

A brief commentary on
“Growing pains: The valuation and cost of human capital”,
by Greg Clydesdale, Department of Management & International
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Preface

I was asked on 21 May by the Ministry of Pacific Island Affairs to peer review the above-mentioned paper. As I was given a very short period of time to perform this review, it was not possible for me to read any of the cited references. I also openly acknowledge that I am not an expert on immigration, nor am I a ‘Labour Economist’. Rather, I am – for want of a better term – a ‘general’ Economist. My comments are offered here constructively, with the intention of increasing the intellectual content of the current debate surrounding some parts of Dr Clydesdale’s paper.^[1]

Given the time constraints, my comments are focussed on the first half of the paper (sections 1 and 2, pp. 1-11), as this seems to me to be the most controversial. The second half (pp. 11-16), though interesting, is less exceptional.

Overall, I found the paper interesting. Clearly, parts of it are provocative, and it has stirred up lots of debate (see footnote 1). To me, though, the paper reads like an early draft, as it is full of typos and stylistic errors. Perhaps the author will fix these and also maybe consider strengthening some of the paper’s content, including the parts commented on below.

Comments

In the Introduction, Clydesdale begins by considering the main theoretical advantages and disadvantages of immigration for a country. He concludes, “The main focus of New Zealand immigration policy has been on attracting human capital.” (For readers unfamiliar with the term, ‘human capital’ refers to the productive characteristics, broadly defined, of human beings. Increases, or ‘investments’, in a country’s ‘stock’ of human capital arise through increases in the education and skills of the population, health improvements, and net migration into the country.)

In addition to potentially increasing a country’s human capital, Clydesdale acknowledges six other potential *economic* advantages of immigration, including technology transfers from overseas and increased economies of scale for domestic producers^[2] arising from larger domestic markets (and see p.2 for the other advantages).^[3] He concludes overall

that the empirical evidence for these advantages, both internationally and for New Zealand in particular, is mixed and not particularly robust. I suspect this is true, although I have not had a chance to review the literature referred to.

It is revealing of the paper's true intentions that the seven positive aspects of immigration are dealt with in a little more than a page. The rest of the paper is concerned with the negative aspects. Related to this, I found the paper's title to be confusing. I appreciate the reference to "Growing pains", but I do not think "The valuation and cost of human capital" is illuminating. Perhaps a better title might be something along the lines of: "The costs of immigration to New Zealand."

In the second section, "The Auckland Economy and Human Capital", Clydesdale claims that "*the* goal of immigration has been to generate economic growth." (p.4, my italics). Is this strictly true? Certainly, *a* goal of immigration has been to generate economic growth. But, logically, I think there are other goals as well – ones that might not necessarily be expected to contribute to economic growth per se. Even if the primary goal of immigration is economic growth, other (i.e. secondary) goals might militate against the achievement of *maximum* economic growth.

I have not had time to read the Immigration Act to discover its stated goals in these respects. But as Clydesdale points out (p.5), 60% of recent New Zealand immigrants came in via the "skilled/business" category, whereas 30% entered under the "family sponsored" (or reunification) category and 10% under the "humanitarian" category. Thus, 40% of immigrants are currently accepted for reasons *other than* their contribution to economic growth per se.

Whether or not this apparent 60:40 split is desirable from the public's point of view is moot. Logically, though, it seems to me that many people would consider accepting many (at least, some) immigrants into New Zealand on "family sponsored" (or reunification) and "humanitarian" grounds to be desirable. Moreover, it is well known that New Zealand has foreign policy responsibilities in the Pacific region. These responsibilities include permitting people from Pacific Islands to come to live in New Zealand. As discussed on page 9, "Islanders from Niue and Tokelau hold New Zealand citizenship, and therefore [have] unrestricted rights of entry." And for immigrants from other Pacific Islands, "the main entry-type used by this group is family reunification. Pacific Nations (*sic*) are the largest source countries under the International/ Humanitarian scheme."

To sum up to this point, it seems to me that one of the central premises throughout Clydesdale's paper – that the only goal of immigration is to generate economic growth – is questionable. Certainly it is *one* goal (maybe even the main goal), but there are others as well. If one accepts there are these other goals (as above), then Clydesdale's subsequent discussion of the purported connection between immigration and the relatively poor economic growth performance of the Auckland region (and, by extension, the New Zealand economy) is less significant. This purported connection is now discussed.

Auckland is the main destination for New Zealand's immigrants, and arguably Auckland's recent economic performance has been less impressive than other New Zealand regions and the rest of country as a whole. If, as discussed above, economic growth were the main goal of immigration, Auckland's poor performance would be puzzling, as "it suggests either economic conditions [in general] are so bad [in Auckland] that they over-shadow the positive effects of immigration, or alternatively, immigration is actually contributing to this poor performance." (p. 4)

Clydesdale acknowledges that, in addition to the number of immigrants Auckland receives, there is a range of other possible determinants of Auckland's economic performance, such as "exchange rate movements", etc. But sadly (though, not surprisingly given the scale of the task and the data requirements), Clydesdale does not perform such a 'growth' study,^[4] nor does he refer to extant studies. It is impossible, therefore, to infer, as Clydesdale seems to, that high immigration to Auckland has caused its poor economic performance. This is not correct. We simply do not know. As acknowledged by Clydesdale, other explanatory factors may be responsible (or not).

Clydesdale goes on to compare the labour market experiences of immigrants who have been in New Zealand for different durations, relative to each other and also locally-born New Zealanders. Based on data from the New Zealand Immigration Service, Table 1 in Clydesdale's report presents detailed earnings information for immigrants classified by duration of time in New Zealand, and also for locally-born New Zealanders. The overall pattern is that the longer a person has lived in New Zealand (including having been born here) the higher his or her income.^[5] The 'newer' the immigrant, the lower his or her income. Also, based on other cited studies, the 'newer' the immigrant the more likely he or she is to be unemployed or not in the labour force, and also the less likely she is an employer or business owner.

Unfortunately, however, the results represented in Table 1, as discussed above, may be spurious as the relationships examined between income and duration of time in New Zealand are essentially bi-variate rather than multi-variate. Other possible determinants of individuals' earnings than their immigration status, age and gender – such as educational qualifications, experience, ethnicity, etc (i.e. the 'standard' explanators of earnings differences from Labour Economics studies) – are likely to be important too, but they are ignored. In other words, the results represented by Table 1 are likely to suffer from missing explanatory variables, so that the effect of immigration status as a determinant of earnings may be over-stated (albeit the qualitative effects may be, a priori, plausible for the reasons Clydesdale discusses).

Clydesdale's objective of presenting the results in Table 1 is also to examine whether or not the New Zealand Immigration Service's points system for selecting "skilled/business" immigrants is working properly: viz., "a logical place to examine the efficiency of a points system to value human capital is the income immigrant's (*sic*) earn in the open market." (p. 5). Clydesdale interprets the results (discussed above) as evidence that "skilled/business" immigrants, on the whole, are less successful in the labour market than locally-born New Zealanders. To me, this qualitative result is believable. I imagine that

the same sort of result is observed in other countries too. Clydesdale provides an interesting discussion of explanations for this phenomenon (see pp. 6-7).

On the other hand, what surprised me was Clydesdale's own apparent surprise at "skilled/business" immigrants having poorer labour market experiences than locally-born New Zealanders. According to Clydesdale (p. 5, my italics):

These immigrants have been given approval under the points system which assesses their human capital. It has determined that these people are "highly skilled migrants who were likely to settle well and make a contribution to New Zealand"^[6]. We could rightly expect an economic performance *better* for these people [immigrants] than the New Zealand average as natives born here are not selected for their human capital.

Of course it's true that "natives born here are not selected for their human capital", but they undeniably have many 'natural' advantages relative to immigrants, such as English language proficiency, social and business networks, understanding of cultural norms, etc. Clydesdale acknowledges all of these natural advantages as being important, as referred to above. To me personally (the son of an immigrant), it is believable that it can take time (maybe even a generation or more) for immigrants to settle into a new country and succeed economically.

Clydesdale also compares the labour force participation rates of nine immigrant groups from different regions of the world (see Table 2). In particular, immigrants from Pacific Island countries have the lowest labour force participation rates. He then surveys the generally poorer experience of people of Pacific Island ethnicity (not just immigrants) on a range of economic and social indicators (see Table 4, plus other indicators discussed on pp. 9-10). He also quotes from a Ministry of Pacific Islands Affairs report (2002, p. 17):^[7]

Economically, Pacific people have always faced considerable difficulties in NZ. Their skills are not always suited to the demands of the New Zealand labour market and they have been over-represented in the unemployment, lower skilled workers and low income earners.

On the basis of this evidence (discussed in Clydesdale's paper), he concludes "the Pacific Islands population is less productive and less likely to contribute to economic growth." Less productive and less likely to contribute to economic growth than who? Other ethnic groups (i.e. on average) presumably. And on the basis of the economic and social indicators discussed (assuming they are accurate).

Given that New Zealand's ethnic groups (on average)^[8] exhibit a range of performances/experiences on the indicators considered, then, by definition, some groups (on average) will be apparently *more* productive and *more* likely to contribute to economic growth, while others will be *less* productive and *less* likely to contribute to economic growth (and some will be in the middle!). At any point in time (e.g. now), these things are true by definition.

But I fail to see why these relative positions must necessarily be the same *in the future*. Why would they not change over time? Specifically, why would the apparent performances/experiences of the Pacific Islands ethnic group not ‘improve’ over time, as has happened (and continues to happen) for other ethnic groups? Clydesdale acknowledges that (p. 10, my italics):

Where Pacific Islanders have similar skills, they *do* appear to catch up over time. However, the skills and education of this group is not improving at a rate that would allow catch-up with the population, and as a whole they run the risk of becoming an underclass.

In my opinion, the evidence presented by Clydesdale in support of the assertion in the second sentence of the quote is inadequate. The only evidence presented (see p. 10)^[9] is a quote from a 2004 OECD report:^[10]

... even the educational and skill levels achieved by their [Pacific Islands people’s] off-spring do not seem sufficient for this group to give the result observed in many OECD countries that second generation immigrants from unskilled backgrounds do much better than their parents.

In my opinion, more evidence than this is needed.

^[1] At the time of writing (25 May) there had been a large amount of media and popular attention directed at the paper. For example, a Google search of “Greg Clydesdale” and “growing pains” produced over 200 hits.

^[2] Strictly speaking this ought to be for domestic producers of *non-traded* goods and services, in contrast to *traded* goods and services.

^[3] Clydesdale and the authors he surveys fail to mention that immigration, by increasing a country’s population, also serves to increase the tax base from which public goods are funded.

^[4] That is, for example, a regression of per capita growth rates on the set of possible determinants, including things such as investment rates, technological change, export performance, etc.

^[5] The exception seems to be for the highest annual income bracket of \$100,000+. A greater proportion of immigrants who had been in New Zealand for less than 2 years were in this bracket than immigrants who had been in the country for longer or locally-born New Zealanders. This likely reflects the substantial “settlement” or “investment funds” some immigrants bring with them and that are a condition of their entry.

^[6] Clydesdale refers to: New Zealand Immigration Service (2003, p. 15; see Clydesdale’s references).

^[7] See Clydesdale’s paper for the reference.

^[8] Of course, averages for any group, by definition, mask individual variations.

^[9] Note too, that in the Conclusion of Clydesdale’s paper, he (belatedly) cites an article by Schnepf (2007).

^[10] See Clydesdale’s paper for the reference.