Submission to the Productivity Commission Inquiry into the Economic Impacts of Migration and Population Growth

Prepared by the New England Centre for Applied Research in Social Science, University of New England, Armidale

Introduction

This submission is concerned primarily with a theme that receives very little attention in the Productivity Commission's Issues Paper of August 2005. That is the question of the regional impacts of, and needs for, immigration. We structure the submission around selected questions flagged in the Issues Paper (IP) and it focuses more on raising issues for further consideration rather than providing hard data and polished analysis. We believe it is important to get the issues correctly specified at the start of the inquiry.

Linkages between migration, population growth, productivity and economic growth (IP 15)

This issue in effect seeks comment on Figure 2 (IP 13), which has several important flaws. At first glance, the diagram creates an impression that immigration is an unalloyed good. In practice, that outcome rests on the qualities of migrants accepted into Australia. If migrants lack technical skills or knowledge, or ability to speak English, then ensuing dilution of human capital might even reduce average level of workforce productivity. Indeed, many of the effects incorporated in Figure 2 may be either negative or positive depending on the nature of the migrants.

Migrants may also have beneficial cultural traits to augment productivity and output: energy and enthusiasm, will to succeed, networking capacity, or fresh ideas and perspectives on products, services and markets. Such traits appear underplayed in the diagram, but we see them as sufficiently different from human capital, with its emphasis on skills, information and knowledge, to warrant separate mention.

The right hand box implies that immigration can lead to increased *consumption of exports*. Does it really mean to say that a larger population might divert some current exports to domestic consumption? The box also does not distinguish between *gross* and *per capita* consumption. While one would expect the former to rise in line with immigration, the latter may fall depending on migrant sources and demographic profiles.

The *other* category in the *other economic effects* box is vague. Does the inquiry have specific issues in mind? Indeed the *interaction effects* box is something of a black hole when it comes to process, with the direction of effects (positive or negative) depending on migrants' personal qualities or abilities.

This said, the major omission from Figure 2 is spatial analysis. It focuses on national aggregates, but there are reasons to suppose that regional growth effects could be quite variable depending on migrant destinations, their skills and other capabilities, their regional multiplier effects, and the incidence of spread and backwash effects created. Such effects are likely to concern rural regions with their more fragile economies compared to metropolitan regions that soak up most immigrants. Some rural regions

have special skill needs that are frequently met by migration. For example, immigrant doctors and nurses play an important role in the provision of rural and regional medical services, which are crucial for retaining population in small towns and ultimately for their economic survival. This underscores the fact that it is often difficult to separate economic and social issues in non-metropolitan Australia. For similar reasons, the Mayor and Council of Young in Central Western NSW made strong representations to DIMIA when the Temporary Protection Visas for Afghan men working in the local Abattoir were about to expire. In addition to performing a useful economic function in the meat industry, they supported other local businesses and made Young a more interesting place in which to live. It even enhanced Young's reputation as an open minded community, which itself may have created beneficial spin-offs[1].

However, Figure 2 could describe a single regional economy, in which case the national picture will be some aggregation, though not necessarily a simple or even weighted one, of the component regional economies.

Regional impacts of population size (and the migration component) on regional productivity and economic growth (IP 15)

Any response to this issue is clouded by the great diversity of regional economies. From a small business perspective, this is demonstrated by Sorensen (2004) who develops a 12 – fold multi-factor classification of regional small business financial performance. We suspect that any given level or skills composition of immigration could have very different regional economic impacts depending on:

1. overall tightness of local labour markets
2. local skills deficits and surpluses – and the extent to which migrants fill the gaps or augment surpluses and therefore impact upon local movements in wages and salaries
3. scale of labour turn-over[2]
4. level of outmigration and out-migrant skills
5. local business profitability (on average and spread around the mean)
6. local economic growth prospects
7. the diversity and robustness of regional production[3]
8. the extent of regional multipliers (output, employment, or wages), which measure local economic interconnectivity
9. strength of local backwards and forwards linkages
10. the scale of local entrepreneurship and risk acceptance
11. local capacity to invent / innovate
12. community economic and social adaptive / absorptive capacities
13. qualities of local society
14. the degree of national integration (as perhaps measured by the relative proportions of regional GDP accounted for by local and state-wide / national business chains)[4]

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1 Professor Stilwell at Sydney University has written on events at Young and their effects on the regional economy.

2 Higher turnovers will increase business costs

3 The difference between diversity and robustness is important. Diversity tends to spread risk everything else being equal. Where diversity is absent (especially in rural economies), robustness and regenerative capacity can also militate against risk.

4 Large national or state-wide companies may be better able to withstand local economic contractions resulting from, say, drought or low commodity prices because of their ability to cross-subsidise branches.

15. industry structure and proportions of employment in growth or declining sectors as indicated, say, by shift-share analysis
16. industry structure in terms of short- and long-term riskiness / instability
17. industry structure in terms of integration with, and susceptibility to changes in, the global economy
18. quality of local infrastructure both now and in the context of likely development trends in the local economy
19. quality of local / state government services and scales of charges
20. the level of mutual support among local businesses
21. availability and cost (broadly construed[5]) of risk / venture capital
22. the seasonality of rural employment

This list of 23 items may not be exhaustive but it gives some idea of the range of factors that might affect local attractiveness to the migrant, the capacity of businesses to trade profitably, changes in business productivity and relative levels of productivity among a set of regions.

Given substantial inter-regional variations on many of these dimensions, one would expect, *a priori*, a large range of productivity and economic growth effects, both negative and positive from any given level and quality of immigration. We do not think it possible to forecast outcomes with any degree of accuracy. Effects will also vary with the following regional transects:

- regional town vs rural vs remote vs peri-metropolitan;
- coast vs inland;
- tropical vs subtropical vs temperate regions;
- bio-physical regional characteristics;
- regional livability; and
- state jurisdiction under competitive federalism[6].

In addition, the productivity and growth effects, may be time specific. Some will cut in quickly and some slowly; some may be positive in the short-term but turn negative in the longer-term (or vice versa); some may follow business or commodity price cycles. Productivity effects might also be different according to labour market segment. At the highly skilled end, Australia functions more as a single market than for low skilled workers where effects are state based of perhaps even regional. So, population growth may influence productivity growth more for skilled workers than for the unskilled.

Does population growth affect productivity growth? (IP 16)

Well, it can, but the rate up or down is affected by the all the above considerations and a few more besides, such as:

- demographic history – the degree of stability in, and composition of, population growth;
- economic history – stages in a nation's or region's economic development[7];

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5 Including cost (interest rates), freedom of action for the entrepreneur, and penalties for default.

6 The productivity commission has drawn attention to the incidence and effects of inter-state bidding wars for infrastructure, businesses, and events.

7 Recent classic cases of national reversals in economic form: slumps occurred in Japan post 1991; and Germany post reunification (1989); national revitalisations were posted in Thatcher's Britain (post c. 1980); in Reagan's and Clinton's US (post 1980); and in Australia and NZ from the mid-1080s onwards.

- stage in long wave evolution[8]
- quality of macro-economic management which, like long waves, may influence productivity and economic growth independent of demographic change. Good business climates, with low and stable interest rates and strong demand, may well stimulate the investment necessary to raise labour productivity
- degree of market orientation: the removal of subsidies and exposure of industries to competition can raise productivity also as happened increasingly in 1990s agriculture. The sector's good productivity performance in that era reflected partially its increasing competition that forced weak producers out of the industry.
- currency movements: a high priced Australian dollar in trade-weighted terms forces efficiencies on businesses that might be unnecessary when they are 'protected' by a low value currency – as occurred consequent of the Asian melt-down in 1997.
- labour market segment: at the highly skilled end, Australia functions more as a single market than for low skilled workers where effects are state based of perhaps even regional. So, population growth may influence productivity growth more for skilled workers than for the unskilled.

We can also argue this issue by analogy. Clearly, the mass flow of Hispanics from Mexico and other parts of Latin America has played a part in sustaining a long boom in the US, in creating strong investment conditions, and in underpinning the US's long-term inventiveness and capacity to innovate. During the last decade, the US has experienced reasonably consistent high productivity and economic growth. Our own economic performance has mirrored US experience with a level of immigration. There appears little reason why Australia cannot emulate the US in this regard.

However, both nations may be susceptible to ecological limits that could constrain – at least in the short-term – the impact of migration on productivity. In rural areas especially, agriculture may be pushing up against production limits in some parts. The Murray-Darling Basin is experiencing worrying environmental deterioration: weak and toxic river flows, salination, damage to wetlands, and soil erosion. These have multiple causes, but over-allocation of scarce water resources is a key ingredient. Restrictions on irrigation could in some areas reduce the gross value (and perhaps volume) of agricultural production. Ecological limitations can show up regional and nationally.

[8] Kondratieff posited occasional spikes in innovation, such as railways, automobiles and so on followed by long periods of digestion. We are currently at the cusp of many major new energy, bio-, electronic and other technologies that are perhaps lifting economic growth above long run averages – irrespective of the underlying demographics. Thus, at some points, population growth will correspond positively with surges in productivity and economic growth; while at others the relationship might be negative. In both instances, there may little causation.