximizing immigrant makes the choice to emigrate, he or she chooses to migrate to a state with generous benefits. Low-skilled labor is disproportionally drawn to California.
Borjas finds support for the hypothesis, that interstate differences in welfare benefits create welfare magnets, which attract the immigrant population. Further on, his findings indicate that immigrants are more sensitive to changes in welfare benefits than natives, though these results are weak. In general, American studies of composition effects find the effects of welfare magnets too small to be of importance (De Giorgi and Pellizzari, 2006).

Turning to Europe, De Giorgi and Pellizzari (2006) use micro data for 15 countries, drawn from the European Community Household Panel, covering the period from 1994 to 2001. The data include date of arrival, wages and benefit generosity in the host-country at time of arrival. Immigrants are identified as those who reported to be citizens of a non EU-15 country or those who were born abroad and lived in a different country before arriving in the country of residence. The raw data displays a varied distribution of immigrant education, with the Nordic and English-speaking countries attracting the higher educated immigrants. The authors control for a number of destination-specific effects, which absorb the strictness of immigration policy and network effects.

The results show that immigrants appear to enter countries with high real wages and low unemployment rates. However, highly educated seem to care less about these economic conditions when they migrate. For a given level of wages and unemployment rates, De Giorgi and Pellizzari find a small, but positive, effect of welfare state generosity on migration decisions. Unlike the US, where mobility is high for both native and immigrant workers, the role of migration as a stabilizing force after shocks is of greater importance in Europe. In the latter, the effects of welfare benefits can be large enough to equalize the changes in migration that would take place from shocks to unemployment (ibid.).

These results imply that the most generous welfare states, i.e. those that apply the Scandinavian model may act as welfare magnets. Immigrants with poor labor market skills will have stronger incentives to immigrate to the Scandinavian countries, than immigrants with high skills, all other factors held constant. The latter will have greater incentives to migrate to countries with more dispersed income distributions, like the US. The US might thus experience positive self-selection of immigrants.

The composition of immigrants is not just due to the welfare levels, but also to the high wages and high employment that attract low-skilled labor in these countries. However, these implications depend on immigration policies across countries. Visas and return policies
restrict access to countries, making it difficult for immigrants to choose the destination with the most generous benefits. As Nannestad (2007) points out, there are only two ways of legal immigration for non-Western immigrants: Family reunification and asylum seeking. Immigrants who come for reunification are restricted by where family members live, regardless of welfare benefit levels. Furthermore, the poor labor market outcomes in the Scandinavian countries may be explained by characteristics and network effects, rather than by negative self-selection. The guest worker programs implemented in the 1970s induced low-skilled labor immigration. The following immigration caused by family reunion may consist of individuals with the same low-skilled characteristics. Thus, it may be the state that has negatively selected immigrants (ibid.)

Moreover, asylum seekers are constrained by logistics as well as immigrant policies. In Europe, refugees are required to seek asylum in the first country they arrive in. Further on, when refugees ‘choose’ destination country, it may just as well be the case that they maximize the chance of being admitted as a refugee, as they would maximize incomes (ibid.). There is evidence that the Nordic countries, as well as Belgium and the Netherlands, admit a larger part of asylum seekers and refugees than other countries (Kogan, 2006). Whether these immigrants come in response to welfare benefits, high wages or immigration policies is hard to say.

Whether or not the welfare generosity level affects the composition of immigrants, it is safe to say that welfare systems, with their different ways of organizing the labor market, affect the composition of immigration. A large part of migration within Europe is caused by labor immigration from East-Europe. Unemployment and wages are reasonable determinants when the choice of host country is made. Once in the host-country, welfare generosity may hamper the mobility of temporary immigrants. Further on, negative self-selection can have negative consequences. Within Europe and within the US, welfare migration makes generosity more expensive because of the externalities related to such policies, everything else held constant. This may cause countries within Europe and states within the US to supply welfare benefits that are too low from the society’s point of view.
3.2 Labor Market Structure

Egalitarian countries redistribute more than others. Norway, Sweden and Denmark for instance, have twice as generous welfare states as the US (Barth and Moene, 2008). In the Scandinavian countries, where collective bargaining contributes to a compressed wage structure, low-skilled immigrants are faced with relative high wages. These countries have strong trade unions that defend the interests of people already employed. This may be a disadvantage to immigrants who are outsiders in the labor market. However, when employed, high protection makes less room for discriminating behavior. It is thus an advantage.

There are several ways of securing an income in the welfare state. These include paid work, unemployment benefits attached to work, and social benefits that can be obtained outside the labor market. Which of these options being realized, depend on the incentives in the welfare system, the labor market structure and immigrants’ preferences and personal characteristics.

In most countries, low-skilled immigrants have higher employment rates than low-skilled natives. The Scandinavian countries, as well as Belgium and the Netherlands, are some exceptions. In these countries, immigrants have lower employment rates than natives. The low-skilled sector may thus be important in understanding the differences in immigrant employment rates across countries. The labor market structure, such as entry wages and supply of low-skilled jobs may affect integration outcomes. Figure 3.1 displays relative employment for low- and high-skilled immigrants in some OECD-countries.
Figure 3.1: Gap in employment rate between native-born and foreign-born population by educational attainment, percentage points, 2007 or latest available year

Note: This figure displays the results for the whole immigrant population, not just Non-Western immigrants.

Source: OECD Factbook 2010: Economic, Environmental and Social Statistics, OECD 2010

The US, Ireland, Luxembourg, France, Germany, Portugal, Italy, Spain and Greece have high low-skilled immigrant employment, while the outcomes for this group are poor in the Scandinavian countries, Finland, Netherlands and Belgium.

In this section, I will go in some more detail when explaining mechanisms that affect immigrant integration. In doing so, circumstances concerning immigrant employment may be repeated because they interact with each other. The section starts with an overview of several mechanisms affecting immigrant employment in sections 3.2.1-3.2.5. It continues with a discussion on incentives in the benefit system in section 3.2.6, before clarifying how the welfare state and labor market structure interact in section 3.2.7.

3.2.1 Substitution of Low-Skilled Labor

In the Anglo-Saxon countries, wages are more flexible than in the continental countries and Scandinavia. In the two latter groups of countries, wages are more stable, and low-skilled employment has to a larger extent been substituted with capital.

A compressed wage structure raises the entry wage. For the employer, a high entry wage raises the price of labor relative to capital. This may cause employers to substitute low-skilled labor with capital in countries where wage compression is high. To see this, assume that low-
skilled labor and capital are the only two factors of production, and that these inputs are substitutes. Price of labor is the wage, $w$, and price of capital is equal to the rent, $r$.

Figure 3.2: Substitution of Labor for Capital

In figure 3.3, $y_0$ and $y_1$ are isoquants that display the choice of inputs by the firm at a given level of output. The slope of the isoquant curves are the technical rate of substitution, which tell us how many units of capital can be saved by a one unit increase in labor. The straight lines are isocosts with a slope equal to the input price ratio - $W/R$. Optimal production is where the isoquants are tangent to the isocosts.

Now, assume that a firm starts out in point a, with a relative low minimum wage. Assume then that wages to low-skilled labor increase. The isocost line shifts and is tangent to the isoquant in point c. The firm demands more capital and less labor. To see this, we can ask how the firm would adapt if both wages and capital rents increased by the same amount, so that the firm would be in a situation along isoquant $y_1$. This is an equivalent way of asking how much the firm would be willing to pay to be on isoquant $y_1$ after wages increased. The answer to this question we get by parallel displace the original isocost line inwards. The firm ends up in point b.

The move from point b to c is the substitution effect. It shows how the firm substitutes labor with capital in response to the price change in labor. The demand for low-skilled labor decreases. Consequently, substitution of low-skilled labor may thus hamper immigrant employment, because immigrants are overrepresented among low-skilled candidates. However, for those able to get a job, wages are higher. The mechanism described above is a partial effect, which only illustrates one part of the picture. A compressed wage structure
makes high-skilled labor relatively less expensive, and this increases the demand for high-skilled labor relative to low-skilled labor. Qualified immigrants can consequently, perhaps, easier move from low-skilled to high-skilled sector in countries where wage compression is high. Thus, social mobility may be less difficult in these countries.

3.2.2 The Job Search

From the supply side of the market, immigrants may settle in low-skilled low-paid jobs as a result of lower reservation wage, stemming from the fact that costs of searching are higher for this group, while the availability of jobs is lower\(^6\). To understand how immigrants differ from natives in the job search situation, I start by presenting the basic model.

Within a search theory framework, assume that an unemployed person spends all of her time looking for a job. The job-seeker does not know the wage each job offers, but she knows the distribution of wages. Workers are risk neutral and get no disutility from working. The immediate utility from working is then equal to the wage, \(w\). An employee risk losing her job at an exogenous rate \(q\). \(r\) is the interest rate which is constant and exogenous and \(\frac{1}{1+r}\) is the discount factor.

We start by expressing the expected discounted utility from working:

\[
(3.1) \quad rV_e = E(w) + q(V_u - V_e)
\]

The expected discounted income is equal to the expected wage plus expected average income loss from losing a job.

Rearranging (3.1), the discounted expected utility of an employee receiving a specific wage, \(w\), can thus be expressed:

\[
(3.2) \quad V_e(w) - V_u = \frac{w - rV_u}{r + q}
\]

The gain from working is increasing in wage accepted and decreasing in utility from unemployment. Since \(V_u\) does not depend on the specific wage offer, \(V_e(w)\) is a linear increasing function of \(w\).

\(^6\) The basic search model is adapted from Cahuc and Zylberberg (2004): 109-114.
An unemployed worker looks for a job until she has found work, and then she stops searching. The applicant will accept a job offer if the discounted expected utility from the offered wage $w$, is higher than, or equal to, the utility from staying unemployed: $V_e(w) \geq V_u$. In this case she will be equal or better off by working than by staying unemployed. Hence, an unemployed person will stop searching when the wage offered is higher than, or equal to, the reservation utility $x = rV_u$, where $rV_u$ is the expected discounted utility of being unemployed. So, for instance, if a job offers a wage equal to $x$, the applicant will get utility from working equal to the utility of staying unemployed ($V_e(w) = V_u$). $x$ is the reservation wage, which is the lowest wage offer that the job-seeker will accept. If the wage offered is lower than $x$, the expected utility will be higher if the applicant stays unemployed. On the other hand, if the wage offered exceeds the reservation wage, there will be gains in terms of increased expected utility from working. At last, if the wage offered equals $x$, the job-seeker may just as well work, since the expected utility from unemployment and working is the same.

A candidate’s success of searching for a job depends on the arrival rate of jobs; $\mu$. This rate captures how easy it is to get work. The arrival rate reflects the labor market situation, as well as personal characteristics of the job-seeker, such as race, education and skills. The effort of the job-seeker is also captured in the arrival rate.

Furthermore, the job search comes with a cost, $c > 0$, at all times. The costs include money to maintain a living while searching, as well as opportunity costs that reflect the time that could have been allocated to other activities. There are gains from searching as well, denoted by $g > 0$. Such gains can for instance be leisure and welfare benefits. The job-seeker gets a net gain $(g - c)$ at all times.

The expected discounted utility from searching is:

\[ rV_u = (g - c) + \mu(V_e - V_u) \]  

(3.3)

The rate of return of unemployment is equal to the net gains and the expected gains from getting a job.

Now, inserting $x = rV_u$ in equation (3.3) and inserting this in (3.4) gives the reservation wage $x$:
Equation (3.4) expresses the optimal reservation wage for an unemployed. The reservation wage is increasing in net gains \((g - c)\), the arrival rate of jobs \((\mu)\) and gains from working \((w - x)\). It is decreasing in the interest rate \((r)\) and the separation rate \((q)\). The reservation wage reflects the worker’s outside option of employment. If the consequences of not accepting an offer mean big net gains and high probabilities of obtaining another income, this is a relatively good outside option that increases the reservation wage. On the other hand, if net gains are small and it is difficult to obtain another job, the reservation wage will be lower.

An immigrant’s reservation wage may be lower from that of a native. First, the search costs may be higher. This could be due to the fact that an immigrant most likely has fewer savings to maintain a living while searching. Further on, immigrants will probably spend more time on an application for a job, because of lacking information about vacancies and poorer language skills than natives. Hence, immigrants may on average face higher search costs than natives. Second, gains from searching may be lower because new immigrants who do not have a work history may not be eligible for unemployment benefits. Higher costs and lower gains lower the reservation wage.

Second, the arrival rate of jobs, \(\mu\), may be lower for immigrants. If employers are not able (or willing) to differentiate between immigrants, so that they think of non-Western immigrants as being one group with lower productivity than natives, this will lower the arrival rate of jobs for immigrants. Moreover, if immigrants have less country-specific human capital, relative to natives, this reduces productivity and lowers the arrival rate. Lower arrival rate gives lower probability of finding a job and, consequently, lower reservation wage.

Third, the separation rate, \(q\), may be higher for immigrants because immigrants often settle in the secondary labor market with more turnover of workers. Fourth, in the low-skilled labor market, immigrants face lower wages, \(w\), which decrease the utility from working. In addition, immigrants may think of wages as being lower, perhaps because they compare themselves to other low-paid workers. All these differences between natives and immigrants will lower the reservation wage.
A lower reservation wage results in a shorter period of job-search and unemployment. To see this, let $[1 - H(w)]$ be the probability of receiving a job-offer which is high enough for the worker to accept. This happens at the rate $\mu$. The average duration of unemployment is:

$$T_u = \frac{1}{\mu[1 - H(x)]}$$

When the reservation wage decreases, ceteris paribus, this reduces the duration of unemployment.

But this result contradicts the observed facts that immigrants are more long-term unemployment than natives. Why might this be the case? Perhaps the answer is that the lower arrival rate, $\mu$, for immigrants has little effect on the reservation wage, perhaps because wages offered are close to the reservation wage. However, the impact of the arrival rate on unemployment duration can be big. Another explanation can be that some immigrants will not want to settle in the secondary labor market, because they are overqualified for such jobs. Thus, the limited transferability of skills, as well as employers’ perception of immigrant productivity as being equal for the whole group, may result in unemployment. The latter mechanism will be addressed further in the next section.

Concluding this section, I will try to draw some implications from the search model. First, shorter period of job-search for immigrants relative to natives may cause immigrants to settle in the secondary labor market with lower wages and more turnover of workers. Second, if immigrants are deprived of rights to welfare benefits, this will result in lower gains from searching and shorter period of job search. This is another way of saying that unemployment duration will be longer if welfare benefits are high. In countries where benefits are attached to work history, non-eligibility of such benefits may, everything else held constant, result in shorter period of job search and employment in low-paid jobs in the secondary labor market. In universal welfare states, the job searching period is longer and reservation rate is higher, ceteris paribus. This may result in higher-paid jobs for immigrants, although unemployment duration is longer. Furthermore, arrival rates vary across countries depending on transferability of skills and level of (perceived) human capital, as well as labor market structure and economic activity. Search costs may differ across countries as well, depending on access to job-counseling and how difficult the language spoken in host- country is.
3.2.3 Productivity

As mentioned above, employers’ perception of immigrants as being less productive than natives can be an explanation of poor integration outcomes. This could be due to information problems, discrimination, and other factors that intervene in the screening process. When the entry wage is high, the employers’ expectation of immigrant productivity level may be too low to enter the market at the entry wage. Employers would more often hire the more productive natives. Thus, immigrants are more often at the margin of the labor market. On the other hand, if wages are flexible and immigrants have lower bargaining power than natives, unemployment would decrease, but at the cost of lower wages.

On this note, assume production of a good uses two inputs; immigrants \( (N_I) \) and natives \( (N_N) \). Immigrants and natives are imperfect substitutes. The economy is competitive with firms producing to meet the constant elasticity demand curve. Prices are set to one. The maximization problem is given by a constant elasticity of production function, minus input costs\(^7\):

\[
(3.6) \quad \max_{N_I, N_N} \pi = \max_{N_I, N_N} (N_I^\rho + \delta N_N^\rho)^{\alpha/\rho} - N_I w_I - N_N w_N
\]

where \( \delta \) is the relative productivity of natives in terms of immigrants, and \( w_I \) and \( w_N \) refer to the wage of immigrants and natives.

After some rearranging, the first-order conditions give:

\[
(3.7) \quad \frac{N_I}{N_N} = \left(\frac{w_N}{\delta w_I}\right)^{\frac{1}{1-\rho}}
\]

Where \( \sigma = \frac{1}{1-\rho} > 1 \) is the elasticity of substitution between immigrants and natives. Relative demand for natives and immigrants depend on relative wages and relative productivity of natives.

---

\(^7\) This wage bargaining model is taken from Causa and Jean (2007) and Rodriguez-Palenzuela (2002)
Let $L_I$ and $L_N$ be the fixed labor supply of immigrants and natives. Then, the unemployment rates are $u_I = \frac{L_I-N_I}{L_I}$ for immigrants and $u_N = \frac{L_N-N_N}{L_N}$ for natives. Taking the logs of equation (3.7) and inserting for the employment rates, while using $\ln(1 - u) = -u$ gives the unemployment gap between immigrants and natives:

\[(3.8) \quad u_I - u_N = \sigma\ln\delta + \sigma(ln w_I - ln w_N) + \ln L_I - \ln L_N\]

The unemployment gap is explained by the relative efficiency of natives, relative wages and relative labor supply. The relative productivity and the elasticity of substitution for immigrants and natives can be explained by the perception of the employer. If the employer believes that natives are more productive than immigrants, $\delta > 1$, the unemployment gap will be positive, ceteris paribus. The substitution elasticity, $\sigma$, will have the same effect. An increase in the bargaining power of immigrants raises their wage, $w_I$. This will in turn increase the unemployment gap. Moreover, an increase in the aggregate reservation wage, raises the immigrant wage and increases the unemployment gap to the disadvantage of immigrants. Wages are affected by wage bargaining structure, degree of employment protection and welfare benefits. These are all important features of the welfare state construct.

Looking beyond the model above, the immigrant-native gap is expected to be more important in countries with a low proportion of low-skilled jobs, as immigrants often are low-skilled. In these countries, immigrants must apply for higher-skilled higher-paid work. In the upper part of the occupational ladder, perfect matching is more important and workers are hired more on the grounds of human capital and characteristics, than on the basis of profit maximization (Kogan, 2006). Because of information problems, immigrants will have a harder time entering the market in countries with few low-skilled jobs. Such information problems are for instance present in the limited transferable skills of immigrants, which create difficulties in recognition of foreign educational skills and experience in host country, and worsen the possibilities for immigrants to enter the labor market. The importance of transferable skills is greater in countries with few low-skill low-paid jobs.
3.2.4 Labor Market Protection

The degree of labor market protection with regard to possibilities for dismissals of employees, and to temporary and permanent contracts, affects labor market participation as well. Few opportunities for temporary contracts and dismissals raise firing costs. In many countries, regulations require that workers must be compensated when dismissed. In addition, there are laws regulating how long a worker can continue after he or she is informed of dismissal. Hence, the costs of imperfect match increase. These firing costs reduce turnover of workers, because it is relatively expensive to hire new workers. This will in turn enforce the importance of matching between productivity and wage, and so, the hiring costs are increased.

Since labor market protection reduces both the number of hirings and firings, it is difficult to say something about the effect. However, for immigrants trying to enter employment, protection is a disadvantage. In addition, strong regulation that makes it difficult to enter may result in more long-term unemployment.

From the immigrant’s perspective, a high entry wage would make work more attractive, for a fixed level of welfare benefits. Assume that the employer offers a wage, which is determined by the wage bargaining model applied in each country. The worker chooses his or her own effort level, which is unobservable to the employer, but the effort level increases the probability of keeping the job. How difficult it is to be fired depends on employment regulation. The decision making structure is as follow: First, the employer offers a wage, w. Second, the worker rejects or accepts the contract. Third, the worker decides on an effort level. At last, the employer decides if the contract should be renewed, or if the worker should be fired. In a weakly controlled labor market, where employees have low bargaining power, workers have incentives to increase efforts to have the contract renewed, provided that he or she is risk averse. However, ex ante, a risk averse worker may be reluctant to apply for the job and may even quit, because of the insecurity related to it. This implies that supply will shift inwards. This problem may be resolved in a highly protected labor market, although some studies show that employees actually feel less secure in sectors with a high degree of protection, likely due to difficulties to re-enter (reviewed in Econ-rapport, 2009) Also, high firing costs may cause the worker to slack off, resulting in lower productivity.
3.2.5 New jobs

For a fixed level of firms, immigrants tend to be the outsiders in the labor market. The excess immigrant labor supply would be larger in countries with a high minimum wage and few low-skill jobs. However, a big proportion of low-skilled employers could give rise to incentives for creation of new businesses. This process may be hampered in some countries.

For firms in sectors that are more exposed to risk, like for instance in construction, employment protection makes it difficult to adjust to the economic conditions in the economy. This may lead to substitution of labor for capital, or make it too risky to start new businesses. Strong protection transfers risk from the employee to the employer. Increased risk causes the levels of investments in new and existing firms to decline. Besides, new firms may be more vulnerable to risk, and this may result in fewer new firms.

The productivity of the employee is important for entrepreneurs who hire workers. On the one hand, reduced turnover increases the investment in the employee, as each worker becomes more valuable to the firm. This results in higher skill acquisition and higher productivity. However, reduced turnover hampers the mobility of labor. Hence, efficiency can be reduced. The productivity outcomes will be of importance to investors, and thus to creation of new jobs for immigrants.

Increased possibilities for temporary contracts would reduce firing costs, increase turnover, and reduce unemployment. If in addition wages are dispersed, this would come at a cost of lower wages for immigrants, as immigrants are faced with the lowest wages. Another disadvantage is that temporary contracts can result in permanent marginalization in the labor market, with low wages and low levels of human capital, and not as an entry port to permanent work. There may thus be a trade-off between low-paid employment on the one hand, and unemployment and high probabilities for welfare dependency on the other hand. Further on, the reductions in the employer’s investment in employees as a result of eased restrictions, may cause lower productivity, and thus reduce the number of new jobs.

One last point to be mentioned here, is whether or not the immigrant group is considered to be temporary or permanent may be an important determinant of investment in human capital, and thus an important determinant of integration. Immigrants who came as guest workers to Western Europe in the 1970s were considered to stay in the host-country only temporary. The investment in country specific human capital may consequently have been poorer for this
group. Furthermore, business cycles are important for immigrants’ employment possibilities (see for instance Bratsberg et al. 2006). Immigrants who arrive in a period with low economic activity may experience a disadvantage in the labor market many years after immigration. Unemployment in the first period after immigration is then an important determinant of integration in the long run.

3.2.6 Incentives in the Benefit System

Welfare benefits are important to secure an income in times of unemployment and sickness, and to supplement low incomes. When job-seeking effort is unobservable, such transfers from the state can increase incentives to seek suited employment. Yet, it is also a possibility that welfare benefits may work as a substitute for incomes in the labor market.

So why should Non-Western immigrants’ incentives differ from natives”? There can be several reasons. First, the decision whether or not to integrate depends on the costs and benefits of integration. The costs include time and recourses spent on acquiring country specific human capital, such as language, while benefits include the expected wage after investments in human capital have been made. If costs are too high, immigrants may choose to depend on welfare benefits, rather than securing a job. Whether or not the difference between the expected wage and the welfare benefits is high enough to outweigh the costs of integration, depends on welfare state generosity and wages. There should thus be a gap in welfare dependency and labor market participation between natives and immigrants, since the latter face integration costs while natives do not. Immigrants then gain less from working than natives.

Second, the incentives for investment in human capital can be even more weakened if immigrants are faced with lower labor market incomes than natives. This could possibly be due to lower skills or discrimination by employers. Third, reservation incomes may be lower among immigrants. Since immigrants are overrepresented in low-paid jobs, they face a smaller loss by becoming a welfare recipient, than would an individual with a high income. In addition, immigrants from poorer parts of the world may think of the level of welfare benefits as being higher, and thus more attractive, than well-fed natives.

In general, there are incentives and disincentives arising from welfare organization. High replacement rates will raise incentives to obtain an income in the labor market, if welfare
benefits are linked to work history. A job may then be an entry port to the most generous insurance schemes, such as unemployment and sick leave benefits. The higher the replacement rate, the higher the incentives to work. Furthermore, it is reasonable to believe that benefits attached to work history will raise incentives for unemployed people to get a job, so that they too can be covered by insurance, if they were to lose their job or get sick. As a result this is expressed in lower reservation wage among immigrants that are new in the labor market and among long-term unemployed.

On the other hand, generous welfare benefits that can be obtained outside the labor market, i.e. that are not linked to work history, may give rise to disincentives to enter the labor force and to maintain employment. These types of welfare benefits can for instance be benefits to families with dependent children, low-income supplements, housing benefits, disability support pension and benefits to people with status as refugee. Such benefits contribute to raise the reservation wage of unemployed. The degree to which a person can obtain an income outside the labor market varies across welfare regimes. Therefore, the incentives for securing a job differ as well.

Generous welfare benefits allow recently arrived immigrants to spend time (or take the risk) on acquiring country specific capital, such as language and culture-conditioned social etiquettes, before entering the labor market. Welfare programs may also provide the participants with job training. Participation in welfare programs may thus result in better job-search skills and higher level of human capital that improve chances of getting a job that matches the candidate’s qualifications. This ‘subsidized search’ can improve immigrants’ possibilities to get work as well as higher paid jobs, compared to if they were to enter a low-skilled low-paid sector. Depending on number of unskilled jobs, bargaining power and labor market protection, the importance of investment in language, job training and other country specific human capital may vary across states.

However, receiving welfare benefits for a period of time comes at a cost of lacking work experience in the first period, which has shown to be important in immigrants’ integration process (Causa and Jean, 2007). Furthermore, if participation in welfare programs is not time constrained, disincentives can arise. People may find it more profitable to relay on benefit transfers from the state, rather than to obtain incomes in the labor market. These disincentives should be increasing in the level of replacement rates and preferences for leisure. However, if for instance unemployment benefits are time constrained and regressive, so that short-term
unemployed get higher benefits on the expense of the long-term unemployed, the bargaining power of the employee increases. This puts pressure on wages and contributes to more unemployment, which is a disadvantage to new immigrants’ labor market entry. On the other hand, regressive benefits increase the incentives for job search and lower the reservation wage of the long-term unemployed.

Even if incomes are higher in the labor market, immigrants’ possible lower reservation income may result in higher welfare use than for natives. Moreover, generous welfare benefits, targeting married couples with several small children, can result in very high replacement rates and thereby give disincentives to work. This is more likely to be the case for immigrants, because they are overrepresented in this group (Liebig, 2009). A magnifying effect could be that immigrant women may have stronger preferences for staying home with children.

Although immigrants in some demographic groups will benefit from being on welfare relative to working, it looks as if immigrants want to be self-sufficient (Liebig, 2009). Immigrant employment often increases with the duration of stay in the host country. This explanation is supported by the observation that low-paid self-employment among immigrants function as an option for marginalization in the labor market. Hence, there are some incentives operating in favor of employment. Such favoring incentives could be stigmas linked to receiving welfare benefits and relaying on the state, as opposed to having a paid job. Besides, in some cultures, having a job may be more important for behavioral factors such as intrinsic motivation and self-respect. Consequently, some immigrants may get less disutility from working than natives. They could even, to some extent, gain positive utility from working.

Moreover, the relative perception of the level of welfare benefits may vary across immigrant groups, depending on what standard of living immigrants are used to and to whom they compare themselves to. In addition, the stigma associated with being on welfare depends on the attitudes towards benefits in the ethnic network.

Further on, the generosity of the welfare state affects immigrants’ occupational choice. The safety net offered by the welfare state may cause people to take on more risk when choosing a job. The protection offered by the welfare state makes people participate in activities associated with higher risks and profits, than they would without this insurance (Sinn, 1995).

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8 Section 4.4 explores the topic of self-employment further.
This could be more important for immigrants, because they may be less risk averse than natives. After all, those who choose to migrate from their country of birth may be relatively more risk-seeking than those who stay behind. Risk-seeking behavior may cause immigrants to get jobs with high risks of becoming unemployed, but with potentially high incomes. Non-Western immigrants are indeed overrepresented in self-employment, which is an occupation with less protection against risk. On the one hand, the insurance offered by the welfare state may remove obstacles and give people, in this case immigrants, opportunity to choose risky occupations that no one want. On the other hand, the safety net may cause moral hazard, in terms of too risky behavior, that results in a worse state than without the safety net. These two scenarios have different implications for the economy. If the first scenario is true, then redistribution by the welfare state may lead to higher incomes for immigrants. If on the contrary the second is true, redistribution gives more inequality for immigrants. Then, if immigrants have more risky behavior than natives, immigrants will face lower incomes.

### 3.2.7 Interactions between Welfare Regime and Labor Market Structure

Welfare organization interacts with the labor market structure and affects immigrants’ labor market integration. In liberal welfare states, the labor markets are characterized by wage flexibility, decentralized industrial relations and market-based social insurance (Engelen, 2002, as described in Kogan, 2006). The conservative welfare states in Central-Europe have more rigid labor markets, high labor costs, relatively compressed wage structures and employment based social insurance. Social democratic regimes, such as the Scandinavian countries, are similar to the conservative regimes with regard to the labor market, except for universal social insurance that characterizes these countries (ibid.).

The Scandinavian countries have high replacement rates. These countries do also have a low share of low-skill low-paid jobs. Immigrants have easier access to low-skill jobs because they are hired more on the same terms as natives in the low-skilled sector. Lack of such work can therefore be a disadvantage to immigrants’ labor market entry. On the other hand, high replacement rates can allow immigrants to restructure and apply for high-skill work. Even though entry wages are high in the Scandinavian countries, immigrants are faced with lower wages than natives. Relatively low wages for immigrants would make welfare benefits more attractive for immigrants than natives. In addition, generous welfare benefits increase the
reservation wage and the corresponding replacement rate, and thereby make the labor market less attractive. Besides, a rigid labor market makes it more difficult to enter, although when entered, wages are high.

In the Scandinavian model, the benefit system is universal and to a less extent attached to work history, as opposed to the continental model. In the continental countries, immigrants will have higher incentives to work, but lower incentives to invest in restructuring and job search. Moreover, the high entry wage in Scandinavia raises employers’ incentives to substitute low-skilled labor for capital, to a larger extent than for instance in Germany and Austria. This could explain why immigrants have more complex problems in getting a low-skilled job in some countries. However, this does not explain why Denmark has a relatively high level of low-skill jobs (Liebig, 2009).

The Anglo-Saxon countries on the other hand, have relatively flexible labor markets. These countries have low benefit levels and flexible wages compared to the Scandinavian and Continental countries. This raises the incentives to work, but leaves little room for restructuring. The immigrant-native gap in wages may thus be large in the English-speaking countries and following, employment should be higher.

Kogan (2006) uses data for several EU countries to test the hypothesis, that liberal welfare regimes display lower chances for unemployment among immigrants, compared to the conservative and social democratic regimes. The European Union Labor Force Survey data set for the years 1992 to 2000 is used. The data contains, among other variables, information on unemployment, education, migration and demographic characteristics. The immigrants in question are third-country immigrants. The regressions include individual characteristics and welfare regime dummies (fixed effects).

The findings suggest that immigrants in the liberal states in question (Ireland and UK) have lower probabilities of becoming unemployed, relative to natives, than immigrants in the conservative states of interest (Germany, Belgium and France). The immigrant-native gap is largest in the social democratic states in the study (Sweden and Denmark). Immigrants in these states face the biggest risk of becoming unemployed. These results seem to confirm the assumption that labor market structure is an important part of the welfare state.

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9 Third-country immigrants are immigrants who are not from the EU-15 countries or Norway, Iceland, Switzerland, the US, Canada, Australia, New Zealand or Japan.
Kogan further suggests that immigrants will be more unemployed in countries with stringent labor market regulations, than in countries with labor market flexibility. In highly protected labor markets, employers are faced with high firing costs. This may cause employers to set the productivity expectations higher for possible recruits. The productivity expectations include human capital, as well as characteristics, such as gender and immigrant status. This may induce employers to let discrimination interfere in the screening process. Thus, natives are preferred to immigrants in the employment process, especially for high-skill jobs where the need for perfect match is important.

At the low end of the occupational ladder, on the other hand, immigrants and natives are chosen more on the same terms, since the employers to a greater extent operate in accordance to profit maximization in this context. In countries with large sectors with low-paid and low-skilled jobs, immigrants will have better chances to enter the labor market. The ‘raw’ data confirms that the Southern European countries have a large low-skilled sector and very strict labor market protection (EPL Index). In these countries, immigrants have lower unemployment rates. In the UK and Ireland, immigrants benefit from the low labor market protection (ibid.).

Figure 3.3: Labor Market Indicators and Unemployment Disadvantage of Recent Third-Country Male Immigrants

The outcomes of the regression analyses suggest that in countries with less strict labor market protection, immigrants have better chances of labor market entry. In the Southern European countries, where low-skilled sectors are large, but with a high degree of labor market

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10 Figure from Kogan (2006)
protection, immigration is more temporary. The low unemployment in these countries can be explained by better matching in supply and demand of labor. Moreover, the analysis confirms that male immigrants are less unemployed in countries with flexible labor markets (ibid.).

Cusa and Jean (2007) estimate the effect of labor market policies on immigrants’ relative employment in 12 OECD countries. The data are from surveys drawn from panel households including immigrants and natives over parts of the 1994-2003 period. Immigrants are defined as those born abroad.

There are large variations in immigrant labor market performance across countries. When comparing with comparable natives, non-EU/non-English-speaking male immigrants have the lowest employment rate in the only Scandinavian country in the study; Denmark. The immigrant-native gap in employment is relatively small in Austria, compared to the other countries of interest.

The findings of the regression analysis suggest that labor market policies affect immigrants’ employment rate, when education, marital status, household characteristics and potential labor market experience are controlled for. First, a higher minimum wage increases the employment gap between natives and immigrants. Second, generous unemployment benefits increases the chance of unemployment of active immigrant men, relative to natives (ibid.).

Further on, the relative level of which employment contracts are divided into temporary and permanent, affects immigrants’ labor market participation. If immigrants are more often employed on a temporary contract, this will decrease immigrants’ relative bargaining power. In countries with weakly regulated labor markets (more use of temporary contracts), immigrants will face lower wages, but higher probabilities for employment, compared to natives. This is true for all immigrants, except for women with more than 15 years of residence (ibid.).

At last, an interesting result is that of Bisin et al. (2010), which suggests that countries with a flexible labor market, such as UK and Ireland, have labor markets with easier access to first jobs for immigrants. However, these countries fail to protect immigrants with strong ethnic identity, because of the weak labor market protection with regard to dismissals and use of temporary contracts. Consequently, immigrants with strong ethnic identity may be the losers in the labor market.
3.3 Welfare States and Integration Policies

An important aspect of the welfare state is integration policies. Such policies grant immigrants with rights, cultural recognition and eligibility of welfare benefits. The policy philosophy of multiculturalism suggests that immigrants will integrate better the easier and quicker they can obtain formal equality, and the more they can retain and develop their own cultural identities and practices (Koopmanns, 2010). Such policies aim to accommodate immigrants, rather than suppress immigrant identity (Banting and Kymlicka, 2006). However, these types of policies have shown to fail throughout Europe.

According to the Migrant Integration Policy Index, Sweden and Portugal are the most generous countries in Europe in granting immigrants with the same rights as natives, by adapting the legal framework to promote integration. Sweden has the highest scores when it comes to labor market access, family reunion, long-term residence, political participation, access to nationality and anti-discrimination policies. The countries with the lowest scores are Switzerland, Hungary, Denmark, Greece and Austria. The Netherlands, Norway, UK, Luxembourg and Germany perform intermediately.

Figure 3.4: Overall integration policy rankings

Note: 100 is the best possible practice

Source: Migrant Integration Policy Index (www.integrationindex.eu)
This section discusses how integration policies affect immigrant labor market participation. First, countries are divided into policy regimes in order to explain integration outcomes. Second, interactions between the welfare state and integration policies are discussed.

### 3.3.1 Policy Regimes

Bisin et al. (2009) divide European countries according to integration policies to explore how such policies can affect non-European immigrants’ labor market participation. Immigrants are defined as first and second generation. Countries are classified according to the Migrant Integration Policy Index’s ratings. The authors use data from the European Social Survey, which covers 25 countries in EU, and Norway and Switzerland. The dataset includes information about socio-economic characteristics of persons and labor market outcomes of immigrants and natives. In addition, the data contains information on ethnic identity, like questions of the importance of following traditions and customs, and the magnitude of religion and language spoken at home. Strong ethnic identity is associated with a significantly lower probability of being employed, throughout Europe.

One group of countries consisting of Ireland, France, Luxembourg and Hungary, score poorly on the ratings for labor market access, family reunion, political participation and especially access to long-term residence. They have, on the other hand, relatively good access to nationality and anti-discrimination policies. However, in this group of countries, immigrants face the highest penalty in terms of unemployment for strong ethnic identity.

In the second group, consisting of Norway, Italy and Spain, there is not a penalty associated with strong ethnic identity, but rather a premium. These countries perform poorly when it comes to access to nationality and anti-discrimination. Nonetheless, they achieve good scores in labor market access, family reunion, political participation policies and particularly in long-term residence policy.

The countries of Sweden, Finland, Belgium, the Netherlands, Portugal and UK have lower penalties than the first group, but do not perform as well as the second group. They have higher scores in integration policies than the second group, except for long-term resident policy.
The findings from the regressions suggest that when immigrants have strong ethnic identity, labor market policies have the strongest and positive impact on employment probability, but that access to nationality may have a negative effect on probability for employment. The latter may help explain why Sweden and the Netherlands perform worse than the group of Norway, Italy and Spain; easy access to nationality combined with a generous welfare state can have a negative impact on labor market participation.

It is important to be aware of that this categorization of countries is based on countries’ laws and rights granted immigrants, and not on actual practices. There may well be rules and conducts in the labor market in each country that influence the importance of laws on immigrant integration. Besides, there is a problem with the endogeneity of integration policies. Countries with a low degree of integration may have extensive integration policies.

Bisin et al. conclude that the combination of ethnic identity and labor-market access policies matter most for employment probability. Naturalization alone is not important in determining the probability of an immigrant with ethnic identity being employed. This could be due to the fact that there are weak links between citizenship and entitlements to welfare benefits, the symbolic value associated with citizenship, as well as special privileges granted citizens (Chiswick and Miller, 1995). Whether or not immigrant naturalization affects the economic performance of immigrants, may depend on the strength of these links.

For instance for the US, results show a five percent earnings premium associated with citizenship (Chiswick and Miller 1992, as described in Chiswick and Miller, 1995). The reason for this could be that citizenship to the US is associated with higher symbolic value, presence of economic privileges for sponsoring relatives, as well as the presence of links between citizenship and welfare entitlements.

Furthermore, Kogan (2003) finds that the effect of naturalization on labor market outcomes varies between Sweden and Austria, when period of immigration and socio-demographic characteristics are controlled for. Whereas Sweden is a universal welfare state, where immigration is considered to be permanent, and residents benefit from the same social and economic rights as natives, Austria is restrictive in granting non-citizens with rights. Because social and economic rights are not attached to citizenship in Sweden, naturalization does not affect labor market outcomes per se, when controlling for period of immigration. The poorer labor market outcomes among non-citizens are explained by short time of residence in
Sweden. In Austria, on the other hand, citizenship has a positive effect on immigrants’ labor market outcomes. Citizenship gives immigrants the same rights as natives and reduces the chance of low-status jobs and employment in the non-tertiary sector.

From the results presented by Bisin et al., it can seem as if the relationship between anti-discrimination policies and practiced anti-discrimination is weak, or that anti-discrimination is a weak determinant of immigrant employment. However, there is evidence that discrimination is a significant determinant of the probability of immigrant employment. For example, Carlsson and Rooth (2006) found evidence of immigrants from the Middle East being discriminated in the Swedish labor market. When employers in small firms were faced with the choice of calling applicants for an interview, they less often called persons with Middle Eastern names, in spite of the fact that these persons had the same skill-level as other candidates. For the US, Bertrand and Mullainathan (2004) reported that applicants with White-sounding names were 50 percent more likely to be called for a job interview than names that sounded African-American. Discrimination was true independent of type of jobs, firm size and type of industry. These findings imply that discrimination is an important determinant of immigrant employment.

3.3.2 Interactions between Welfare Regimes and Policies

Integration policies and welfare regimes interact in a variety of ways. Integration policies decide who gets access to certain rights, and thus who are granted welfare benefits. Countries can be categorized according to types of welfare regimes and integration policies, inspired by Esping-Anderson’s classification of social democratic, conservative and liberal regimes.

Koopmans (2010) argues that there is a trade-off in granting immigrants with the same rights as natives and fronting a policy that obtain cultural differences. Giving immigrants and natives the same rights and welfare benefits will on the one hand increase immigrant welfare. It can, however, on the other hand, lead to dependence of welfare benefits and thus create economic inequality. He suggests, referring to employment rates in eight European countries on integration outcomes, that multicultural policies combined with a generous welfare state have produced low levels of labor market participation compared to that of the native population. Further on, he argues that the structure of the welfare state decides the socioeconomic position of immigrants in different countries.
Among the countries in the study, Sweden is a typically social democratic regime. Koopmans defines France, Germany and Switzerland as conservative regimes, and UK as a liberal regime, and argues that Austria, Belgium and the Netherlands have elements from both the conservative and social democratic types.

According to Koopmans, the Netherlands is an example of a state, which has fronted a multicultural policy combined with generous welfare benefits. The country is now a leading example of failure of successful immigrant integration, and is among those European countries where immigrants have the worst socioeconomic position in spite of a large scale of recognition and rights. Furthermore, Belgium and Sweden are also examples of states with poor immigrant integration, compared to Austria, Germany or Switzerland with less inclusive integration policies or in contrast to the UK with a less generous welfare state (ibid.).

Sweden, Belgium and the Netherlands have high naturalization rates, while Germany and Austria have low. In addition, long-term dependency of social benefits can block possibilities for naturalization in Germany and Switzerland. Moreover, cultural rights are extensive in the Netherlands. Until 2004, the Netherlands was one of few countries to offer full state funding of ‘own language and culture ‘classes in public schools. Further on, fully state funded Muslim and Hindu schools have been allowed in the Dutch education system. There are also subsidized Muslim and Hindu broadcasting organizations, as well as 20 percent reserved broadcasting time on public TV and radio for programs accommodating ethnic minorities. Moreover, some public housing corporations have built special homes designed for some ethnic and religious groups. One example is a housing project for Muslims, where the toilet seat did not face Mecca. The kitchen was in a separate room, centered in the middle of the apartment, so that the women could serve the men without being seen by them (ibid.).

Koopmans argues that the degree of ‘decommodification’ matters for immigrants’ socioeconomic position out of three reasons. First, through the negative selection effect, which arises when immigrants with poor educational skills and low labor market position tend to migrate to a country with a relative equal income distribution and high degree of insurance against economic inequalities. Second, through investments in human capital to improve the labor market position. It is likely that generous welfare benefits will weaken the incentives to make such investments, because it is possible to maintain a decent standard of living without making the effort to invest. At last, these two reasons can be magnified by a third component; the subjective perception of the levels of social benefits. It is likely that an immigrant from
poorer parts of the world will think of the benefit levels in the host country as higher than natives, and thus be more content with the benefits and more reluctant to apply for work.

From the arguments above, Koopmans derive the following hypothesis:

‘Welfare regimes and integration policies interact multiplicatively: Countries that have either limited welfare states with low provision level (UK) or exclusive policies that make immigrants’ rights dependent on cultural assimilation and avoidance of welfare dependence (Austria, Switzerland, Germany) will have a relatively high labor market participation of immigrants. Conversely, countries that have comparatively generous welfare states and multicultural integration policies (Sweden, Netherlands, Belgium-Flanders) will have relatively low labor market participation of immigrants. Countries that combine a comparatively generous welfare state with integration that are individually inclusive, but culturally assimilationist will have intermediate levels of immigrant labor market participation (France, Belgium-Wallonia)’ (ibid.).

This hypothesis is interesting, and it may be confirmed by looking at the employment levels of non-Western immigrants introduced in the beginning of the chapter. However, this does not explain why for instance Norway, a country with a generous and universal welfare state and multicultural policies, has high immigrant employment rates. In further studies of this hypothesis, one should therefore include empirical analyses with control variables, such as education and country of origin, to better understand the causal effects. Since Koopmans simply compares employment rates across countries, it is unknown whether the differences across countries are due to welfare regimes, immigration and integration policies, or other factors such as self-selection and demographic composition.

Büchel and Frick (2005) take control variables into account when they use the welfare state framework to analyze the economic performance of immigrants in eight European countries. They use household panel data for the years 1994-1998 for the countries Denmark, Great Britain, Italy, Luxembourg, Spain, West Germany, Ireland and the Netherlands. Denmark is considered to be a social democratic regime, while Great Britain and Ireland are categorized as liberal regimes. The other countries have traditionally been viewed as conservative, but the Southern European countries, among them Spain and Italy, differ from Central-European conservative countries, and may therefore be seen as a separate category (confer section 2.2).
The authors try to isolate the welfare state effect, i.e. the causes of institutional differences between countries from other parameters of immigrant policy, such as composition of immigrant population and integration behavior across countries. They argue that a successful integration policy should result in an equal labor market performance between natives and immigrants, when other factors are controlled for. The results suggest that this is not the case. Country-specific institutional features, such as restrictions on access to the labor market and parts of the social security system, that are connected to citizenship or immigrant status, play a significant role in restricting the economic performance of immigrants (ibid.).

Büchel and Frick compare immigrant households’ economic performance to the native population. Economic performance is measured as pre-government income, as well as post government income\(^1\). This income is divided into different components to find the most important source of income. Income portfolios, consisting of market income, non-market income, taxes and benefits, are then compared.

The findings suggest that wages and salaries are the most important sources of income for all residents in the major part of the countries considered, except from Denmark where only 40 percent of all immigrants depend mostly on wages and salaries. In Luxembourg, which is considered to be a conservative welfare regime, salaries and wages are more important to immigrants than to the native population. One reason for this can be that pensions are of less importance to this group. Concerning public transfers, immigrants in almost all the countries are more often receiving unemployment benefits than natives. For other social benefits, the difference between natives and immigrants is small in almost all countries. Again, the exception is Denmark, where other social benefits as primary income are five times higher for the immigrant population. 40 percent of the immigrant population has other social benefits as their major income. It is unclear whether these findings are explained by the capabilities of immigrants alone, or if there are socioeconomic and institutional factors that lie beneath. Büchel and Frick thus control for socioeconomic differences in the regression models.

Contribution of taxes and social security varies between the different welfare regimes. Taxes and social security contributions are by far largest in the only social democratic regime in the study; Denmark. First runners up are the conservative welfare regimes of Germany and Austria. In the liberal welfare regimes of Great Britain and Ireland, taxes and social security

\(^1\) Pre-government income is the market income, i.e. income before government redistribution, such as taxes and benefits.
are as expected low, though Luxembourg has equally low contributions. Moreover, taxes and social security paid by immigrants to Denmark are low. This can be due to the composition of the immigrant population, which is characterized by a high fraction of low-skilled immigrants from non-EU countries (ibid.). Nevertheless, in the majority of countries in the study, immigrants’ non-market income is lower than for the native population. In all the countries considered, with the exceptions of West-Germany and Denmark, immigrants are more heavily taxed than natives. This can have various explanations, such as discrimination, high immigrant incomes and better market performance by the immigrant population compared to natives. The latter is a plausible explanation for Ireland, where a large part of the immigrant population is from Great Britain and the US (ibid).

Furthermore, the findings suggest that non-EU immigrants living with a native adult perform better in the labor market, except for Denmark, Austria and West Germany, where immigrants perform worse. In almost all countries considered, non-EU immigrants not living with natives are the less assimilated group. However, it is only immigrants in Denmark and West Germany who profit considerably from redistribution. Moreover, the results show that Germany and Denmark have low levels of immigrant labor participation, but that the economic situation of immigrants improves with the duration of stay. These countries were also the ones where immigrants to the largest extent suffered from their immigrant status. The authors argue that this could indicate that Denmark and Germany to a large extent have successful integration policies, and that integration policies matter for the differential between natives’ and immigrants’ market performance, when socioeconomic characteristics are controlled for.

### 3.4 A Special Case: Immigrants from Former Yugoslavia and Turkey

Some of the biggest problems with the results discussed thus far are the difficulties concerning the causal effects of integration. In particular, it is difficult to control for the composition of the immigrant population. Besides, the time period of immigration can be of significant importance for the economic conditions immigrants are faced with in the host-country.

Now, we turn to two studies that try to isolate the effects of welfare state institutions, and integration and immigration policies, on immigrant labor market integration. These studies
compare one immigrant group’s outcomes in two host countries. By looking at one ethnic group instead of looking at immigrants in general, one can, to some extent, control for social and cultural background, and thus be surer to find the welfare state effects on integration outcomes.

**Ex-Yugoslavs in Austria and Sweden**

Kogan (2003) aims to explain how the institutional differences in welfare regimes, labor structures and integration policies affect immigrant labor integration, by comparing Yugoslavian immigrants in Sweden and Austria. She uses micro data for Austria in 1996, and data from the Swedish 1997 labor force survey to explain ex-Yugoslavs’ labor force participation, unemployment, occupational status and sector concentration in the two countries.

Looking at one immigrant group does not mean that individual characteristics are fully controlled for. The decision to migrate to Sweden or Austria may thus be explained by individual characteristics to some extent. Nevertheless, in both countries, Yugoslavs immigrated in the same time periods, first as labor migrants, then later due to family reunification and as refugees. For these reasons, one might be able explain how institutional differences in the two countries influence immigrant labor market integration.

There are institutional differences between Sweden and Austria. While entitlements to welfare benefits are citizen-based and universal in Sweden, benefits are employment-based in Austria. In Sweden, integration policies are extensive and multicultural, while these types of policies are scarce in Austria. The time from immigration to naturalization is twice as long in Austria compared to Sweden, and the latter has one of the easiest naturalization processes in Europe. In Austria, on the other hand, citizenship is restricted to those who have a regular income, a place to live, and to those who are integrated into the society. In addition, immigrants must give up their former nationality and have no criminal record. Immigration to Austria is to a relatively large extent characterized by temporary labor immigration, while immigrants in Sweden are mostly permitted on humanitarian grounds. There are differences in labor market structure as well. Whereas Sweden has an extended service sector, Austria has a relative large non-tertiary sector (ibid). Institutional differences are summarized in table 3.2.
Kogan argues that Yugoslavs have integrated better in Austria than in Sweden for two reasons. First, the increasing need for high-skilled labor in Sweden following the early 1970s resulted in lower labor market participation among immigrants in Sweden compared to immigrants in Austria. Immigrants (both high- and low-skilled) in Sweden meet greater competition in the labor market than in Austria, where demand for low-skilled labor better met the supply. Second, the two countries applied different integration policies in the 1970s. While Sweden implemented multicultural policies, Austria, had restrictive integration policies with social exclusion, temporary visas and lack of integration measures.

The study controls for individual characteristics such as education, age and regional unemployment in the regressions. The results imply that ex-Yugoslavs in Austria have equal or even higher labor participation rates than the native population, ceteris paribus. The same immigrant group in Sweden has lower participation than natives, but integration increases with the duration of stay. However, after 20 years in Sweden, ex-Yugoslavs are still much less likely to be employed than natives. This could be due to the fact that immigration to Austria was characterized in a greater extent by labor immigration. Moreover, the risk of unemployment of more recent ex-Yugoslavs is greater in Sweden than in Austria. The reason may be explained by the relatively worse economic situation in Sweden during the 1990s (ibid.).
Even though immigrants in Austria display higher labor market participation and lower risk of unemployment, immigrants are represented in low-status jobs in the secondary labor market. However, their chances for better occupational choice increase with the duration of the stay in Austria. In Sweden, employed ex-Yugoslavs are more often employed in high-status jobs than ex-Yugoslavs in Austria. Kogan suggests that these findings can be explained by the different structures of the two countries. In Austria, integration policies are employment-oriented, and loss of citizen rights is a consequence of unemployment. Furthermore, the labor market structure provides high demand for low-skilled labor. In Sweden, however, the universal welfare system provides immigrants with support in case of unemployment and during job training. This makes it possible for immigrants to seek suitable work, instead of being soaked up in low-skill employment (ibid.). Finally, it is worth mentioning that differences in integration outcomes may be due to language acquisition. It may well be that Yugoslavs had better proficiency in German than in Swedish. If this is the case, labor market participation may have little to do with welfare states and integration policies.

**Turks in Germany and the Netherlands**

Now turning to Germany and the Netherlands, Euwals et al. (2006) try to isolate the policy effects on integration outcomes by comparing Turkish immigrants’ labor market outcomes, relative to natives, in the two countries in question. The labor market outcomes include employment rates, tenured job rates and job prestige scores. The authors use micro data drawn from the German Socio-Economic Panel and data from the Dutch Social Position and Use of Provisions Survey and the Labour Force Survey in the year 2002. The study includes both first and second generation immigrants.

Germany and the Netherlands both recruited Turkish guest workers during the 1960s and 1970s. The two countries have quite similar labor market institutions, but the immigration and integration policies have varied. Family reunification policies have differed, with the Netherlands as the most liberal. While Germany has restrictive integration policies with low naturalization rates, the Netherlands on the other hand, has implemented multicultural policies to a large extent. Naturalization is relatively easy to obtain in the Netherlands, while it is difficult for immigrants without German ancestors to apply for naturalization in Germany. Yet another difference between the countries is that Germany implemented return migration policies in the early 1980s, a policy which the Netherlands never has introduced.
To explain how the differences in characteristics affect employment, Euwals et al. use a version of Oaxaca decomposition to separate differences in characteristics from other explanations. They find that Turkish immigrants have lower labor market participation relative to natives in both countries. This gap can be explained by age composition and lower level of education among the Turkish immigrants. The gap in employment between Turks and natives is for men 23 percentage points in Germany and 14 percentage points in the Netherlands. Particularly, men without children and elderly perform poorly compared to natives. In Germany, the lower educated Turks perform well in the labor market, and they have even higher employment rates than native Germans. The large number of low-skilled Turks may indicate a low level of investment in human capital which may not be favorable in the long run. Furthermore, the higher educated Turkish immigrants perform worse than their native counterparts.

When they control for observable characteristics, the employment gap remains large for the Netherlands, while it becomes smaller for Germany. When comparing the two countries, the immigrant-native gap in employment and tenured jobs is higher in the Netherlands than in Germany. On the other hand, the Turks in Germany are often employed in low-status jobs, compared to the Turks in the Netherlands.

These results imply that education is important for good labor market outcomes. When controlling for education, Euwals et al. find the native-immigrant employment gap to decrease. This could indicate that Germany has a composition of immigrants which is more favorable with regard to the labor market. This may be due to the restrictive immigration and return migration policies in Germany. Furthermore, the large gap for elderly men in the Netherlands may be due to the oil crises in 1979, which caused many Turkish male immigrants to depend on welfare. Finally, the authors mention discrimination and lack of networks within the firm as reasons to why highly educated immigrants have low job prestige scores.

In the two studies above, an important determinant of employment was omitted; namely language acquisition. Some of the effect may be picked up by the education control variable, but language proficiency should nevertheless be included in further studies.
3.5 Limitations

There are big empirical challenges in separating welfare state effects from other country specific effects. When explaining integration and immigration in relation to welfare state models, one cannot be sure that outcomes are the results of welfare state organization. When reviewing the literature, it is my impression that the authors in general do not show enough respect for these basic challenges when discussing their results.

Some challenges are listed below:

- Often, studies include country dummies in the regressions and argue that the differences observed in immigrant integration are due to institutional differences such as integration policies and welfare organization. However, one cannot rule out what part of the institution is affecting integration outcomes.

- Data across countries may not be comparable. There is no coordination in matching national statistics between countries. Data may have been collected in different time periods, with different definitions and with different calculation methods.

- Generalizing by drawing conclusion about welfare models is difficult when only looking at some countries. For instance, a study of immigrants in Denmark cannot conclude that the Scandinavian model gives poor integration outcomes. The external validity can be limited.

- Studies utilize surveys that are often not made to look at immigrants. It is natural to assume that new immigrants are underrepresented because they are overrepresented among non-respondents. Thus, the sample is biased.

- Comparable studies that utilize data across countries (e.g. the European survey) at one particular point in time (cross-sectional data) may fail to understand the underlying causes of outcomes.

- Language proficiency is omitted as control variable when causal effects between welfare state and integration is explained. In the liberal welfare states, English is spoken. Non-Western immigrants may have better skills in English than other
European languages since English is spoken in universities and in the media around the world. Thus, immigrants to these countries may be better integrated, not because of the welfare model, but simply because their language proficiency is better. In the case with Yugoslavs in Austria and Sweden, it may as well be the case that these immigrants knew German better than Swedish. Further investigations could therefore benefit from including such a variable or an instrument, to control for language skills.

- Welfare policies are endogenous. The status of immigrants may determine how welfare benefits are distributed. A large proportion of asylum seekers increase the need for welfare benefits. Since the causality runs both ways, the internal validity of such studies may be limited.

Nevertheless, the findings in this chapter are important to the understanding of how the welfare state affects immigrant integration.
4 Further Issues

Up until this point, the thesis has focused on linking organization of the welfare state to immigrant integration. In doing so, some important determinants of integration have been left out. Language acquisition is one important factor that decides integration. Furthermore, ethnic networks and ethnic residential segregation are important in determining demand for welfare benefits and employment. This section takes a closer look at these topics, in order to better understand employment outcomes.

4.1 Language

Language acquisition refers to the process in which immigrants who are not fluent in the resident country’s language improve their language skills. The literature of labor economics recognizes language acquisition as an important type of human capital affecting immigrants’ labor market participation. Several studies argue that integration policies that give immigrants right to claim benefits and support learning of minority languages can have a negative effect on labor market participation. On the other hand, policies that stress linguistic and cultural integration will exercise pressure on immigrants to obtain skills, knowledge and social ties that improve their labor market outcomes, such as earnings (Koopmans 2010, Chiswick and Miller, 1995). Increasingly more countries have stricter language requirements and tests, with sanctions for those failing. Language acquisition is sometimes a condition to get a residence permit, family reunion or citizenship. A reasonable number of countries have language regulations, but not all invest in official language courses. Nonetheless, an increasing number of countries implement language training programs to ease the labor market integration of immigrants (Causa and Jean, 2007).

According to Chiswick and Miller (1995), language fluency among immigrants can be expressed as a function of three variables: Economic incentives, exposure and efficiency. Economic incentives for language acquisition are increasing in the market wage rate, the rate of employment and the duration of stay, while it is decreasing in consumption costs, including search costs, related with a higher level of fluency. Learning of the host-country language would, ceteris paribus, be lower for immigrant groups with a high level of return migration.
Exposure refers to a person’s utilization and exposure through for example the media to the host-country language both prior to immigration and at the destination. It is positively related to marriage to a native spouse, duration of stay, short ‘language distance’\textsuperscript{12} and formal instruction in host-country language. Further on, exposure is negatively correlated with residential segregation. Policies that stress formal language instruction may be of great importance to labor market participation.

Efficiency relates to the degree in which host-country language exposure generates language fluency. For instance, the young may have a more impressive efficiency to require language skills than the old. Efficiency in language acquisition may be reinforced by education, possible due to the fact that people with education are better in acquiring new terminologies and concepts. Another explanation is that people with education have learned languages in the educating process. Besides, it can also be that language acquisition is a requirement for enrollment in higher education. Refugees may have lower language efficiency because they are less positively self-selected, so that economic performance is less likely to be due to socioeconomic factors\textsuperscript{13}.

Chiswick and Miller (1995) summarize the implications in the following equation:

\[ LANG = f \{ \text{expected wage increment for language fluency } (+), \text{ expected future duration } (+), \text{ duration in destination } (+), \text{ married to native of destination } (?), \text{ married to native of origin } (-), \text{ children } (?), \text{ minority language concentration } (-), \text{ destination language instruction } (+), \text{ linguistic distance } (-), \text{ age at migration } (-), \text{ education } (+), \text{ refugee status } (-) \} \textsuperscript{14} \]

Dustmann (1994) finds that immigrants’ language acquisition in Germany is positively influenced by duration of stay and marriage to a native, while there are negative effects of old age at migration. Further on, the results imply that language proficiency is a significant determinant of immigrant workers’ earnings in Germany. The advantage, however, is not big enough to close the gap in immigrant-native earnings (ibid.).

\textsuperscript{12} Exposure to the host-country language prior to immigration is greater the more similar the two languages in host-country and country of origin are.
\textsuperscript{13} Chiswick argues in several studies that immigrants are positively self-selected from the country of birth, because immigrants can cover the fixed costs associated with migrating.
\textsuperscript{14} Sign of partial derivatives are given in parenthesis.
Chiswick and Miller (1995) use data for Australia in the years 1981 and 1986 to test the importance of language fluency on earnings. They find that English-language fluency is associated with significantly higher earnings. For 1986, the partial effect of English-language fluency on earnings was 8.3 percent. This shows that language acquisition is in deed rewarded in the labor market.

For the UK, Dustmann and Fabbri (2003) report that language has a strong and positive effects on employment probabilities. Furthermore, lack of English fluency leads to substantial earnings losses of immigrants. English fluency contributes considerably to reducing the differences in the income gaps between natives and immigrants.

However, results for Norway show that language acquisition has no effect on immigrants’ earnings (Hayfron, 2001). An explanation may be that Norwegian language proficiency is required to get work. When employed, Norwegian language proficiency may not affect immigrants’ earnings (ibid.).

There have been few empirical evaluations of language training programs. Nevertheless, the results indicate that language training has a positive effect on labor market outcomes, especially short time after arrival in the host country. The positive effects seem to be reduced with duration of stay (ibid.). Still, there might be a trade-off in offering language training, because such programs keep immigrants out of the labor market. Immigrants will then lack early labor market experience, which is important for employment possibilities (Jean et al., 2007). Moreover, language proficiency may be of greater importance for immigrants’ labor market participation in countries with an inflexible labor market. Such inflexibility makes it, ceteris paribus, more difficult to enter.

At last, it is worth noting that immigrants may have an advantage entering the labor market in English-speaking countries, since English is spoken in the media and taught in schools all over the world. This may contribute to explain why Anglo-Saxon states have higher immigrant employment than social democratic states.
4.2 Immigrant Ties

Contact between immigrants from an ethnic group, through social networks and ethnic residential segregation, is important in determining employment outcomes. Immigrants with a strong ethnic identity may be discriminated by employers, and they may therefore have a disadvantage on the labor market. Furthermore, ethnic social networks supply information about the welfare system and job vacancies. These networks are thus important to the job search. At last, when an ethnic group resides the same area, benefits to production may arise, when the number of immigrants exceeds a critical mass.

4.2.1 Ethnic Identity

Ethnic identity is the degree to which individuals of a particular ethnic group associate themselves with their ethnic background or culture (Bisin et al., 2009). Strong ethnic identity can result in adverse labor market outcomes when the minority culture and the mainstream culture are opposing (ibid.). Strong ethnic identity that leads to opposing cultures can be influenced by education in country of origin, old age when immigrating, short time spent in host-country, poor language acquisition, residential segregation and exposure to ethnical attacks (reviewed by Bisin et al., 2009).

When controlling for gender, age, education, years since arrival and country dummies, Bisin et al. find that immigrants with a strong ethnic identity have 3 to 5 percent lesser chance of finding work in the host-country than immigrants with weak ethnic identity. This penalty is larger for immigrants than for natives with the same characteristics. The results change only slightly with and without country dummies, implying that the connection between labor market participation and ethnic identity is not different within Europe. However, the penalty of ethnic identity may vary according to labor market policies applied in different countries.

4.2.2 Network Effects

How social ethnic networks influence immigrant integration has been widely discussed in the social sciences. Social networks can affect choices made by immigrants, when ethnic communities pass on information about welfare benefits and the labor market. The networks can assist immigrants’ labor market positions by providing information about jobs and thereby improve immigrants’ capacities to worker-to-job matching. However, if networks are
excluded from the rest of the society, they can be a disadvantage to the labor market position and increase the use of welfare benefit programs. Furthermore, attitudes towards welfare benefits in the ethnic network are important in determining stigmas related to such benefits.

Formally, let $U$ be the utility of consumption, $w$ is the wage, $b$ is the replacement rate and $t$ is the tax rate. $\alpha$ is the difference between utility from spare time and the intrinsic utility from working. $f(n)$ is the disutility or stigma from receiving welfare benefits. The stigma is increasing in number of people, $n$, not receiving welfare assistance (i.e. $f'(n) > 0$).

Immigrants will choose to work as long as

$$ (4.1) \quad U[w(1-t)] > U(bw) + \alpha - f(n) $$

When many people from the same ethnic group receive benefits, the stigma is reduced, and the utility of not working increases. If an immigrant decides to rely on welfare rather than working, this may transmit to others in the network as well. Attitudes in ethnic networks are thus important when the choice of working or receiving welfare is made.

The importance of social networks is stressed by Borjas and Hilton (1996). Their findings from the US suggest that the types of welfare benefits received by earlier immigrant waves affect the type of benefits received by newly arrived immigrants. The corresponding correlation suggests that there might be information networks operating within an ethnic community. These networks supply the community with information on the availability of welfare benefits. Borjas and Hilton use panel data drawn from the American Survey of Income and Program Participation to examine the trends in immigrant’s participation in welfare programs.

According to Borjas and Hilton immigrant households are more likely to receive welfare benefits than native households. The findings suggest that the welfare gap between natives and immigrants increased during the 1990s, and that it is only to some extent explained by socioeconomic characteristics of the populations. Recent cohorts and immigrants with a long duration of stay in the US are more likely to be on welfare.

The authors find that some ethnic groups receive different types of welfare benefits. They argue that this can have its origin in network effects, when ethnic communities transmit

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15 The equation is obtained from Lindbeck (2006).
information about welfare programs to other immigrants. Borjas and Hilton test this hypothesis by investigating whether or not newly arrived immigrants’ use of welfare benefits depends on the history of the ethnic group’s participation in welfare programs. They estimate the following regression model using OLS:

\[
q_{ij} = X_{ij} \beta + \alpha_1 p_j + \alpha_2 \bar{p}_j + \alpha_3 \bar{q}_s + \epsilon_{ij}
\]

where \(q_{ij}\) is the fraction of time household \(i\) from group \(j\) in state \(s\) uses in the same program, and \(p_j\) is a particular program the ethnic group \(j\) is participating in. Further, \(\bar{p}_j\) is the probability of the immigrant group receiving benefits, while \(\bar{q}_s\) is the participation rate of natives in state \(s\). \(X_{ij}\) is a vector of a list of household characteristics.\(^{16}\) Thus, they have a measure of state generosity (\(\bar{q}_s\)), demographic background (\(X_{ij}\)) and propensity of welfare program participation for one group (\(\bar{p}_j\)), along with the probability of new immigrants participating in a program, which the ethnic group has already been exposed to.

The results suggest that \(\alpha_1\) is significantly positive, \(\alpha_2\) smaller and sometimes zero, while \(\alpha_3\) is positive for only two programs, when the characteristics are controlled for. This implies that the more a group has been participating in a particular program in the past, the more likely it is that new immigrants from this group will participate in this program.

The strong relationship between former immigrant wave’s participation in a particular welfare program and newly arrived immigrants’ propensity to participate in the same program, suggests that there are network effects operating to spread information about these welfare programs. However, Borjas and Hilton point out that this correlation can be due to other factors that determine immigrants’ access to welfare programs. The results may thus suffer from omitted variable bias.

Hao and Kawano (2001) emphasize the importance of networks within the immigrant community in immigrants’ economic success, and that immigrant use of benefits depends on both social and human capital. When immigrants invest in language proficiency, education and work experience, they will earn higher wages and have better occupational choice. Not investing in human capital can on the other hand lead to welfare dependency. Further,

\(^{16}\) The standardized characteristics include household income and composition, rural/urban area and socioeconomic background.
information on labor markets is important for families to be self-sufficient. The authors examine the relationship between immigrants’ use of two welfare programs and ethnic networks in the US by looking at two subgroups; single-mother households and elderly units.

The findings indicate that a concentration of low-income ethnic immigrants do not rise single-mother families’ use of Aid to Families with Dependent Children, though greater country of origin contact increases elderly immigrants’ use of Supplemental Security Income. This is of greater importance to elderly immigrants, who have stayed in the US for a substantial amount of time and built up the required work experience to qualify for the program. Hao and Kawano argue that networks support elderly immigrants’ welfare use by reducing the stigma associated with such benefits. Moreover, they find that decisions to receive welfare benefits are made at the time of migration, meaning that networks spread information from the country of residence to potential immigrants in the home country.

On the other hand, Bisin et al. (2010) find indications that networks, measured by family reunion policies, are important in finding a job, but that this effect diminishes with the strength of ethnic identity.

In general, networks are important for immigrants’ job search efficiency, because immigrants have less knowledge of the labor market. Often, networks, such as family and friends, are operating to identify potential candidates for a job. Immigrants’ lack of networks may result in limited access to the labor market (Liebig, 2009). On this note, the findings in this section stress the importance of information on labor markets, rather than on welfare benefits, to influence single-mother families’ participation in the welfare program.
4.3 Segregation and Economic Performance

Segregation has been widely debated with regard to immigrant integration. Some claim that residential ethnic segregation gives low labor market participation and large immigrant-native income gaps, while others emphasize the importance of ethnic segregation on immigrants’ abilities for self-sufficiency.

4.3.1 The Case of Somali Immigrants in Minneapolis

The Swedish economic historian, Benny Carlson, has studied Somali immigrants in Minneapolis, Minnesota. In his book, Somalier I Minneapolis- en dynamisk affär (2006), (loosely translated: Somalis in Minneapolis-a Dynamic Case), he tries to answer why Somali immigrants living in an enclave in Minneapolis have significantly higher labor market participation rates than Somali immigrants in Sweden. Carlson mainly applies qualitative methods, covering questioners and interviews, to explore integration outcomes in Minneapolis.

Following the civil war in Somalia in 1991, a large wave of refugees hit Europe and North America. Minneapolis is the city with the largest concentration of Somali immigrants in the United States. There are several explanations to why Somali immigrants have chosen to settle down in Minneapolis. Good possibilities for employment in the pharmaceutical industry during the 1990s, well known educational systems, tolerant native population, easy access to the housing market and a large existing community of Somali immigrants are some of the reasons mentioned (Carlson 2006).

Minneapolis is located in Hennepin County in Minnesota. Minnesota has one of the highest employment rates and one of the lowest unemployment rates in the US. Hennepin County has even better figures than the average of Minnesota. In 2000, the US employment rate was 0.61, while it was 0.7 in Minnesota and 0.72 in Hennepin. Furthermore, the unemployment rate was 0.52 on average in the US, while it was only 0.36 in Minnesota and 0.33 in Hennepin.

In Minnesota, 5 percent of the population is born outside the US, while the number is 10 percent in Hennepin. This pattern is nearly opposite of that in Scandinavia; an area with a large number of immigrants has high employment and low unemployment. Among the Somali immigrant population, 47 percent were employed in Minnesota in 2000, against only
23 percent in Sweden in 2003. Nonetheless, in 2000, 59 percent of Somali immigrants in Minnesota had an income below the poverty line. As a benchmark, for the total American population the number was 12 percent. The Somalis in Minneapolis are in other words not a wealthy group.

The language acquisition among the Somali immigrants in Minneapolis is better than other comparable immigrant groups in the ‘Twin Cities’ (Minneapolis and Saint Paul). Some Somali immigrants learned English while they stayed in refugee camps in Kenya, while others acquired it by attending classes in the US. During the 1990s, low unemployment and high demand for labor resulted in low language requirements. Hence, immigrants could easily get access to the labor market (ibid.).

The Somalis in Minneapolis have several community centers, which supply job training and social services supported by the government and other organizations. Social activities are in a large scale managed by the immigrants themselves. In contrast to the Scandinavian countries, the Somali immigrants in Minnesota have their own private schools and local TV shows that spread information. In Minnesota, Somali immigrants are mainly employed in the industry sector, transporting sector and the service sector, while Somali immigrants in Sweden are more commonly employed in health care (ibid.).

In the US, employment counseling aims at removing obstacles between the employer and the job seeker to improve the job search. Human beings are expected to work. Therefore, the main task at the work centers is to remove obstacles for persons who have not been able to get a job. The most common obstacles, reported by a Minneapolis work center, are lacking education, women lacking work experience, reluctance to ‘step down’ from a high-status job in the native country to a low-status job in the host-country, Muslim outfits, poor mental health, lacking language acquisition, reluctance to leave children at day care and issues concerning hygiene. In addition, former convicts can have problems entering the labor market, as well as lack of money for transporting and clothes can be a problem. Some of these obstacles can be resolved by money support from government and non-profit organizations. Conversely, the problems that cannot be resolved, may lead the unemployed immigrants to self-employment (ibid.).

The Somali group in Minneapolis is interesting, because it draws a picture of the results of multicultural policy, combined with less generous welfare benefits and more segregation
compared to Scandinavia. (It is important to be aware of, though, that since the Somali’s are refugees, they can rely on support from the government in a larger scale than other immigrant groups in the US.) The result is a high degree of labor market participation compared to Scandinavian countries, but low income levels.

The high degree of labor market participation can have its origin in the heated economy in the US during the 1990s, which made it easy to obtain work. This was quite another labor market situation than the Somali immigrants in Scandinavia were faced with when they arrived during one of the worst economic recessions of the century (ibid.). These differences may have been preserved because of the relative generosity for long-term unemployed in the Swedish welfare system (Cahuc and Zylberberg, 2004:643). Moreover, the Somalis are a relatively new immigrant group, and this may therefore be a factor contributing to low income levels in the US. Whether these income differences will even out in the long run is yet to see. According to Carlson (2006), the Somali immigrants in Minneapolis are a group in dynamic development.

4.3.2 Ethnic Enclaves

So what are the mechanisms operating in the Somali community? There are approximately 25,000 Somali immigrants in Minnesota, with the majority living in Minneapolis (ibid.). The Somali immigrants in Minneapolis are ethnic enclaves. The enclaves function as magnets attracting people with the same characteristics as the pioneers. The ‘pull’ factors are economic and social support, and the liberty to presume what is important to the individual (immigrant) in question, such as religion and family and clan ties. The enclave economy is brought to life when four conditions are fulfilled. First, capital must exist or be accumulated in the enclave. Second, some members of the enclave have to be acquainted with accounting and finance. Third, some in the work force must be willing to work longer hours at lower wages, than outside the enclave. At last, local shop owners and employers have to rely on workers with the same ethnic background to handle the production (ibid.). Abrahamson (2001), as described in Carlson (2006), argues that enclaves are of special importance to refugees, which are also the immigrant group with the largest receiving social support. He emphasizes the importance of the beneficial economic opportunities and political power in the enclaves, as well as control of living conditions and empowerment.
Light and Gold (2000), as referred to in Carlson (2006), point out that enclaves contribute to a number of disadvantages. Besides low wages, long hours and poor conditions, life in the enclaves can result in reduced language acquisition, lacking labor unions and thereby bargaining power, as well as ‘cannibalistic competition’ when the members compete with each other within the same business. Enclaves affect immigrants’ labor market participation through several channels. On the positive side, the enclaves have positive network effects. The networks increase possibilities for labor market transactions and help spread information about available jobs. Furthermore, they reduce the risk of discrimination in the labor market. The enclaves can moreover be important to create a critical mass necessary to support ethnic enterprises (Waldfogel, 2003, as described in Cutler et al., 2008). In general, the benefits associated with enclaves can be thought of as reducing costs of assimilation to the host country, essentially by making this process less necessary for economic success (Cutler et al., 2008).

On the negative side, the enclaves can decrease the rate of host country skill acquisition. Furthermore, immigrants can experience discrimination in the labor market. Besides, they may not have other choices than to settle down in the enclaves, even if the enclaves are located far from the work place. This phenomenon is known as ‘spatial mismatch’, which is discussed in the literature as a possible mechanism linking racial segregation to poor labor marked outcomes for African-Americans in the US. While the enclave can have positive effects on labor market participation outcomes in the short run, through positive network effects, the difficulties to expand beyond these networks can be costly in the long run (Cutler et. al, 2008). Whether or not the enclave is a good place to live concerning labor market participation and economic performance, depend on the level of human capital externalities, i.e. the level of human capital in the enclave (Carlson, 2006).

The empirical results of residential segregation on economic performance support the theories above. Hence, they do not point in one direction. Economic performance depends on the characteristics of people living in the enclave. Cutler et al. (2008) find that segregation tends to have more positive effects for groups with higher levels of average human capital. This may indicate that ethnic low-skilled groups, like for instance Mexican immigrants in the US, suffer from residential segregation. Furthermore, they find differences between the estimated impact of segregation and the impact of neighborhood concentration. In some cases, the average effect of segregation on outcomes is positive, while the effect of neighborhood
concentration is negative. These results can imply that residence near, but not in, an enclave can have a positive impact on economic performance (Cutler et al. 2008).

So how is the welfare state connected to residential segregation? One the one hand, a compressed income distribution in a country would make immigrants less marginalized in the housing market, and thus segregation should be lower. On the other hand, however, in these countries welfare benefits may make immigrants less active in the housing market. Koopmans (2010) argues that integration policies are most relevant with regard to segregation. Welfare states with multiculturalist integration policies have more segregation than countries that have stressed assimilation. Belgium, Sweden, the Netherlands and the UK have high levels of ethnic residential segregation compared to France, Germany and Switzerland. Nonetheless, this may be due to the composition and number of immigrants. Muslim immigrants live more segregated than others, so countries with a large Muslim population may experience more segregation.

### 4.4 Self-employment

Non-Western immigrants are overrepresented among the self-employed compared to other employed, and self-employed immigrants tend to have lower incomes compared to salary employed. The immigrant self-employment sector is an important source of income for newly arrived immigrants (Yuengert, 1995). However, self-employment may be an option to the marginalization on the labor market, and low-paid self-employment may uphold income inequalities between immigrants and natives (Liebig, 2009). The circumstances concerning immigrants’ decision to become self-employed may differ from that of natives, as self-employment may be an option to unemployment. This may in turn cause immigrants to be treated differently by public institutions, financial institutions and consumers, when establishing themselves as self-employed (Andersson and Wadensjö, 2004).

Unproportionally high rates of self-employment among Non-Western immigrants are common in the Western world. Yet, there are differences between countries, with the Scandinavian countries having relatively high rates. In Norway, for instance, an unproportional amount of immigrants are self-employed. Immigrants from Non-Western countries amount to 6 percent of the population, while there are 2 percent Western immigrants. The immigrant population owns 8 percent of Norwegian enterprises. Among these owners, 4.7 percent were from Non-
Western countries. Primarily, the ownership involves taxi driving and managing salad bars, hot dog stands and fast food restaurants (Statistics Norway\textsuperscript{17}).

Immigrants’ propensity to become self-employed is in the literature explained by tradition, the labor market situation, tax avoidance and by enclave effects. Also, foreign-born may have a more risk-seeking behavior than natives. In accordance with traditions, immigrants from certain countries with high rates of self-employment may be more likely to start their own businesses. Weak labor market positions among immigrants may result in self-employment, since the reservation income will be lower for this group. Self-employment can therefore arise as an option for those who wish to be economically independent and avoid being dependent on benefits and have difficulties in finding a regular job (Andersson and Wadensjö, 2004). This reflects the labor market situation. Moreover, incentives for tax avoidance can lead to self-employment with its greater opportunities for deductions. In the US, immigrants tend to be concentrated in high-tax states, and may therefore have higher self-employment rates (Yuengert, 1995). Further on, enclave effects can lead to opportunities for self-employment when immigrants have a comparative advantage in serving the needs of the consumers of a national group, compared to the rest of the population. The comparative advantage arises when immigrants have better knowledge of immigrant preferences and language spoken by people in the enclave (Borjas, 1986).

The empirical findings of reasons for self-employment are mixed. Borjas (1986) finds that more immigrants than natives in the US are self-employed, and that this result can be attributed to enclave effects. He reports that Hispanic immigrants are more likely to be self-employed in cities with large concentrations of Hispanic immigrants. Borjas further reports that the impact of assimilation on self-employment rates is positive. Conversely, Yuenger (1995) reject the hypothesis of enclaves leading to higher rates of self-employment, though he finds effects of enclaves on sectoral earnings. Instead, he finds support for the hypothesis of immigrants from countries with larger self-employed sectors having high self-employment rates in the host country. This indicates that decisions of becoming self-employed are affected by tradition, and it has little to do with settlement. Tax avoidance is also a hypothesis supported by the data. In the US, immigrants face higher taxes than natives on average, and this may contribute to higher self-employment with possibilities for illegal and legal tax avoidance (ibid.).

\textsuperscript{17}http://www.ssb.no/vis/emner/10/01/ner/arkiv/art-2006-06-16-01.htm
Kanas et al. (2009) find that educated immigrants in the Netherlands are less likely to be self-employed than salary employed, when job-skill level is taken into account. The probability of self-employment is declining in country of origin work experience. Moreover, Lofstrom (2000) reports that educated immigrants in the US are less likely than educated natives to become self-employed. These results may imply that self-employment is an alternative to unemployment.

The income levels of self-employed immigrants are generally lower than for natives. This may be due to the fact that immigrants have lower reservation wages, making low-paid self-employment a more attractive option to immigrants than for natives. Further on, immigrants may tend to have access to certain sectors of the economy that do not require education and large start-up costs. Still, a large degree of competition can lead to ‘cannibalistic competition’, when immigrants are employed in the same sector, making incomes lower.

Generally, it could be that immigrants are discriminated by consumers and financial and government institutions. Consumer discrimination can arise when consumers avoid shops and businesses run by immigrants. Financial discrimination can occur when immigrants are not able to get the same financial capital as native self-employed, while government discrimination can arise when immigrants cannot attain the same rights as natives to start businesses (Andersson and Wadensjö, 2004). Blanchflower et al. (2004) find evidence that minority-owned firms are discriminated against in the market for credit in the US. They argue that this is due to credit market failure, because commercial banks in the US appear to be the major cause of credit constraints facing minorities.

Yet another explanation of low earnings among self-employed immigrants, as pointed out by Andersson and Wadensjö (2004), is related to the way the business is organized and incentives for reporting income. Immigrant businesses are commonly organized in a way that makes households work together. If social assistance benefits are attached to the individual, rather than to the household, there will exist incentives to spread the income among family members as oppose to the self-employed reporting the income. This tendency will typically be strong for countries with a progressive tax system.

Andersson and Wadensjö compare Sweden and Denmark, and find that incomes among self-employed relative to wage earners are higher in Denmark than in Sweden. This may be due to the fact that in Denmark, welfare benefits are attached to the household, in contrast to Sweden
where benefits are related to the individual. Andersson and Wadensjö argue that even though incomes are low for self-employed immigrants in Denmark and Sweden, incomes are often supplemented by welfare benefits in the start-up period. The reason is that unemployed people, or individuals who face the threat of becoming unemployed, are entitled to financial support to start a business. The financial support includes unemployment benefits for a period, even if a person is self-employed (Andersson and Wadensjö, 2004).

Besides for Scandinavia\textsuperscript{18}, financial support aiming to assist unemployed with starting up a business exists also in some of the US states and in most of the European continental countries as well as in the UK. Figures for 2003, confirm that Germany by far is the country with greatest start-up benefits to unemployed, while UK and Belgium have the lowest (Wandner, 2008). Compared to Germany, all the other countries, including the US, have relative low start-up benefits. Further on, findings from 17 OECD-countries suggest that that the relationship between self-employment assistance programs and self-employment rates is positive, and that it is a negative relationship between unemployment insurance and self-employment. However, the literature supplying evaluations of self-employment support programs on immigrant labor market participation is scarce. It is therefore difficult to say something about the effect of such programs on immigrants’ employment possibilities.

Yet, there are indications that non-Western immigrants receive less state financial support when starting a business. For instance, OECD (2010) reports that non-Western immigrants in France receive aid less often than their native counterparts. Moreover, the same report points to the fact that new businesses run by non-Western immigrants are more vulnerable, than those run by natives. Immigrant firms that perform well are those with a large local client base, while those in the construction sector perform poorly compared to native firms. Hence, information about government programs for self-employed may be important for financial support to self-employed immigrants.

We can conclude that incentives induced by the welfare state in terms of reporting of income and public policies may affect immigrant integration and explain differences in integration outcomes across countries. The self-employment sector is important to understand how immigrants can enter the labor market. Given the lack of evaluations of the effects of self-

\textsuperscript{18} Start-up benefits exist in Norway, but are of small importance (Wandner, 2008).
employment support on integration, it would be important that further studies address this issue to ease the road to self-employment and higher incomes for immigrants.
5 Summary and Conclusion

Lower labor market participation and greater extent of welfare dependency among non-Western immigrants, compared to comparable natives, is common in Western welfare states. A first glance at immigrant-native employment gaps, suggests that the Central-European and Anglo-Saxon countries generally have smaller gaps than Sweden, Denmark and the Netherlands. The motivating question of this thesis was why integration outcomes vary across welfare states, and how the welfare state affects integration outcomes. The answer is complex. Based on a survey of the literature I have identified what I consider a tentative pattern. I have not been able to really confirm the pattern by my own empirical investigations. Yet, I find the pattern of some interest:

The welfare state affects immigrant integration through several channels. Before the time of immigration, the generosity of the welfare state may influence potential immigrants’ decision of where to migrate. When all other factors are held constant, countries with generous welfare benefits, such as the Scandinavian countries and the Netherlands, may experience negative self-selection in the sense that low-skilled immigrants choose to migrate to these countries. Countries with less generous welfare systems, such as the US and UK may attract high-skilled immigrants. However, this welfare magnet effect is marginal. More important are immigration restrictions and wages in the host-country when choice of destination is made. Networks and immigration policies are influential in the selection process of immigrants as well. Countries with restrictive policies, e.g. Switzerland, have a relatively ‘good’ selection of immigrants. Finally, welfare policies are endogenous. The Scandinavian countries admit a bigger proportion of asylum seekers than other countries, and this in turn affect the need for support from the state.

After the time of immigration, incentives in the welfare benefit system affect immigrants’ choice to invest in human capital and the choice to participate in the labor force. For instance, if welfare benefits are attached to work history, the incentives to participate in the work force are higher than if rights to such benefits are given independently of work experience. On the other hand, generous welfare benefits make it possible for immigrants to restructure and invest in human capital, which is important for social mobility and integration in the labor market in the long run. However, these benefits must be time constrained to avoid welfare dependency. Attitudes and culture play an important role in immigrants' effort to apply for
jobs as well. Countries that apply a universal welfare model may experience lower immigrant employment than countries with an exclusive or miser welfare state.

Two important aspects of the welfare state with regard to immigrant integration are labor market structure and integration policies. In countries with collective bargaining, such as in the Scandinavian countries, minimum wages are high. This may be a disadvantage to immigrants’ labor market entry. If immigrants are less productive (or perceived to be so) than natives, or low-skilled, this is a disadvantage to immigrants in these countries.

In addition, the degree of labor market protection is of importance to immigrants’ entry in the labor market. Countries with strict regulation tend to have lower immigrant employment than countries with low degrees of regulation, when observable characteristics are controlled for. However, for immigrants with strong ethnic identity, countries with little regulation fail to give enough protection. Thus, labor market protection may be important in reducing discrimination for employed immigrants. Further on, possibilities for temporary contracts may cause immigrants to be permanently marginalized in the labor market. Besides, self-employment can increase the labor participation, although it may contribute to maintain marginalization. Self-employment will typically be the case in enclaves, where the self-employed exploit the advantage of immigrants' labor supply and consumer demand.

Moreover, the size of low-skilled sector in a country is of importance to immigrant employment. Immigrants have easier access to the labor market in countries with a large low-skilled sector, like the Southern European countries. However, employees in the low-skilled sector will generally have more physically demanding jobs and worse working conditions than in high-skilled sector. This may cause active immigrants to exit the labor force after a period of time, especially if the benefit system is generous.

Another aspect of the welfare state is integration policies. The degree to which a country recognizes immigrants’ rights and inclusion in the welfare system differs across welfare states. Countries that are strict on this area, e.g. Austria, Germany and Switzerland, tend to have better labor market participation. However, these countries may have little social mobility and poor wage integration in the long run. Countries with universal welfare models, such as Sweden, Denmark and the Netherlands, have relative low immigrant employment. One reason for this outcome can be that these countries traditionally have applied a multiculturalist approach to integration, by actively supporting ethnic diversity. This may
contribute negatively to immigrants’ labor market integration. In addition, the penalty facing immigrants with a strong ethnic identity is smaller in countries with relatively extensive labor market access policies and restrictive naturalization policies, such as in Norway, Italy and Spain.

To summarize, immigration policies decide characteristics of immigrants admitted to the host-country. Integration policies in turn decide who gets access to welfare benefits, for instance through naturalization. The decision to receive welfare benefits and enter the labor market is influenced by incentives induced by the welfare state, as well as interactions between the welfare state and labor markets, integration policies, networks and business cycles. These findings have some implications for welfare state organization.

Countries that apply the social democratic welfare model (e.g. Scandinavia, the Netherlands and Belgium) may on average experience relative low immigrant employment due to generous welfare benefits and high wages, which increase the supply of immigrants. However, Norway is an exception with relatively restrictive immigration policies and high immigrant employment. Nevertheless, there are some general mechanisms operating in the social democratic welfare model. Employment regulations may hamper the possibilities for labor market entry, although when entered, the ‘insiders’ get high wages. The degree of human capital is important in these countries, because a small low-skilled sector and a large high-skilled sector increase the importance of perfect matching. In addition, a multiculturalist integration policy, combined with generous benefits may be an unfortunate mix for labor market integration. However, inclusion of immigrants in restructuring programs, allow immigrants to learn the language and culture, which is two important specific capitals. Such programs give immigrants more time to search for jobs as well.

The Central-European states (e.g. Germany, France and Austria) have a relatively favorable composition of immigrants. The composition, combined with a relative big secondary labor market, increases the chances of labor market entry. In addition, these corporatist welfare states offer insurance linked to work history. Such circumstances, combined with restrictive integration policies, push immigrants to non-tertiary sectors as well.

The liberal Anglo-Saxon countries (e.g. UK and US) have flexible labor markets, with weak regulation and flexible wages. On the lower part of the occupational ladder, where non-Western immigrants generally are located, wages are likely to be low. Liberal integration
policies may hamper integration, but such policies may also allow immigrants to obtain larger networks and organize production in a way that utilizes demand from other immigrants. In addition, English-speaking countries may have better integration outcomes, due to the fact that English is a world wide language.

One last question to rise is whether or not the welfare state hampers integration. I conclude that the welfare state in general does not hamper successful integration, although parts of the welfare organization may cause challenges that must be met. What needs to be done in order to improve immigrant integration, depend on the source of the problem. It is thus important to understand how the welfare state affects immigrant integration.

Independently of reasons, training programs and job counseling are important to increase level of human capital and help immigrants to enter the labor market. However, the literature evaluating such programs is scarce. In order to obtain a better understanding of these issues, future research should involve evaluation of concrete labor market policies and training programs. Lastly, I want to mention that this thesis has paid little attention to business cycles and discrimination, which are important topics in the integration literature.
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