The Effects of Temporary Immigration on Prices of Non-Traded Goods and Services

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Abstract

This paper analyzes the impact of temporary immigration on the prices of non-tradable goods and services. It presents a model of a small open economy that produces two goods/services, one tradable and one non-tradable. It is assumed that temporary immigrants are confined to work in the non-traded sector and that they are only imperfect substitutes for permanent immigrants and native low skill workers. In our theoretical set-up temporary immigration is predicted to have a negative effect on the prices of non-traded goods and services, while the effect of permanent immigrants depends on the relative low skill domestic labor intensity of the non tradable sector. We test these predictions empirically using a panel dataset of 14 U.S. cities for the period 2000-2006. In line with other recent empirical studies we find that both types of immigration have a negative impact on the
relative price of non-tradable services as a whole. These findings confirm that immigration, like trade and offshoring, has the potential to increase welfare through the reduction of consumer and input prices. When distinguishing individual non tradable sectors, though, we find evidence that permanent immigration increases the price of transport and health services. This finding is in line with the predictions of earlier theoretical work and suggests in the context of our model that these sectors are less low skill domestic labor intensive than tradable goods and services.

- **JEL Classification:** F22, P42, F16
- **Keywords:** Temporary Migration, Permanent Migration, H2-b visas, United States of America, Prices, Factor Specific Model.

I. Introduction

An old concern, constantly revived, over immigration aliments the current public debate in numerous industrialized countries, including France and the United States. The debate in these countries tends to focus on one main concern: the expected negative impact of immigrants on the wages of competing domestic workers. Not surprisingly, therefore, the relationship between immigrants and domestic wages has also been widely documented in the academic literature, with the relevant empirical literature finding only relatively small negative effects of immigration on domestic wages.1

The public debate tends to neglect the potential positive effect immigration has on domestic prices. Indeed, if immigration increases the supply of certain types of labor it is likely to decrease production costs of the goods and services that use this type of labor with negative effects on equilibrium prices. Consumers of the relevant goods and services take advantage of this downward pressure on prices. While the consumer gains from price reductions have been emphasised in the debate on the welfare effects of trade, these potential gains have received far less attention in the debate on the economic effects of migration.

Yet, there appears to be awareness of the potential role immigration can play in this respect, in particular in occupations that natives “are not willing to do” and that cannot be outsourced because they relate to non traded goods and services, like

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