

# AN ECONOMICS PERSPECTIVE ON CANADIAN IMMIGRATION

Don Drummond and Francis Fong

To judge the successes of the immigration system from an economic perspective, say Don Drummond and Francis Fong of the TD Bank, we need to answer four basic questions: "What are the objectives of the system? Are the objectives being met? If not, why not? And finally, how can the system be improved to more closely align it to the objectives?" They argue that the legitimate test of Canada's immigration system is not whether it maximizes the size of Canada's population or its output, but whether it raises the standard of living. But the evidence suggests that the system has done a poor job at breaking production bottlenecks and facilitating greater output per person. To improve Canada's performance in that regard, they recommend a closer alignment between selection criteria and employers' demands concerning language skills, education and work experience, as well as greater support to help immigrants build a network of Canadian contacts.

Pour mesurer d'un point de vue économique la réussite d'un système d'immigration, affirment Don Drummond et Francis Fong de la Banque TD, il faut répondre à quatre questions fondamentales : « Quels sont les objectifs du système ? A-t-on accompli ces objectifs ? Si non, pourquoi ? Et, comment améliorer le système en vue de les atteindre ? » Pour évaluer l'efficacité du système canadien, poursuivent-ils, le véritable test consiste non pas à déterminer s'il permet d'accroître la population et la productivité du pays mais bien d'améliorer son niveau de vie. Or les données indiquent que notre système d'immigration n'a favorisé ni le désengorgement de la production ni la productivité par habitant. Pour améliorer notre performance à ce chapitre, les auteurs recommandent de mieux aligner les critères de sélection sur les exigences des employeurs en matière de compétences linguistiques, de scolarité et d'expérience de travail, tout en offrant aux immigrants un meilleur soutien en vue de développer un réseau de contacts canadiens.



Immigration can satisfy many objectives. Here we only focus on the economic one. From that perspective, there is significant evidence suggesting that, at least from an economic perspective, Canada's immigration system is not working as well as it should. For the nation's low birth rate and aging demographic, which saps the growth of the domestic labour force, immigration has traditionally been regarded as the panacea. Unfortunately, new immigrants are finding themselves in a difficult position upon arrival in Canada, as good jobs are difficult to obtain, resulting in their falling into low-income status. The problems are often related to language barriers, foreign credentials and work experience not being widely acknowledged. The labour market outcomes of many immigrants are far poorer than those of their Canadian-born counterparts, and each new generation falls increasingly further away.

To judge the successes and shortcomings of the current immigration system from an economic perspective, we pose

four basic, but fundamentally difficult questions. What are the objectives of the system? Are the objectives being met, and if not, why not? Finally, how can the system be improved to more closely align it to the objectives? We believe that an intense research effort organized around these four questions can yield important benefits. Unleashing these benefits will require refinements to the process of selecting new immigrants and more effective processes to facilitate the economic integration of current and past immigrants. Much is at stake in terms of improving not only the well-being of immigrants, but as well the entire Canadian population.

A fairly common but simplistic perspective is that immigration is needed to offset the slowdown in domestic labour force growth caused by the aging of baby boomers, who are expected to retire en masse in the next 10 to 20 years. This implicitly sets one of the system's main objectives as the

maximization of the overall size of Canada, either in terms of population or of output. However, a recent C.D. Howe report by Robin Banerjee and William Robson indicates that net immigration levels would need to be more than 2.5 times larger just to offset the natural decline in labour force growth caused by the aging population.

A slightly more sophisticated ver-

sion of this argument is that immigration is needed to slow the aging of the Canadian population as a whole, thereby dampening the ratio of seniors to the working-age population, or the old age dependency ratio. However, while the median age of immigrants is lower than that of the domestic population, the level of net immigration, again, is simply too small in relation to the existing population to actually lower the overall median age or the dependency ratio.

**But as a small, open economy with access to large external markets, Canada has considerable scope to exploit economies of scale. The country does not necessarily have to depend on a rapidly growing domestic market to build up standards of living. So, similar to the shifting of the dependency ratio and alleviating general skilled labour force shortages, tapping economies of scale is likely not a convincing objective for Canada's immigration program.**

The same C.D. Howe report indicates that even significantly increasing the number of immigrants and skewing the selection aggressively toward younger immigrants made very little difference in their projection of the dependency ratio. With regards to the age structure of the population, Statistics Canada projects that the median age will rise by five years from its current level of 39 years to about 44 years by 2050. In order to halve the rise in the median age, the inflow of immigrants would have to be increased fourfold to 1 million per year. And if Canada is already struggling with the economic integration of the current volume of immigrants, then contemplating even larger numbers makes little sense until the system is improved.

Higher education institutions will play an increasingly important role and will have to adjust to address such skilled labour shortages. In 2006, Human Resources and Social Development Canada released a report indicating that for two-thirds of all new labour demand over the next decade, which combines new jobs with vacancies created by retirees, post-secondary education (PSE) will be required. Many

provincial governments have recognized this and have recently set their sights on providing PSE to a larger percentage of the population. For example, the 2010 Ontario Speech from the Throne set out the goal of increasing PSE attainment rates for the 25-54 age cohort from its present 62 percent to 70 percent by 2020. Hence, given that skilled labour shortages are a widely recognized issue that can be addressed through a number of policy avenues other than immigration, and that HRSDC does not foresee any glaring shortages in the overall labour market, this too is an unlikely candidate to be the primary objective of the immigration system.

It is certainly conceivable that skilled immigrants could raise the living standard of existing Canadians if they removed bottlenecks and facilitated significant output and income gains. We return to this notion, but first it should be noted that fears of large scale skilled worker shortages in Canada are largely overdramatized. Aside from certain conditions, it is unlikely that large, persistent labour shortages can or will exist, because if dissonance is struck between labour supply and labour demand, then prices and related economic conditions will adjust. Real wages would rise, limiting demand and raising supply. There would be a substitution of capital for labour. More labour services would be outsourced overseas, and greater efforts would be made to tap pools of underutilized domestic labour such as existing immigrants, youths, the growing Aboriginal population, older workers and, in certain occupations, women.

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This begs the question of whether it makes sense to set the objective of maximizing the size of Canada's population or its output. Would existing Canadians be better off if the population doubled from 33 million people to 66 million while average incomes remained unchanged? Probably not.

If there were strong economies of scale, then it is conceivable that a larger population could raise per capita incomes. But as a small, open economy with access to large external markets, Canada has considerable scope to exploit economies of scale. The country does not necessarily have to depend on a rapidly growing domestic market to build up standards of living. So, similar to the shifting of the dependency ratio and alleviating general skilled labour force shortages, tapping economies of scale is likely not a convincing objective for Canada's immigration program.

Instead, the immigration policy's objective could be to maximize the well-being of the existing population. From this perspective assessing the immigration system is substantially different, and the question becomes, Does immigration make those already in the country better off? Theoretically, this could be true. Immigrants with skills that are not indigenous to Canada

Yet another perspective is that Canada is going to face a signifi-

could break production bottlenecks and facilitate much greater output per person, thus raising productivity, wages and the standard of living. In addition, immigrants with certain human capital could bring with them connections to their home countries and new markets for Canadian products; this could also generate new employment and income for the domestic population.

With regard to raising Canadian productivity, this is difficult to corroborate with empirical evidence, as the data available are scarce. Canada's immigration policy indeed focuses on evaluating potential newcomers by their skills, such as educational attainment, prior work experience and whether or not the newcomer has an existing job offer. One vantage point could be to observe the achieved levels of earnings by immigrants as an indication that they possess skills that are demanded here in Canada. If immigrants are breaking bottlenecks and opening new market possibilities, then one would think that their marginal value of labour would be quite high. And if immigrants are paid at this marginal value, then their wages would also be reasonably high relative to the existing Canadian workforce. Unfortunately, this could not be farther from the truth.

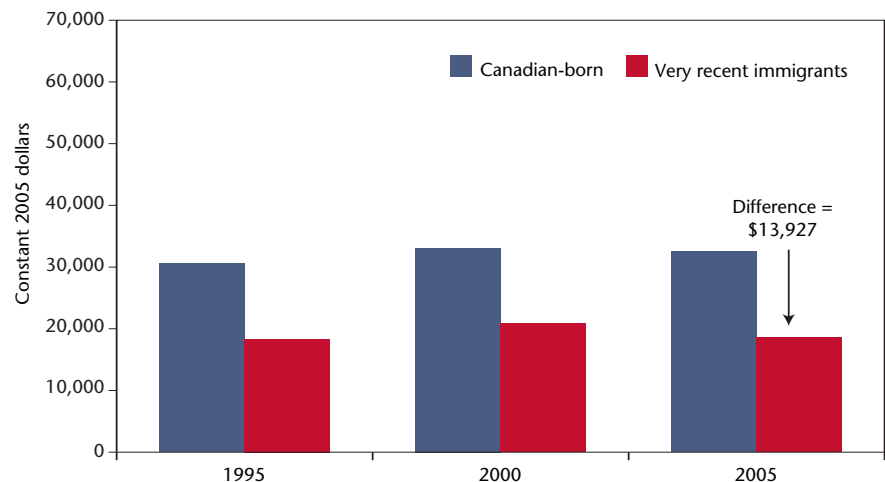
As discussed above, labour market and economic outcomes indicate that there is a large disparity in the earnings of immigrants and their Canadian-born counterparts, despite the fact that a comparatively higher proportion of immigrants have post-secondary degrees. In fact, as shown in figures 1 and 2, the gap in earnings is even larger between those with post-secondary education than between those without. In the past, they could generally hope to close this gap over time, but with each new cohort of immigrants, the level of relative earnings falls increasingly away from that achieved by those born in Canada (see figure 3). As an example, an individual who arrived in Canada in the late 1970s earned, on average, in the first 5 years of his/her arrival, about 85 cents for every dollar earned by a Canadian-born person. This gap has closed to about 98

cents since the beginning of the millennium. Those who arrived at the beginning of the 1990s, however, earned upon their arrival just 59 cents relative to Canadian-born citizens, and even after 15 years they only earned 79 cents for each comparable dollar. In addition, immigrants tend to have higher unemployment rates and lower employment rates, likely reflecting the difficulty that many have in finding gainful employment (see figure 4).

There is a myriad of explanations for the wage discrepancy. For example,

many recent immigrants have their credentials recognized by the immigration system, but not by employers; they also face significant language barriers. Thus, they are either forced to take a compromising position likely unrelated to their original field, or perhaps they are only able to find temporary work where wages are lower. The discrepancy could also be a result of immigrants and potential employers facing a mismatch in labour market information where immigrants are unaware of what Canada's labour market standards are

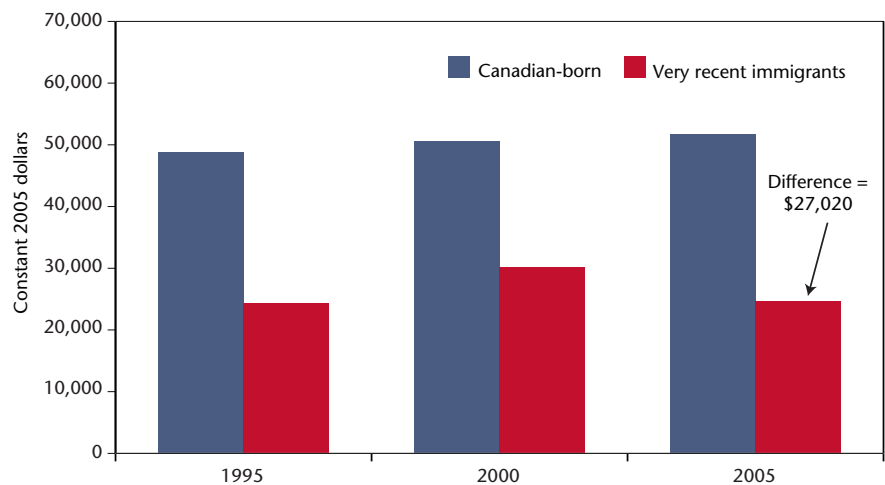
FIGURE 1. REAL MEDIAN EARNINGS OF CANADIAN-BORN WORKERS AND VERY RECENT IMMIGRANT WORKERS<sup>1</sup> WHO DO NOT HAVE A UNIVERSITY DEGREE, 1995, 2000 AND 2005



Source: Statistics Canada.

<sup>1</sup> Full-time, full year workers aged 25 to 54 who arrived in Canada less than five years before the survey date.

FIGURE 2. REAL MEDIAN EARNINGS OF CANADIAN-BORN WORKERS AND VERY RECENT IMMIGRANT WORKERS<sup>1</sup> WHO HAVE A UNIVERSITY DEGREE, 1995, 2000 AND 2005



Source: Statistics Canada.

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and employers face difficulties in evaluating foreign education and work credentials. Certainly these aspects could partly explain the increasing disparity between the incomes of recent immigrants and those of Canadian-born citizens. At the same time there has been a shift in the sources of immigrants away from the United States and Western Europe toward Asian nations, with which Canadian employers are unfamiliar, and where wages are relatively low. Regardless of the explanation, however, the fact that immigrants have such low levels of earnings suggests that they are not being used to their full potential, and this limits the benefits to the standard of living of those already in the country.

The above explanations for why immigrants are being paid less than Canadian-born citizens essentially assume that everyone is paid in accordance to the marginal value of their labour. However, this may not be the case. Perhaps immigrants are contributing more in terms of the value of their labour than suggested by their compensation. Perhaps immigrants are as productive as Canadian-born citizens, but are willing to work for less due to wages in Canada being far higher than those in immigrants' home countries. Perhaps the lower compensation reflects other forms of exploitation. Regardless, these possibilities should also be deeply troubling to Canadians.

Empirical research regarding the second potential boost to productivity that immigration can provide, opening up new markets for Canadian goods and services by bringing connections to businesses and industries and knowledge regarding trade practices in their home countries, is also sparse.

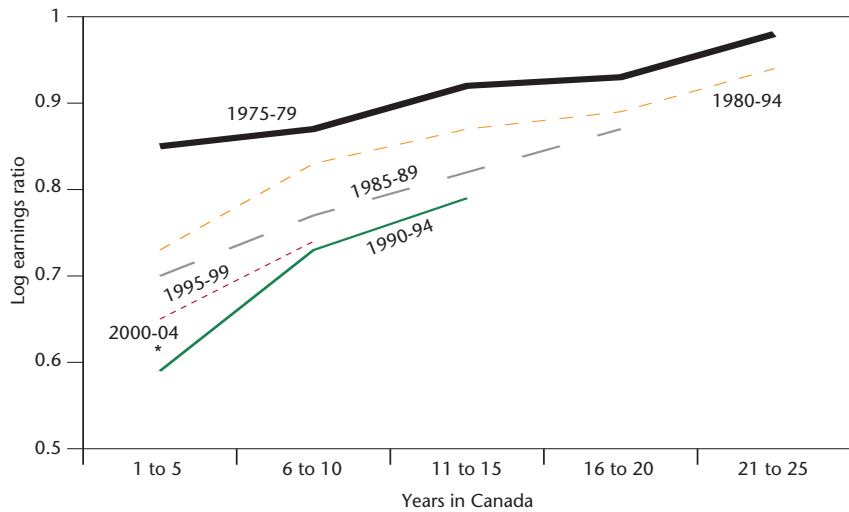
Two economists, Keith Head and John Reis (1998), estimate that a 10 percentage point increase in immigrants leads to a 1 percentage point increase in exports and a 3 percentage point increase in imports. While their results vary widely according to the immigrant's country of origin and the class of immigrant, this provides some

empirical evidence that immigrants do, indeed, bring down nonfinancial trade barriers and increase overall trade flows. However, one has to question whether this improves our standard of living since, given that the size of exports and imports is broadly equivalent in Canada, these figures indicate a net outflow of income rather than a net inflow. In fact, the authors estimate that in 1992 alone, if no new immigrants had entered the country, net

exports would have been \$1.2 billion higher than they actually were.

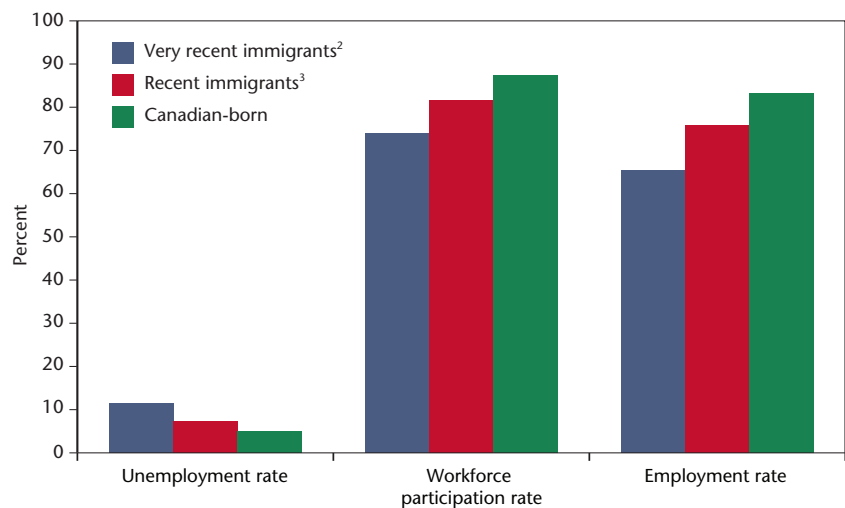
But one should not discount the overall benefit of improved trade relations and an increased level of openness with the countries from which Canada accepts immigrants. There are benefits of developing business and technology networks; for example, those between Waterloo in Ontario and Bangalore in South India, two cities that are burgeoning centres of

FIGURE 3. EARNINGS OF MALE IMMIGRANTS<sup>1</sup> BY NUMBER OF YEARS IN CANADA RELATIVE TO EARNINGS OF CANADIAN-BORN CITIZENS



Source: Statistics Canada, Censuses of population.  
<sup>1</sup> Full-time, full-year workers aged 16-64.

FIGURE 4. SELECTED LABOUR FORCE STATISTICS FOR IMMIGRANTS,<sup>1</sup> BY NUMBER OF YEARS IN CANADA, AND FOR CANADIAN-BORN CITIZENS



Source: Statistics Canada.  
<sup>1</sup> Full-time, full-year workers aged 16-64.  
<sup>2</sup> In Canada for less than five years.  
<sup>3</sup> In Canada for between five and ten years.

technological innovation and from which many immigrants to Canada come. Further, increased imports could bring welfare gains to Canadians through lower costs and higher productivity, such as when modern technology is embedded in imported machinery and equipment. Also, no attempt has been made to establish what the overall benefit will be in the long term, rather than just in a single year.

Hence, it is difficult to establish the impact of immigration on the Canadian population's standard of living. Even at a theoretical level, the issues are complex, and adding an empirical dimension would further complicate the analysis. Nevertheless, there is substantial evidence that immigrants are not integrating well into the Canadian economy, and this challenges the notion of immigration raising the standard of living of the present Canadian population. In-depth research is required to better understand what is really going on. Then that research must be used to modify policy. The modification could affect the target for immigration flows. Under the objective specified here, the test would be not so much whether a certain immigration flow is achieved, but rather how many immigrants and what sort of immigrants can come to Canada under a reasonable proposition that they will raise average Canadian incomes. Experiences of past immigrants can certainly be used to modify the selection and integration processes to maximize the probability of such a test being met.

One of the primary reasons why many recent immigrants are not finding success integrating economically is that they lack the necessary capacity for English and/or French. As briefly addressed above, the source of immigrants has increasingly shifted toward Asian nations, from where almost 60 percent of Canada's immigrants come each year. As such, the share of immigrants whose mother

tongue is neither French nor English has increased from 53 percent in 1981 to 80 percent in 2006. But if many of these individuals are being admitted under the skilled immigrant category and are unable to find proper employment, then it appears that the language test being applied by prospective employers is much more stringent than that being applied by the immigration system.

A number of surveys performed by nonprofit institutions and government agencies have indicated that a larger proportion of immigrants indeed have weaker literacy levels than do Canadian-born citizens, and this has a definitive impact on their ability to penetrate certain occupations and, thus, on their earnings level. Language barriers are also cited by immigrants themselves as the biggest difficulty they face upon arriving in Canada.

However, it is not simply "language" in the traditional sense that is the issue. The ability to read and write, even at an advanced level, provides little indication regarding one's ability to communicate effectively. Soft skills such as being able to explain one's thoughts in a cohesive, succinct and understand-

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able manner, especially in a business setting where language proficiency implies something very different than simply being able to converse with an average person, are integral to becoming an effective part of the workforce. And though the test applied by the immigration system does include an oral aspect, the fact that so many immigrants report language barriers and trouble finding gainful employment as the two biggest challenges upon arriving in Canada is telling that perhaps the system does not

prepare immigrants well enough for them to integrate effectively.

Education and occupational issues are also extremely significant. Many immigrants entering Canada are given a pass by the immigration system, as many have accreditation from institutions in their home countries and relevant work experience. However, once more they run into a wall in the workplace, as employers seem to be particularly picky about an immigrant's field of study, the institution attended, and the type of work experience they have. A post-secondary degree on its own seems to hold little to no value when the institution is not readily known by prospective employers. In addition, work references may be hard to track down or evaluate, since little information is available to Canadian employers regarding work practices in foreign countries.

While the practice of bringing in temporary workers to confront occupational shortages in particular sectors unambiguously helps in both easing bottlenecks and in the economic transition of those workers, those shortages are only likely to be temporary. Hence, if the

immigration system does not react fast enough, then a large disparity could develop between the skills held by incoming workers and the jobs that are no longer waiting for them. Consider the information and communications technology sector, where immigrants with engineering and computer science degrees came in droves over the course of the 1990s and the early 2000s as the dot.com craze built up. However, once the bubble burst in 2001, many of those jobs disappeared, even as an increasing

number of immigrants continued to arrive. This had a tremendous impact on a large number of new immigrants and is cited by Statistics Canada in a recent study as a major cause of the decline in average real earnings among immigrants as a whole.

Ottawa recently announced a program that will speed up the immigration process for those entering under the skilled worker class in 38 specific industries that Human Resources and Social Development Canada (HRSDC) has determined are currently facing skilled labour shortages. However, there is reason to be cautious regarding such a program. There is no indication as to how HRSDC chose these fields, so we are naturally skeptical about whether there are genuine shortages in these fields and, if there are, how long they will last. Several of the 38 occupations are also subject to professional accreditation problems, such as physicians, which is contradictory. How can the process be sped up if none of those who apply can even practice in Canada? The Auditor General's fall 2009 report to Parliament indicated that the analysis behind the selection of these occupations was not particularly robust, and that Citizenship and Immigration was unable to provide any substantial reason regarding why or how the 38 occupations were chosen or even how this would help reduce the number of new applications (one of the goals of the program). As such, caution should be taken to avoid another situation as outlined above.

Having contacts in Canada, particularly in the business world, but also through family and friends, can have an enormous impact on the success of an immigrant's economic transition. Newcomers are at an extraordinarily high risk of falling into low-income status within the first few years following their immigration (see figure 5). Interestingly, those who enter under the skilled-worker class have a higher probability of falling into low-income status within their first year than do those coming under the family reunification class. It should be noted, however, that the high incidence of low income for people in the skilled class may in part result from their higher

likelihood of arriving with significant assets, and hence having less of an immediate imperative to earn income. The relative initial probabilities of falling into low-income status for skilled and family reunification immigrants seems to imply that having family or friends already in the country has a significantly positive impact on those who are just arriving. A number of cities have implemented mentoring or internship programs that provide contacts and Canadian experience. These may be critical in enabling immigrants without contacts to overcome some of the obstacles when they arrive.

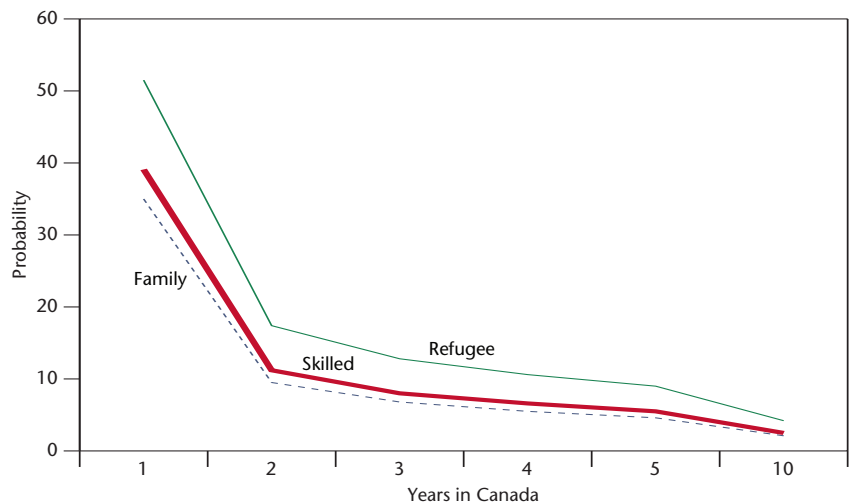
The experiences of Canada's existing immigrants suggest that there is discord between the way in which the immigration system and the labour market are evaluating incoming immigrants, and this is resulting in poor labour market and economic outcomes. As such, there is enormous room for improvement, and the discussion above provides some policy direction for improving the economic situations not only of recent and past immigrants, but also of future cohorts.

First, language barriers faced by current immigrants have to be removed. Doing so will require a combination of developing language pro-

grams to train existing immigrants and raising the bar for English and French for new cohorts before they are allowed to come in. This must involve some notion of communication beyond what is already tested via the oral component of current evaluations.

Second, credential and experience recognition is critical toward immigrants achieving their highest potential, and the scope of what is being sought by the current immigration framework will likely have to be narrowed. This is particularly true for education credentials, which, perhaps, will have to be narrowed right down to the field or even the institution. A federal-provincial program called the Pan-Canadian Framework for the Assessment and Recognition of Foreign Credentials was recently proposed in order to ease the transition of skilled professionals who may spend years working in an unrelated field due to the fact that their experience and credentials are unrecognized here in Canada. The new program would advise applicants within one year of their submission whether their credentials would be recognized, and it is expected to be online by 2012. This is certainly a significant step in the right direction, but only time will tell if the program proves to be successful. Lastly,

FIGURE 5. PROBABILITY OF IMMIGRANTS<sup>1</sup> TO CANADA ENTERING LOW-INCOME STATUS, BY IMMIGRATION CLASS AND YEARS IN CANADA



Source: Statistics Canada.  
<sup>1</sup> Aged 20-54 at entry into Canada.

some consideration should be given to awarding more points when an applicant has pre-immigration contacts that could prove useful in Canada.

The trade-off between evaluating the general characteristics of immigrants (the points system) and specific

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occupational backgrounds (filling occupational shortages) is still in need of further research. With regard to the latter, there is legitimate worry that the identified sectors do not really have labour shortages, and that even if they do today, the workplace changes so rapidly that the shortage could shift to another industry before the immigration system has time to react. So if too much emphasis is placed on occupation characteristics, rather than on issues like education, language and contacts, then the immigrants may become economically stranded.

It is also important to consider the labour market and the related policies more generally. For example, if we were to assume that there are shortages of certain types of workers in certain geographical areas, and not all over Canada, then what prevents existing Canadian workers from moving to those areas of their own accord? Why do employers often seek foreign workers, including temporary foreign workers, when there are apparently pools of potential surplus workers in other Canadian regions? These are the kinds of questions that need to be brought back into the immigration debate, in combination with the issues discussed above.

In part, gaps in the labour market information currently available are one of the primary causes of this inefficiency. A lack of information on available job opportunities, local labour market conditions and skill and education requisites prevents regional labour markets from adjusting to changing macroeconomic environments and effectively matching open positions with qualified job seekers.

This is especially true for interprovincial matching, where a prospective employer in Calgary having difficulty in finding specialized labour will be unable to find a fully qualified professional in St. John's, due to the unavailability of a centralized information source. In addition, the

employment insurance program effectively subsidizes those who are unemployed to remain where they are, despite a lack in employment opportunities. In tandem, these policy stances effectively limit the mobility of the labour force and likely play a role in exacerbating the challenges faced both by employers and workers.

It should be noted that much of this discussion has focused on immigration, social, and labour market policy at the federal level; however, immigrants are increasingly entering Canada under provincial jurisdiction through the provincial nominee programs. Certainly, if the federal program is reevaluated to ensure that incoming immigrants are well-prepared to integrate into the Canadian labour market, then so too should the provincial programs. And indeed, the Auditor General's 2009 evaluation of the immigration system criticized the fact that the provincial nominee programs typically bypass Citizenship and Immigration Canada's minimum selection threshold in order to accelerate the process. The provincial and federal programs will have to be aligned to ensure consistency in both the process and the immigrants that Canada accepts.

**T**here is a substantial amount of evidence that suggests that the Canadian immigration system is not working optimally from an economics perspective. In part, this may flow from a lack of clarification over the objective of the system. In this article we have very narrowly identified one of the immigration system's many objectives, that of improving the standard of living for those

already in the country. The poor economic performance of recent and established immigrants both in absolute terms and relative to Canadian-born citizens provides the evidence and bodes poorly for the future of Canada's economy. As immigrants will likely make up a significantly large portion of the labour force in the coming decades, their economic success equates to that of the nation, as a whole. Thus, there is enormous room for policy to step in and ease their transition: language programs, credential and experience recognition, and employer-sponsored programs will be essential for them to achieve their full potential.

While initiatives have been put forth by the federal government, more can be done, specifically with regard to language issues. Policy initiatives also need to draw upon past experiences, not only to reshape the integration process, but to refine the selection process. Repositioning the selection criteria to better identify those with the characteristics necessary to integrate well into the Canadian economy must involve the recognition that this can have direct implications on the number of immigrants sought. In other words, the objective should not be driving toward a particular total, but rather to satisfy the condition that economic immigrants will be successful in finding gainful employment, which would have a positive impact on the standard of living of all Canadians. Peripheral issues such as the poor state of labour market information and other policy bottlenecks that create inefficiencies in the labour market must also enter the equation, since they have a significant impact on immigrants' ability to integrate in the labour market. Immigrants come to Canada looking for a better life, and these actions are critical for us to give it to them.

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