

BROOKINGS
TRADE FORUM
— 2006 —

GLOBAL
LABOR MARKETS?

Susan M. Collins and Carol Graham
EDITORS

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Editors' Summary

An important feature of globalization is the increasing cross-national integration of labor markets. Yet there is little consensus on the implications of that integration, or on the costs and benefits for the many very different groups involved. While there is agreement—at least among most economists—that there are likely to be aggregate welfare gains from increased integration, it is clear that there are losers as well as winners in both developed and developing countries. For example, politically contentious debates about the effects of immigration on the wages of low-skilled workers have proliferated in the advanced industrial economies while poor developing countries have become embroiled in equally contentious debates about the effects of out-migration of skilled workers on their human capital base. Untangling the myriad effects is made even more complex by intermediate arrangements, such as the offshoring of various productive activities by developed country firms to emerging-market economies. This creates new opportunities for skilled workers in the latter, but at the same time offshoring may alter employment opportunities for skilled workers in the advanced economies, and the wage distributions in both.

This ninth issue of the *Brookings Trade Forum* brought together some of the foremost experts on migration, representing diverse perspectives and backgrounds. New research commissioned for each session launched an interrelated series of lively discussions during the conference, held on May 11 and 12, 2006. The objective was not to attempt to reach consensus, but to broaden and deepen our understanding of the extent and implications of the integration of global labor markets. Thus the forum addressed a wide range of topics—from the welfare effects of immigration on labor markets in both developing and developed economies, to the relationship between education systems in sending countries and labor market outcomes in recipient countries, to the merits and demerits of proposals that would drastically reduce restrictions against cross-border labor migration.

Despite the wide range of topics, a number of themes emerged from the analyses. We highlight four. Perhaps the most obvious was the difficulty in drawing general conclusions about the welfare effects of global labor market integration. Various papers and discussions highlighted some of the many critical mediating factors. These include the skill set of the particular group(s) under discussion, the labor market composition in the recipient countries, the relative returns to different types of labor in the sending and receiving countries, the nature of the contractual arrangements relevant for immigrants' work, and more general macroeconomic and financial market trends.

A second theme was that the investments that developing countries make in higher education are no guarantee of retaining their best and brightest. Indeed those very investments may increase the likelihood of out-migration, particularly when the returns to skilled labor are much lower in developing than in the advanced economies.

Third, if international labor markets were more flexible, participants stressed that cross-border labor mobility would likely skyrocket relative to current levels—even if that flexibility entailed only temporary migration. On balance, that increased mobility would have positive effects for poverty reduction worldwide, but its effects on particular nations and on recipient country labor markets would be more mixed. Finally, the discussion made quite clear that, while the economic effects of proposals to increase international labor mobility are themselves difficult enough to measure, the related questions of political rights and citizenship for temporary workers are daunting and have implications for international as well as national norms and standards.

This volume presents the revised papers, invited commentary, and general discussions from the conference. One paper in the volume explicitly examines flows of skilled migrants across countries and how such flows are affected by education investments in the sending countries and by differential returns to skilled labor across countries. Another focuses on the evolution of wage dynamics during development and how those dynamics are affected by global labor market integration. A third paper examines mobility between formal- and informal-sector jobs in emerging market and transition economies and how those trends are affected by the nature of each country's integration into the global economy. Two papers focus explicitly on the potential effects of significant reductions in international labor market mobility, from temporary work permits for migrant workers.

A final panel was asked to reflect broadly on these topics. The first panelist questioned the adequacy of the traditional Heckscher-Ohlin framework for explaining developments in a world where trade patterns do not conform to the

underlying assumptions. He suggests an alternative in which productivity differentials can lead to the matching of skilled workers from advanced economies with skilled workers from developing countries—and the potential for increased inequality between skilled and unskilled workers in both. A second panelist discussed costs and benefits of international labor migration within the classic Heckscher-Olin framework and then assessed how that framework has been altered by the increase in offshoring. The final panelist explicitly addressed the effects of increasing immigration on wage inequality in the United States, as well as the broader implications for a growth model based on significant labor and capital inflow but a fragile prosperity based on high levels of indebtedness, increasing poverty and inequality, and limited mobility and opportunity. In the remainder of this introduction, we summarize the main points that emerged in each of these sessions.

LANT PRITCHETT BEGINS his stimulating paper by asking why there are such large discrepancies in wages across countries if labor and capital markets are as mobile—and policies and institutions are as similar—as most traditional models suggest. He notes that even with the increase in the number of sovereign states in the post–World War II years, there should be more economic integration than there actually is. Instead, differential productivity shocks have led to permanent divergence between countries and, in the most extreme cases, the existence of what he calls “ghost” countries and “zombies.”

Pritchett argues that region-specific shocks can lead to long-run shifts in labor demand, even after other factors have adjusted. If there is population mobility, for example, between regions within a country, one should expect to see population drop sharply in the region experiencing a negative shock (hence the term ghost towns), with little variability in wages across regions over the medium to long run. However, if populations are immobile, which is typically the case across sovereign borders, the adjustment occurs via a decrease in wages. Instead of ghost countries, the results are “zombies”: living dead economies, with wages and incomes falling over time—a situation that characterizes many countries in sub-Saharan Africa. Even if policies and institutions matter a lot, which they do, geography can still also matter. Thus lack of mobility results in countries with many more people than they should otherwise have, regardless of their domestic policies and institutions.

To test his proposition, Pritchett looks at a number of episodes of labor migration and population and wage change across states, provinces, and regions within countries, and across countries—both when mobility is restricted and during an era of open borders. He finds that the variability in per capita income growth

rates is spectacularly larger among countries than among regions within countries. At the same time, the variability in population growth across countries in the world is absolutely smaller than the variability across regions within countries. For example, he shows that there has been huge variability in population growth across regions in the United States. He also cites the contrasting examples of Ireland, where the population shrunk dramatically following the potato shock of 1871, and Bolivia, where the population is 90 percent higher than it was in 1972 despite huge economic shocks.

Pritchett identifies a number of countries that are hardcore geographic zombies (such as Zambia) contrasted with those that he labels as policy zombies (such as Cuba). Zambia is a classic case. He concludes that if its population had fallen in accordance with the economic shocks at the same rate that Ireland's population fell, then it would now be just 18 percent of its current level. If it had fallen at the same rate as in some U.S. regions that suffered negative shocks, then it would now be at just 25 percent of its current level.

He concludes by noting that all aid is based on the presumption that countries can increase their income levels. His analysis points to an inconvenient fact—even in fully integrated economies, there can be big changes in desired population. Without population mobility, geographic shocks create a different dynamic: one of falling wages and outputs. If labor supply cannot be elastic, it is prices that must adjust. However, aid policies focus on *national* development strategies, not the well-being of populations—for example, on Zambia rather than on Zambians. He concludes that a policy that dramatically increased labor mobility—perhaps through temporary work permits and strong penalties for exceeding stay limits—would do much more to reduce world poverty than millions of dollars of foreign assistance to national governments.

Both discussants found Pritchett's results on population and wage trends compelling, and his arguments and proposal thought provoking. Cliff Gaddy highlights the extent to which Pritchett's interest is in zombies—where the actual population significantly exceeds the desired one—rather than in ghosts and in spatial zombies rather than in institutional ones. He notes that spatial zombies are worse than policy zombies because policies can be fixed, while geography in most instances cannot.

Gaddy applies Pritchett's framework to Russia, where his own research is based. However, instead of geographic shocks and mobility constrained by national borders, Russia provides examples in which people are forced to live in places that geographic features make very unattractive. He compares cities in Russia with those in free economies that have similar climate and resource endowments (including distance from the market). For example, consider Perm,

Russia, and Duluth, Minnesota. While the current population in Duluth is about the same as it was in 1920, Perm's population quadrupled over the same time period. Based on the relative distribution of pre-Bolshevik Russia, when the population was more concentrated in the European part of the country, Gaddy estimates that many populations in large Russian cities are now two to four times their desired size.

He concludes that Russia is a case in which policies prevent cities that should be ghosts from becoming ghosts, so they remain zombies, and where resources (oil and gas) subsidize economic activity in those zombie cities that would otherwise be defunct.

Simon Johnson commends Pritchett for yet another innovative paper that breaks new ground and will prompt a great deal of further investigation. He agrees with the core point motivating Pritchett's analysis. Since 1945 cross-border migrations are not only on a much-reduced scale compared with the past, they are also asymmetric. It is much easier to move into boom areas than it is to move out of bust areas. And, perhaps most important, migrations out of small, poor countries are now quite difficult. In addition, Johnson identifies a major risk that is only hinted at in the paper: economic depression may lead to deadlock and conflict, exacerbating the income decline.

Johnson finds Pritchett's analogy to ghost towns a provocative but productive way to think about some of the problems in relatively poor countries today, from Haiti (whose economy was previously based on sugar) to parts of West Africa (where commodity booms come and go). However, he notes that when people cannot leave becoming a zombie is not the only possible outcome. The inhabitants may find something else to do. Perhaps they have skills that are useful for other activities or they can attract other kinds of investment. Barbados, for example, has managed to achieve a much higher level of income than Guyana, despite the fact that both have strong heritages of sugar, slavery and other forms of forced labor, and deep ethnic divisions.

He concludes by noting that almost none of the great successes of the past fifty years (that is, rapid sustained growth, starting with weak or very weak institutions) have been based on commodity price booms. Instead, the catalyst has been figuring out how to better integrate into global manufacturing production chains. Low wages are not a sufficient solution, but they are also not necessarily an obstacle to initiating a sustained growth process.

MARK ROSENZWEIG EMPIRICALLY analyzes the cross-country migration of students. This group has received surprisingly little prior attention among researchers, despite its importance. For instance, the flow of students to the

United States far outpaces flows of other immigration categories, such as skilled workers or legal unskilled workers. Using data on student visas, Rosenzweig examines the direction of migration, the returns to various skill levels, and differences across different countries. He notes that most migration models fail to account for either different skill levels of migrants or differences in returns to skills across countries. He exploits a new data set from the New Immigrant Survey to examine the flow of students to the United States, the stock of U.S. foreign-born students, and the number of U.S. foreign-born students who become permanent residents. His paper extends beyond the standard focus on the GDP of the sending countries and looks at rewards to skills across countries.

He tests two separate models of migration. One is a schooling constraint model, in which migrants come from countries with high rewards to skills but low opportunities to obtain additional schooling at home. The second is a model in which migrants acquire skills at home, where the skill price is low. However, expanded schooling opportunities at home actually increase migrant outflows because the domestic rewards to skills remain much lower than in the developed countries.

Rosenzweig first notes that the direction of migration flows is very clear. The lion's share of the world's student migration goes to the United States, followed by the United Kingdom, and then to Australia and Canada. At the same time, (purchasing power parity) PPP-adjusted earnings of high school and college graduates vary tremendously across countries. In countries such as Nigeria, college graduates earn as little as \$1,000 per year; in Korea, college graduates still earn less than \$10,000 per year, while in the United States, high school and college graduates earn \$35,000 and \$50,000 per year, respectively.

The main sending countries are in Asia. Topping the list are countries with high economic growth rates, but with low skills prices (China and India). They are also far away from the United States, have at least one university ranked in the top 200 in the world, and have very large populations. Rosenzweig finds that growth rates and per capita GDP both affect the capacity of countries to send student migrants. The number of U.S. student visas issued annually, the stock of U.S. foreign students, and the number of foreign-born students who remain permanently in the United States are all higher for countries with lower skill prices and for countries with a larger number of universities per capita.

It is interesting that Rosenzweig finds that an increase in the number of home universities increases the number of student stayers in the United States. This suggests a story of educated students coming to graduate school in the United States, seeing huge wage differentials, and thus choosing to stay. It also sug-

gests that some kinds of developing country investments in education can exacerbate brain drain. Thus higher skill prices in the home country are negatively correlated with student outflows; when controlling for skill prices, greater domestic investment in education is associated with more out-migration. As he notes, a better understand of these linkages will be important for determining the optimal distribution of additional investments in schooling. Somewhat less surprisingly, he also shows that those migrants who have come to the United States with prior student visas and have been able to become permanent residents (that is, they acquire green cards) are much more likely to get a job and to get married. This is in part because they are more likely to meet someone while in school.

In concluding, Rosenzweig also cautions readers that his data select only one kind of migrant—those with relatively high educational attainment. Other types of immigration may also have important implications for schooling. For instance, remittances from unskilled migrants may contribute to better education in the home countries.

In his discussion, Douglas Irwin notes that the paper sets up a horse race of sorts between the “school constrained” and the “migration” models. Rosenzweig finds overwhelming evidence for the migration model because of the huge gaps in wage levels—regardless of skill level—between developing and OECD (Organization for Economic Cooperation and Development) countries.

Irwin finds the framework in the paper compelling, but he is skeptical of the conclusions for two reasons. First, he is puzzled why so many migrants return home if wage differences are really so large. In this context, he highlights the large variation in the propensity of students to stay in the United States who come from sending countries with similar wage levels.

Second, Irwin argues that an analysis based on time series data might provide more compelling support for a school constrained model than the cross-country results reported in the paper. For example, in Korea, rewards to higher skills increased over time, but so did demand for foreign higher education, as domestic education became inadequate.

In his extensive commentary, the second discussant, Jeffrey Williamson, both highlights a number of important contributions of the paper and makes a variety of suggestions for extending the analysis. He notes that the brain drain debate would be better served if we spent more time understanding foreign student migration. The United States today admits two to three times as many foreign students as those already-schooled foreign born who are admitted on the basis of their skills. Further, it is much easier for potential immigrants as students to get permanent skilled jobs in the United States than any other way.

Williamson highlights two very important findings in the paper. Student migration is positively correlated with gaps in skill wages. More and better schools at home are correlated with more student emigration, not less, *ceteris paribus*, where the *ceteris paribus* that matters most is low skill wages at home. This is a powerful finding, which might suggest that investment in the quantity and quality of educational institutions in poor countries will serve to push more students abroad, rather than retain more at home.

However, Williamson stresses that both findings speak to *correlations* only. The critical next steps should focus on establishing *causation*. He then discusses three potential flaws in the paper that might influence these inferences: selectivity, omitted variables, and causality. On the selectivity front, Williamson points out that good students go to “good” schools in host countries *and* at home. Although the analysis controls for average schooling quality at home, a country with low average school quality can still have a number of excellent schools from which the emigrants are selected.

In terms of omitted variables, one concern is lack of a “friends and relatives” effect. Long-distance migration is expensive, and contacts in the host country are key to help with finance, job search, and assimilation. He posits that the addition of stocks of foreign born to the regressions will dramatically change the results. He also worries that the population size variable may pick up effects of the spectacular demographic transition underway in many developing economies. An alternative would be the share of the university-aged population.

He then turns to causality. The paper reports that more and better schools at home are correlated with low skill wages at home. Why? Similarly, tables 5 to 7 report that more and better schools at home are associated with more students abroad. Is this because more and better schools lower the cost of migration? Or does the emigration serve to encourage schooling demand by the next cohort? Williamson cites the need for the author to reconcile his results with the brain drain–gain literature.

Finally, Williamson uses his economic historian hat to note that Rosenzweig misses four great opportunities to deal with the past and the future, which could help confirm or deny his conclusions. First, when did foreign students start arriving in big numbers at Australian, Canadian, British, and American universities? Second, how will student migration flows play out over the next few decades? Third, how do host countries compete for students? Fourth and finally, the analysis should allow for increased skilled immigration from poor countries to reduce the OECD skilled wage gap, thereby increasing skill scarcity at home. During the great mass migrations before 1913, European emigration contributed to wage

convergence in the Atlantic economy. Why should we expect things to be different in the twenty-first century?

ANDREW WARNER'S PAPER presents and analyzes new data on wages by occupation for fifty-eight countries. The paper also provides empirical evidence from a number of sources on how wage levels correlate with GDP—both across countries and across time within countries—and explores determinants of cross-country wage levels.

The paper begins with a useful overview of strengths and limitations of the available international wage data. A key problem is lack of consistency, both across countries and over time. Further, most of the data focus only on manufacturing, and breakdowns are often not available by occupation. Historically, data sets also tended to include very few of the poorer countries. Recently, the well-known Freeman-Oostendorp data set provided a major advance by estimating standardized wages and earnings from the large data set of the International Labor Organization (ILO). Thus an important advantage of the data presented here is that they were all collected using the same methodology and during the same time period (January–February 1999). This implies a high degree of comparability across countries.

The data come from collaboration with the World Economic Forum's executive opinion survey. Samples were chosen to be proportional to the sectoral distribution of nonagricultural workers. Data on typical 1998 monthly wages and salaries for five occupations were collected through personal interviews (in principle with a top manager in each enterprise). The occupational categories were office cleaner, driver, secretary (with five-years experience), mid-level manager, and senior manager. Warner reports that adjusting the wages for observable differences in firm characteristics across countries has little impact on his results.

Warner highlights two notes of caution relevant for interpreting the empirical results he presents. First, at a sufficiently aggregated level, wages will necessarily be strongly correlated with GDP per worker. However, wages of specific occupations that represent fractions of an economy can behave quite differently from economy-wide GDP. Second, wages and GDP are both clearly endogenous. Thus the relationships presented in the paper should be viewed as descriptive, not causal. The analysis at the end of the paper attempts to address this issue by controlling for the capital-labor ratio—a key factor that simultaneously affects both wage levels and GDP per worker.

Warner presents three major sets of results. He provides a wealth of charts as well as simple regressions to explore correlations between wages and per

capita GDP. Focusing on results using his new data, wages in less-skilled occupations tend to rise proportionately with real GDP as expected. But it is interesting that managerial wages (the most-skilled occupations) are found to rise less than proportionately. Consistent with existing literature, he also finds that dispersion of average wages across occupations (for example, managers compared with drivers) declines as GDP rises, both between and within countries.

The second set of empirical results clearly indicates the importance of capital-labor ratios in explaining differences in wages for similar work (occupation) across countries. Finally, the paper also relates average occupational wages to variation across countries in skill abundance, labor market institutions, product market competition, and exposure to globalization, controlling for capital per worker. Globalization is measured with a subjective variable (on a 1 to 7 scale) of the extent to which managers in a country speak a foreign language. The author finds that the positive association between average wages of managers and GDP per capita is weaker in countries with higher share of managers who are proficient in English. He finds negative effects of average levels of skill accumulation across countries on wages in high-skilled occupations. The paper also shows some evidence of roles for minimum wage rules, market competition, and a greater degree of openness in the market for managerial occupations.

Warner concludes by noting that differences in the quantity of capital around the world, coupled with still significant barriers to mobility of labor, capital, and goods and services, are the major reasons for vastly different wage levels for similar occupations around the world. He offers two possible explanations for the finding that the gap between wages of managers and office cleaners (an indicator of the skill premium) tends to narrow as countries become wealthier. One is that relative skill supplies tend to increase, reducing the skill premium. The second is that pay for managers in poorer countries may be pulled up toward global pay scales if workers in these occupations have acquired language and other skills that make them competitive in a global market for managers.

Both discussants, Nina Pavcnik and Harry Holzer, stressed that an important contribution of the paper is to bring a useful new data set to bear on the analysis of cross-country differences in the returns to labor. Advantages of the data are that they overcome some of the comparability problems that typically plague cross-country data sets and that they provide detailed information about firms. In terms of limitations, Pavcnik mentioned the absence of information over time and expressed concerns that the relatively small samples taken in each country may not be nationally representative.

Pavcnik is reassured by Warner's finding that average occupational wages are strongly positively correlated with GDP per capita for all occupations. Yet she finds it striking that this positive correlation is smaller for higher-paying occupational groups such as managers and that the positive association between average wages of managers and GDP per capita is weaker in countries where a higher share of managers are proficient in the English language.

A recurring theme in Warner's paper, which Pavcnik highlights, is the extent to which the weaker correlation between occupational wages and GDP per capita observed for managers reflects a labor market for managers that is more influenced by global factors than are the labor markets for lower-skill occupations such as janitors or office cleaners and drivers. Yet she questions the use of the foreign language variable as a measure of globalization, as it likely reflects country characteristics such as the country's colonial ties and the quality of domestic institutions. She suggests that the paper would benefit by focusing on a particular aspect of globalization, enabling the analysis to pinpoint the channels through which that aspect of globalization might affect wages. The implicit assumption underlying the paper's argument is that globalization should make average wages less dependent on local economic conditions. However, theory does not necessarily predict whether trade liberalization will cause wages to equalize across countries. If trade is driven by differences in relative factor abundance, wages could equalize if the countries produce the same goods (that is, are in the same cone of diversification) and use the same production technology. But if trade is driven by relative productivity differences, cross-country real wage differences might persist—even with free trade.

Pavcnik emphasizes that it is very difficult to establish the link between globalization and aggregated wages. Recent work in international trade, including her own with Penelope Goldberg, has moved beyond looking at cross-country averages and instead uses microlevel surveys of workers and firms to emphasize the importance of heterogeneity in the impact of globalization within a country. These recent studies show that, following changes in industry tariffs, trade affects individuals with similar observable characteristics differentially depending on their industry affiliation. She concludes by noting that future work will make additional use of Warner's detailed data to further our understanding of determinants of wages in a globalized world.

In addition to commending Warner on his interesting new data set, Holzer also notes the importance of the questions the paper raises. To what extent do different groups of workers in different countries share in the economic growth associated with international trade? To what extent are they compensated for

the higher risks and growing inequality that trade often generates? Overall, he finds Warner's main results—relating wages to real per capita GDP and to capital-labor ratios, as well as a variety of market and institutional characteristics—to be broadly consistent with expectations. However, he notes that Warner's finding that wage responsiveness to real GDP declines with the rise in skill level of the job is somewhat contradicted by the other studies that Warner cites, such as those by Freeman and Oostendorp and Ashenfelter and Jurajda.

Holzer encourages Warner to further explore the role of capital-labor ratios in explaining wages across countries within each occupation. He wants to know more about the partial contribution of this variable to the results, and about its use as an instrument variable. He raises questions about several additional variables. The indicator measuring a respondent's perception of the intensity of competition does not specify any kind of reference point, making it difficult to interpret in a cross-country context. The foreign language variable arbitrarily assigns a value of 6 on a scale of 7 to countries where the use of English is widespread. Such a measure could be a proxy for many different characteristics of countries in the regressions that are estimated.

Holzer concludes by noting that his specific criticisms do not detract from the fact that Warner has addressed some of the most important questions in international labor markets, generated a potentially important new set of data, and produced some descriptive findings that are very useful.

DEVESH KAPUR AND JOHN MCHALE in the fourth paper provide a general critique of Lant Pritchett's Plan B, which would allow massive flows of temporary migrants across borders. They do not focus on the specifics of this proposal but on the general case for using migration as a poverty-alleviation tool. The idea is "if you cannot bring good institutions to the poor, allow the poor to move to the good institutions."

They make five basic points. First, differences in institutional quality are significant determinants of differences in living standards, but institutional improvement is very hard to "buy" without high levels of foreign aid, and even then it can be an elusive objective. Second, there is potential for large income gains through institutional arbitrage as economically debilitating institutional structures are left behind because of high levels of out-migration. Third, there may be negative effects for host countries that include distributional harm to the incomes of the less skilled, fiscal harm from attracting individuals who impose net costs, and harm to civic capital arising from reduced cohesiveness within communities. Fourth, to the extent that rich countries target the highly

skilled, institutional development in developing countries may be hurt by the loss of human capital. Finally, given weak institutions in sending countries, it is critical to design any program to ensure that the benefits of expanded migration accrue to the intended beneficiaries and not to rent seekers.

Kapur and McHale frame their discussion with a debate in political philosophy between nationalists and cosmopolitans. Focusing on the concept of “partial cosmopolitans,” they apply Amartya Sen’s concept of consequence-based evaluation to assess Plan B. This allows the evaluator—for example, the rich country—to consider both the interests of co-nationals and the interests of foreign-born individuals, with the weight on the latter increasing, the worse off their starting point is.

Kapur and McHale note that standard development strategies often fail because they focus on poor countries rather than poor people, resulting in a continuation of high levels of poverty. If you accept partial cosmopolitanism, however, then the case for Plan B is largely empirical and based on the answers to such questions as: How much would the migrants benefit? Would rich country natives be hurt (and if so, which ones and how much)? Would those left behind be hurt? (On the one hand they gain from remittances, but on the other they and the home country lose through skill loss, a problem that is worse for small countries).

The authors then review the evidence. They note extreme divergence in income levels among countries due to institutions and physical capital per worker, and they argue that these income gaps are due more to places than to people. Their evidence for this is that, while human capital is lower in poor countries, there are still huge gains from migration. The impact on rich countries from reasonable levels of skilled migrants is on balance good: increased innovation, knowledge spillovers, specialized skills, scale economies, and the fiscal benefits from more well-paid earners. Not surprisingly, many rich countries seek to attract mobile talent.

There is much more skepticism about the benefits of unskilled migration, as suggested by the work of George Borjas documenting the negative effects on the wages of U.S. unskilled workers (that is, native born). Yet the authors note that these findings are disputed by many other researchers, some of whom conclude that the effects of immigration on wages wane over time. Also, immigrants and natives are not always perfect substitutes, as the standard models suggest. However, Kapur and McHale also state that the fiscal rights of migrants should not impose fiscal burdens on natives.

Finally, the impact on the sending countries appears to be very sensitive to the skill composition of emigration, with skilled emigration posing the great-

est risk of harm. Not all of the effects are bad, however, as skilled emigrants may return later and become positive forces for institutional change. The risks are greatest, meanwhile, for small countries, for whom the pool of skilled individuals that can generate momentum for institutional change is very small.

The authors conclude by noting that the devil will be in the details. Implementing such a plan, which would inevitably include a smaller supply of visas than have been requested by poor country citizens so far, would provide huge potential opportunities for rent seeking. It would be critical to ensure that the beneficiaries of the plan were the emigrating citizens. While endorsing Plan B in principle, they caution that much more needs to be done before it could be implemented.

In his comments, Gary Burtless began by noting the very persuasive evidence in Lant Pritchett's paper showing that cross-regional differences in average incomes are much narrower where the legal impediments to migration flows are small. Pritchett's message is that, while cross-border mobility may not be an engine of development in lagging areas, it is a driver of cross-regional income equalization. Yet he notes that the paper by Kapur and McHale makes a different point: that cross-regional income differences are not only due to economic shocks but also are due to regional and national differences in institutions. Burtless would add to this list differences in social norms, including trust and honest dealing in the market place. He sees institutions and norms as essentially stuck in place. To change them, citizens can either make a revolution or move somewhere else. The latter is what usually happens.

However, modern nation-states tend to regard cross-border mobility with suspicion—particularly mobility by those who want to compete with native workers. Rich democracies do not make distinctions between those migrants who want to work for a few years and those who want to stay indefinitely.

Burtless points out that Kapur and McHale's discussion of political philosophy leads them to conclude that it is a good idea for nation-states to take the interests of people—and particularly poor people—in other countries into account in addition to the interest of their own citizens. Although this perspective may not be particularly radical to employees of universities, international institutions, or nongovernmental organizations, he doubted that it was typical of the median rich country voter. He stressed that the political viability of Plan B depends on what the median voter thinks, and in particular on how she or he would weight welfare gains to immigrants against the distribution of gains and losses among fellow citizens.

In Burtless's view, the essential fact—made clear in the Rosenzweig paper—is that most Third World workers would benefit tremendously if they could

enter the United States freely to work. Gains and losses for everyone else are less clear and hard to estimate reliably. Some home-country residents benefit through remittances. At the same time, no one knows whether out-migration hurts or helps local governance, entrepreneurship, education, or public health in developing countries. Burtless noted that the authors' own conclusions about the welfare effects on unskilled native workers are imprecise. While some of these losses can be ameliorated by transfer programs, it is difficult to reliably identify the losers. When social protection programs are more generally available, as in many European countries, voters may be even more suspicious about benefits accruing to migrants.

Burtless concludes that immigration has most likely improved the welfare of both migrants and of native-born individuals in the United States. But identifying those gains precisely is very difficult. And in the long run, the political feasibility of Plan B depends crucially on persuading rich-country voters that they ought to accept more migrants for moral reasons or that they are very likely to derive economic benefits from doing so. In his view, the current political debate in the rich countries reflects little consensus on either of these propositions.

THE FIFTH PAPER switched gears to focus on labor mobility within, instead of among, countries. Suzanne Duryea, Gustavo Marquéz, Carmen Pagés, and Stefano Scarpetta report on their ongoing empirical analysis of job and earnings mobility in low- and middle-income countries. As they note, developing countries are often observed to experience even larger rates of labor market mobility than do developed economies, as jobs are created and destroyed and as workers move among jobs and change their labor market status. While this dynamism can promote economic efficiency and growth by moving resources into more productive activities, the welfare losses associated with high job insecurity can be considerable. Furthermore, the limited social safety nets in developing economies are less able to insulate workers against economic risks. Their findings highlight that mobility is indeed very high both across jobs as well as in and out of the labor market and that there appears to be significant earning consequences associated with some types of mobility.

The work analyzes experiences in nine countries. Three are in Latin America (Argentina, Mexico, and Venezuela). The remaining six are in eastern Europe and the former Soviet Union (Albania, Georgia, Hungary, Poland, Russia, and Ukraine). This sample is quite heterogeneous, with per capita incomes ranging from less than \$2,000 in Georgia to more than \$12,000 in Argentina. The period of study varies across countries, from two to twelve years from 1990

to 2004, depending on data availability. While countries such as Venezuela experienced almost no GDP growth during the period of study, others such as Albania and especially Ukraine grew rapidly. Most of the countries opened up more to trade. The Latin American economies all experienced considerable volatility, including the peso crisis in Mexico and the beginning of the crisis in Argentina. The economies of eastern Europe and the former Soviet Union were all undergoing transitions toward more market-oriented economies, although restructuring proceeded at different paces. The data enable the authors to consider six distinct labor market statuses: out of the labor force, unemployed, farmer, self-employed, and wage employee in either the formal or the informal sector.

Their analysis uncovers a complex picture of labor mobility. Although there is considerable cross-country heterogeneity, some broad themes emerge. All nine countries exhibit a high degree of mobility both in and out of the labor market and among types of jobs. Wage jobs in the informal sector tend to be less secure than those in the formal sector, and there is much more movement between wage jobs in the formal and informal sectors than there is between wage jobs and self-employment. Those who leave self-employment are more likely to move into the informal sector, become unemployed, or leave the labor force than they are to secure formal sector jobs. Although limited social safety nets imply that workers typically cannot afford long periods of unemployment, the authors find greater unemployment persistence in transition economies.

This labor mobility has implications for earnings. While moving from the formal to the informal sector tends to reduce earnings in Latin America, it had the opposite effect in some transition economies. Switching from informal employment to self-employment tends to be associated with increased earnings. However, the authors find evidence that switching is associated with worker characteristics that are likely related to their productivity, suggesting selection biases that are important for interpreting their results.

In her discussion of the paper, Carmen Reinhart focuses on three main issues. She stresses that her background caused her to think about a country's economic performance from the macroeconomic perspective. During the period studied, some countries in the sample had experienced large output swings, while others were just emerging from a severe recession. Exchange-rate or banking crises characterized some of the episodes. In many cases, there were large changes in key relative prices, such as between traded and nontraded goods. These developments would all be expected to have labor market implications, such as displacing workers from formal sector jobs. Furthermore, crisis periods within a country and countries that are crisis-prone may not be representative

experiences from which to draw general lessons about labor market dynamics. Thus, she thinks that it would be very important for the authors to control for macroeconomic variables in their future analyses.

Reinhart encourages the authors to enrich their analysis by also studying transitions within labor market groupings. For instance, in many of the economies, she believes that there had been significant shifts of labor from agriculture and industry into the financial sector. Much of this would have taken place within the formal sector and thus not classified as a transition. It would also be interesting to know how much of the formal sector dynamics could be associated with downsizing of state-owned enterprises, especially in transition economics.

Finally, she expresses some concerns about the data. In particular, she cautions that the data for the informal sector may be of relatively low quality. It would be helpful for the authors to discuss potential measurement errors and to explore ways to check the robustness of their conclusions. However, she also stresses that despite its limitations the type of econometric analysis these authors are using is very valuable for helping us understand labor market dynamics within developing countries.

OUR THREE PANELISTS were asked to think more broadly about global labor market and migration issues. Michael Kremer examined two new ways of modeling trade and immigration that have different implications from those of the traditional Heckscher-Ohlin (H-O) trade model. Standard versions of the H-O model predict that inequality will tend to decline in poor countries that open up to trade but rise in rich countries that allow increased immigration of low-skilled workers. In contrast, Kremer's models shows that, under some sets of assumptions, trade can increase inequality in poor countries, while migration can raise the relative wages of low-skilled workers.

Kremer first surveys the evidence that higher levels of trade lead to declining inequality in developing countries. He finds that most empirical studies have concluded that inequality and openness are in fact positively correlated, particularly in Latin America. These studies suggest the need to move beyond the factor endowment basis for trade contained in the Hecksher-Ohlin framework.

One of the trade models proposed by Kremer captures the globalization of the production process. A key feature is that workers of varying skill levels maximize output by working together only when the relative difference between their skill levels is not too great. Globalization enables workers in rich and poor countries to work together. However, it is only the higher-skilled workers in developing countries who have sufficient skills (such as speaking English) to join the

global supply chain. Thus trade benefits the better-off in developing countries while leaving low-skilled workers unaffected, thereby worsening inequality.

Kremer's second model approximates a type of immigration that has become prevalent in many newly rich countries such as Hong Kong and Singapore. These countries have instituted programs that encourage foreigners to immigrate and work as private household workers (nannies) for a limited period of time. This frees up higher-skilled natives, mostly women, to leave domestic work and enter the labor force. The taxes paid by the migrant women constitute a pure gain for the host society, while increased participation of high-skilled women may reduce the skill wage premium.

Kremer uses his model to calibrate the effects a Hong Kong-type program would be likely to have in the United States. In contrast to the negative distributional impact and small increase in welfare implied by the Hecksher-Ohlin framework, Kremer finds that a foreign private worker program could cause the relative wage of low-skilled workers to rise by 10 percent and welfare to increase by 1.84 percent of GDP. Furthermore, his model suggests that wage inequality would decrease, even if three-fifths of the immigrants leaked into the general economy to compete with native low-skilled workers.

Arvind Panagariya explores some of the recent issues in the migration debate in the context of the conventional trade literature on the "brain-drain." This literature typically analyzes implications of migration for each of the three entities involved: the migrant, the source country, and the destination country.

Because migration enables the migrant to earn a higher wage in the destination country, the traditional literature sees him as an unambiguous beneficiary. Some question this view in the context of Third World mothers who emigrate to care for First World children, leaving their own children behind. However, Panagariya argues that the traditional conclusion is correct: Migrating mothers make the choice voluntarily; the income they earn improves life for their children (cared for by family back home); they bring loving care to the First World children (perhaps unavailable from super-busy First World mothers).

The effects of emigration on the source country are more complex and controversial. The traditional literature shows that if the migrant does not own any other factors of production before or after emigration, his departure hurts those left behind. However, remittances could more than make up for the decline in their income.

Since remittances are more likely and larger if migration is temporary, some economists suggest temporary migration as an alternative development strategy. Panagariya is skeptical. Examples of developing countries experiencing rapidly rising living standards on a sustained basis through emigration in the

last fifty years are few and far between. He stresses that virtually every successful growth experience has taken place in the presence of rapidly expanding trade and either low or declining trade barriers. More important, world markets are open to international trade, so a strategy based on outward-oriented trade policies is readily available. In contrast, opening rich country markets to migration—be it temporary or permanent—on a large enough scale to make a dent in global poverty is a fantasy at present.

For small developing countries, however, there is some evidence that skilled emigration has reduced the welfare of those left behind despite remittances. In particular, in some African and Caribbean countries, the proportion of emigrants who are skilled has exceeded 45 percent—in some instances reaching as high as 80 percent.

Panagariya argues that skilled emigration may benefit larger developing countries, even if remittances per migrant are relatively low. At 4.3 percent, the proportion of skilled workers emigrating from India is less likely to have created a serious shortage of such workers at home. Further, the conventional welfare losses have been more than offset by faster development of the information technology industry, increased incentives to seek technical education, and a variety of “diaspora effects,” such as improved political and economic links between the United States and India.

There is a large literature on the effects of immigration on the destination country, principally the United States. The dominant theme has been that immigration depressed wages, worsened the income distribution, and imposed fiscal costs on the native population. However, Panagariya finds that the theoretical and empirical bases for these propositions are rather fragile. He argues that most existing studies fail to account for the interaction of immigration and trade on wages and that increased supply of labor from immigration is likely to be offset by reduced supply of labor through trade. Immigration expands those sectors that use the migrating factor more intensively, reducing the need for imports of these goods and services.

Panagariya also argues that the adverse impact on natives from immigrants’ access to welfare programs and public services has been overstated. In his view, typical calculations consider only the cost side of the equation. Immigrants also provide services such as gardening, housework, and child care that either generate surplus for native consumers or allow them to earn much higher incomes through participation in the labor force. A balanced evaluation must take both sides of the equation into account.

Isabel Sawhill focuses on developments in rich-country labor markets and the extent to which these are affected by migration issues. She notes that much

of the debate on immigration in the United States focuses on wage inequality, which, similar to the number of individuals in poverty, has been rising. Clearly, the United States has a strong economy that attracts a great deal of labor and capital from abroad (thereby providing numerous opportunities for migrants of all skill sets). However, she sees its prosperity as fragile, both because of its reliance on high levels of foreign debt and because the strong growth was, rather ironically, accompanied by more inequality and poverty and by low mobility rates compared with other OECD countries.

Sawhill's comments focus on three sets of new research results. The first was work by William Dickens and Erica Groshen examining trends in real wages across OECD countries. These authors found that the United States has less real wage rigidity than do most other wealthy economies, with levels comparable to those in Greece. Labor markets in the United States are characterized by high levels of flexibility, which is often cited as part of the reason for such strong U.S. rates of growth.

Another part of the story, though, is increasing levels of wage inequality. In exploring this dimension, Sawhill cites research by Melissa Kearney and others. From 1973 to 1990, wage inequality increased in the upper (as measured by the ratio in earnings between the ninetieth and fiftieth deciles) and lower (as measured by the ratio between the fiftieth and tenth deciles) tails of the income distribution. In the 1990s, however, wage inequality increased only in the upper tail. In other words, the distance between the wealthiest workers and the rest of the distribution increased, while trends in the lower tail remained the same. At least on the surface, this does not suggest that unskilled immigrants were the force driving changes in wage inequality. However, it is important to note that these official data do not include earnings of illegal immigrants.

Sawhill also cites recent work by Tom Hertz, which looks at trends in social mobility. Hertz examines intergenerational mobility as measured by the earnings elasticity between fathers and sons. In his sample of OECD economies, the United States has the lowest level of social mobility after the United Kingdom, a result that she argues defies the image of the United States as the land of opportunity.

Finally, Sawhill cites research by Carol Graham that examines happiness levels—and their relation to GDP levels—across countries. This work finds little correlation between per capita income levels and happiness in either developing or developed economies. It suggests that growth alone—without a broad base, with high levels of inequality and insecurity, and absent a broad base of opportunities for upward mobility—will not increase happiness.

Sawhill concludes that these bodies of research suggest that immigration is not to blame for trends in inequality in the United States. But at the same time, our current—and fragile—pattern of growth does not benefit the average citizen as much as it does the wealthier ones, nor does it increase happiness or subjective well-being.

IN SUM, the presentations and discussions at the conference raised a remarkably wide range of important policy issues—as well as questions for future research. While there was widespread agreement in some areas, many others were quite controversial, such as those highlighting normative questions about political rights as well as the empirical questions about welfare benefits for workers in both sending and recipient countries. Many of these issues will remain at the forefront of public and policy debates on migration and labor markets for years to come. It is our hope that the empirical and theoretical work presented in this volume can help to inform those debates and to provide impetus for the broad range of new research that will be necessary for a fuller understanding of our increasingly global labor markets.

