

Welfare effects of Immigration under Policy Coordination

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Non-technical summary

This paper constructs a theoretical model which explains how a developed country designs its immigration policy by setting a skill-specific quota on foreign workers. The methodology developed shows how this policy changes when the sending and receiving countries form a political union. The model provides explicit rationale for the formation of immigration quotas on the level of the country and the union. The key findings are summarized below.

1. The receiving country benefits from immigration because the wages in a non-migrant sector increase more than the wages decline in a migrant sector. The costs of immigration are related to border and immigration control, migrants' access to welfare, public services, education or simply locals' dissatisfaction from having foreigners around. The optimal immigration quota is determined when the benefits of immigration equal the costs.
2. The sending country prefers to have less migrants than the market level because of the negative diaspora effect, whereby "new" migrants decrease the wages of "old" migrants.
3. Since migrants' welfare is cared for in a political union, the union quota equals the market level of emigration when the social costs of immigration are zero.
4. Under certain conditions, the introduction of a binding quota strictly increases the welfare of the sending country thus decreasing the extent of brain drain.

Key words: immigration costs; wage effect; welfare; immigration policy; coordination