Did the European Free Movement of Persons and Residence Directive Change Migration Patterns within the EU? A First Glance

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In April 2004, the European Parliament and the Council of the European Union adopted Directive 2004/38/EC "on the right of citizens of the Union and their family members to move and reside freely within the territory of the Member States", the so called "European Free Movement of Persons and Residence Directive". The adoption of the Directive is controversial and has triggered debates across Europe. This is especially the case in Germany with its well developed welfare state. Some experts argue that the free movement of persons represents a basic condition for making a single European market fully effective. People would move from areas with low economic opportunities to the centres of economic activity. The outcome would be a better allocation of production factors within the European Union (Sachverständigenrat, 2004, 117–118). Other experts, however, raise concerns about potential welfare tourism. According to them, people would move from areas with low social standards towards regions with more generous social support. The result would be a free ride to the social welfare state (Sinn 2004, Sinn and Ochel 2003 and Sinn et al. 2003).

Who is right: the optimists, who expect low levels of economic arbitrage migration or the pessimists, who expect high rates of social benefits arbitrage migration? In the following, we aim to bring together a variety of aspects related to the European Free Movement Directive and its potential influence on migration patterns within the EU. First, migration trends of EU-14 nationals (old EU Member States excluding Germany) to Germany are examined. In this context, we look at flows as well as at the composition in terms of age structure and employment status. We focus on the "old" EU members because transitional arrangements (TAs) have excluded free mobility for the eight new Eastern European member countries for the moment. The acquis communautaire will be fully applicable in all Member States after a two-phased transition period of five years (with a review after three years) and a possible prolongation for individual Member States for an additional two-year period. Sweden and Ireland decided not to apply any TAs to the new EU states from the beginning of their EU membership (on 1 May 2004). The UK abolished ex-ante restrictions and has kept a Workers Registration Scheme only. Greece, Portugal, Finland and Spain lifted the restrictions in 2006. Most of the other EU countries have decided to abandon the restrictions in the near future. Only Austria and Germany are still applying the TAs in a rather restrictive way – most probably until the TAs irrevocably come to an end on 30 April 2011. Thus, we cannot consider the effects of the "Free Movement and Residence Directive" for the migration flows from Eastern Europe to Germany in isolation from the last two years.

Secondly, in particular in the context of welfare tourism, the Swedish case after EU-enlargement cannot be ignored and is thus dealt with here. Sweden was one of the countries that did not apply any TA to new EU Member States. Thus, it is useful to have a closer look at whether changes in the migration flows to Sweden can be observed after such a short period.

The theory of immobility could provide some insights into a rather slow and weak reaction to the lifting of mobility restrictions within the EU. Using what we call the *Insider-Advantage Approach,* we

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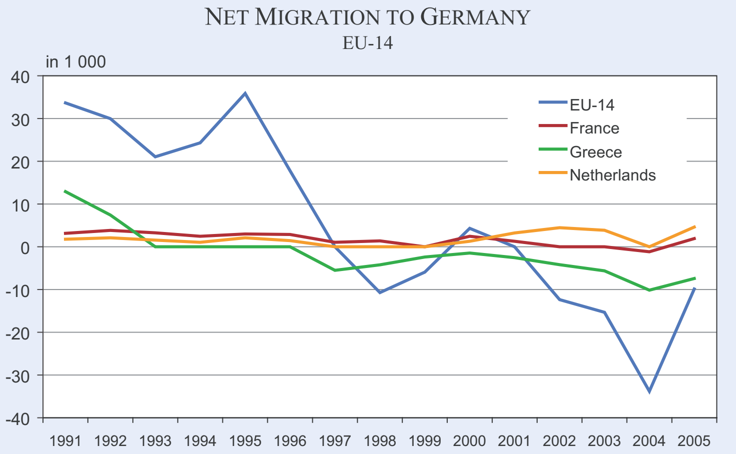
argue that it is reasonable to expect lower rather than higher intra-European migration flows. Lastly, we turn to the impact of immigration on public finances. The literature that includes third country-nationals provides a useful starting point and would suggest that the European experience of the effects on public coffers is mixed.

While taking into account the scarce evidence available at this early stage of the Directive, we conclude that arguments sustaining the probability of large changes in migration patterns within the EU, in particular towards countries with generous welfare systems, are not justified. At least for the moment and with regard to the first – still limited – empirical evidence, we conclude that the European Free Movement of Persons and Residence Directive has not had a statistically significant impact on the size and structure of European migration flows. Furthermore, we would not expect that intra-European migration flows will reach a dimension posing any serious threat to jobs, wages and public coffers in the destination countries in the future. Quite the contrary: intra EU migration might help to overcome some of the economic and demographic challenges of the future.

Figure 1



Source: Federal Statistical Office Germany; own calculations.

Migration trends of EU-14 nationals to Germany

In the case of Germany, a net outflow of migrants originating from the EU-14 has been registered since the early 1990s. This net loss migration peaked in 2004, when Germany experienced an inflow of 92,931 EU-14 nationals against an outflow of 126,748. When looking at the migrants by nationality in more detail, the picture for the year 2005 presents itself as follows in the table below. For some of the listed countries there was a significant outflow of residents from Germany.

Main in-/outflows from EU-14 to Germany in 2005

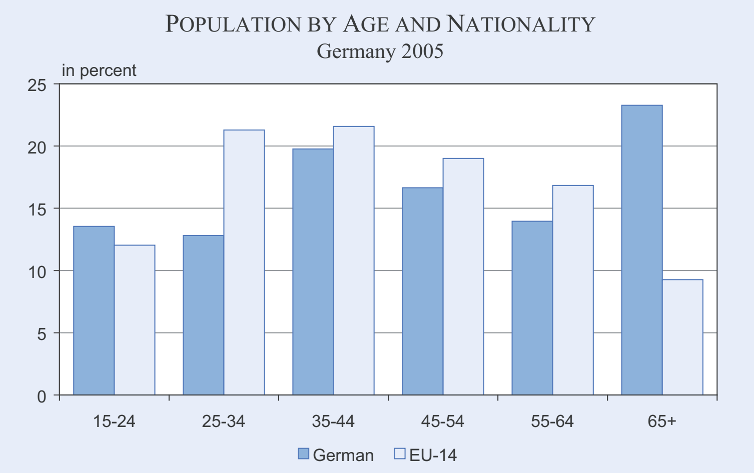
Nationals	Leaving	Arriving
Italian	27,118	18,349
French	10,354	12,260
Greek	16,391	8,975
Dutch	5,479	10,088
UK	7,864	7,853
Spanish	8,185	7,147
Portuguese	6,912	5,010

Source: Federal Statistical Office Germany.

Especially nationals from the traditional labour exporting countries such as Greece, Spain, Italy and Portugal exhibit a negative net migration, while a clear net gain in migration is noted with regard to nationals from France and the Netherlands. However, our own calculations using data from the Federal Statistical Office of Germany show that even though there is a slight increase in the inflows of EU-14 nationals to Germany for the year 2005, the overall flows still represent a net loss in migration.

Besides observing these trends in migration flows and stocks, it is imperative to determine further their disaggregated composition. Only a closer look at the individual characteristics of migrants would allow an assessment of their likelihood of being or becoming welfare migrants. First, the age structure of migrants can provide valuable insights both into their potential labour market performance (i.e. the younger they are the more motivated they should be) and their prospective dependence on social benefits (e.g. old-age pension). When looking at the age structure of EU-14 nationals in Germany in 2005, one can easily observe that the majority is fairly young. Whereas for the categories "under 25 years" and "above 65 years" the figures for EU-14 nationals are below those for Germans, EU-14 nationals are over- represented in the working age categories. As far as the age category of 25 to 34-year-olds is concerned, the figure for the EU-14 nationals is considerably higher than that for Germans. Given that the number of migrants aged below 25 is relatively small, no major additional education-related costs are to be expected.

Figure 2



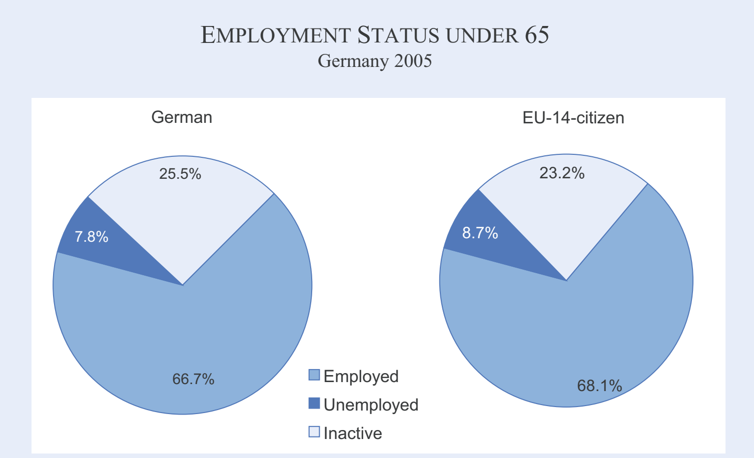
Source: LFS; own calculations.

EU-14 nationals present in Germany in 2005 were fairly young and well-represented in the working age categories of 25–54 years, with a particularly high share in the age group of 24 to 34 years. Finally, nationals from EU-14 countries display high employment levels, which are even slightly higher than those of Germans.

Secondly, the employment status of EU-14 nationals under 65 years in comparison with Germans of the same age is an important indicator for determining their likely dependence upon social benefits. A total of 68.1 percent of the EU-14 population present in Germany in 2005 was employed, while the equivalent figure for Germans was 66.7 percent. Their unemployment rates seem to be slightly higher than those of Germans, but this is also a result of their higher participation rates in the labour force.

In general since the early 1990s there has been a constant trend towards a net loss in migration of EU-14 nationals to Germany, a trend that reached its height in 2004. For 2005, the overall migration level of EU-14 nationals was still negative, even though a slight upward trend was observed. Net loss migration figures were particularly high for nationals from Italy and Greece in 2005, both of which are countries with relatively unattractive social welfare systems.

Figure 3



Source: LFS; own calculations.

Welfare tourism to Sweden?[1]

Together with Ireland and the UK, Sweden did not introduce the TAs in the context of the EU-enlargement to Central and Eastern Europe. It allowed the free movement of workers and was the only country to grant unrestricted access to its social welfare system. This unlimited access to the welfare system could have theoretically resulted in an increase in welfare tourism; however, this has not proven to be the case.

First results indicate that immigration to Sweden from the ten new Member States did not become an uncontrolled flood. Data on residence permits for work purposes show that the number of EU-10 citizens increased from 3,800 in 2003 to 5,200 in 2004. Numbers have since decreased to 4,500 in 2005. The data are not fully comparable; however, the general trend is clear: inflows have been very moderate and even declining.

Furthermore, fears of welfare tourism did not materialise, as utilisation of social welfare benefits so far has been very limited.

Under EU Regulation 1408/71, which aims at fostering the free movement of persons between the Member States, any person entitled to family benefits in any EU Member State has a right to benefits for his/her family members even if these live in another Member State. These family benefits include benefits for children and parenthood, housing allowances as well as study allowances.

[1] This section is based on a recent publication by Tamas and Münz (2006).

In practice, any EU citizen working in Sweden could export these benefits to his/her family members living in another EU Member State. A report covering the period from March to December 2004 found that the possibility of exporting social benefits to the ten new Member States had only been used to a very limited extent. Rather, social family benefits for families with children were more commonly exported to the Nordic countries.

As commissioned by the Swedish government, the Unemployment Insurance Inspectorate presented quarterly reports on EU certificates from each Member State that involve payment of Swedish unemployment insurance coverage. The quarterly reports for the third and the fourth quarter in 2004 indicated only low levels of usage. Among 800 applications to export unemployment insurance, only four involved a new Member State in the third quarter, and nine out of 740 in the fourth quarter.

Moreover monitoring measures were also directed at social security benefits in accordance with the Social Services Law. A report presented in 2005 noted that, as of September 2004, there had been no significant increase in utilisation of such social benefits since enlargement (Tamas and Münz 2006). Therefore, concerns about a potential abuse of the social welfare system – Sweden acting as a magnet for social tourism – were unfounded.

Immigration and public finances[2]

When examining the social welfare effects of migration, it is useful to have a closer look at the literature on the impact of immigration in general – i.e. including third-country nationals.

The European experience with immigrants' contribution to the public coffer is mixed. In a number of countries such as Austria, Belgium, Denmark, France, the Netherlands and Switzerland immigrants are apparently more dependent on the welfare system than the native population. However, in several other countries, such as Germany, Greece, Portugal, Spain and UK, immigrants make a similar or even higher contribution to the treasury compared to natives (IOM 2005).

[2] This section is primarily based on a new study by Münz et al. (2006). See also similar conclusions in Diez Guardia and Pichelmann (2006).

A Home Office study calculated that immigrants make a positive net contribution to the UK economy (Gott and Johnston 2002). It estimates that in 1999/2000 immigrants in the UK contributed US$ 4 billion more in taxes than they received in benefits. Furthermore, if intergenerational considerations are taken into account, the contribution made by immigrants may be higher since second generation immigrants, i.e. children of immigrants, are likely to be net tax payers.

Germany has had very large immigrant inflows, including ethnic Germans from Central Europe and CIS countries, labour migrants, asylum seekers and family members joining spouses or parents already living in this country. Germany also has a progressive tax structure and rather generous welfare provisions. Thus, the immigrant fiscal transfers ultimately depend on immigrant employment opportunities, given rigid labour markets (Bevelander 2000). A recent ILO study stressed that 78 percent of immigrants in Germany are of working age and, thus, an average immigrant makes a positive net contribution, up to EUR 50,000 over his/her lifetime (ILO 2004).

The latest study on the share of immigrants' contribution to the public coffer, published in October 2006, concludes that immigrants contributed on average EUR 1,840 more to the tax and social security system in Germany in 2004 than they received in benefits. If calculated on the basis of the 15 million people in Germany with a migration background (including foreigners, naturalised migrants and persons who have migrant ancestors), the surplus would be even higher, given that naturalised migrants and persons who have migrant ancestors are generally better educated and integrated than more recent migrants (Bonin 2006).

The Swedish example highlights how public transfers to foreign-born persons are sensitive to two key determinants: education and residence status. For example, if refugees in Sweden had had the minimum (or compulsory) level of education in 1992, then their public finance transfers would have been negative for almost their entire life. On the other hand, if the Swedish foreign-born residents had been admitted as non-refugees with university education, then the public finance transfers would have exceeded the average Swedish-born contribution by a three-fold margin. However, the refugee portion of the Swedish population did not result in a positive transfer, and this led to calls for a limitation in the admission of foreign-born persons in general (DeVoretz 2006).

Another example shows that the specific skill and origin structure of the immigrants in Spain resulted in positive effects both economically and for the social security system (OECD 2003). EU foreigners who bring capital with them (usually elderly British, Dutch and German pension receivers) increase demand, e.g. real estate prices grew by 30 percent per year for the period 1995-2001. They also contribute through direct and indirect taxes. The highly skilled pay relatively high income taxes, while they are often accompanied by investment flows, require less per capita spending and have limited claims to the Spanish pension and social security system. This is partly the case also with temporary workers, who are net contributors to the treasury in the short run.

In Italy, successive regularisation programmes have resulted in very large numbers of legalised immigrants joining the formal sector, thus widening the tax base and enhancing social security revenue (OECD 2005).

Different studies mentioned here used different methodologies, i.e. in the benefits and contributions considered, the area of analysis, and in the way the value of the services provided was calculated. However, the size and direction of the public finance transfers clearly depend, first of all, on the characteristics of the immigrants: education and skills, age, family status, and countries of origin. Second of all, public transfers towards migrants seem to depend also on their mode of entry and on the access to the educational system and the labour market, the recognition of qualifications and skills, and thus on the integration policy of the receiving country. Accordingly, the employment rates of EU-15 nationals in other EU-15 countries are high (as already shown for the case of Germany). The average employment rate within the EU is 67.0 percent: 73.6 percent for males and 60.4 percent for females (Münz et al. 2006).

A question of immobility

Compared to the United States, Europe is characterised by relatively low rates of mobility of people. As far as intra-EU mobility is concerned, this pertains to occupational and geographical movements within as well as between the EU Member States (European Commission 2002). This is also the case with regard to the East-West migration patterns. There have been many econometric studies forecasting the East-West migration potential. Independent of the methodology, this research tends to show a long run migration potential in the range of two to four percent of the source populations. Cumulated over 15 years this is about three million people, or about 1.2 percent of the working-age population of the EU-15 and certainly not enough to affect the EU labour market in general. However, some countries and regions in Germany and Austria could face some short-run adjustment problems and labour market disturbances (Diez Guardia and Pichelmann 2006, 16).

Nevertheless, from a more long-term perspective, it remains the case that less than two percent of Europeans currently live in a country other than their own. The phenomenon of immobility has traditionally been explained by high transport and transaction costs or institutional obstacles and risk adversity. While transport and transaction costs have been falling and progress has been made in the EU to remove obstacles to migration, internal movement rates have had a tendency to decrease substantially since the late 1960s and 1970s, and mobility between the EU Member States is still low.

An alternative approach to explaining immobility is what we call the *Insider-Advantage Approach* (Fischer 1999). This approach stresses that during periods of immobility at a particular location individuals invest in the accumulation of location-specific skills, abilities and assets. Here, we differentiate between insider advantages according to their origin (work- or leisure-related) and specificity (firm-, place- or society-specific).

Place-specific advantages make the individual particularly attractive for all or at least some firms in his/her region of work. Examples of such insider advantages are expertise in the location-specific preferences, desires and habits of clients or insider knowledge of the peculiarities of the political situation in a region. Society-specific advantages broadly emanate from the social relations and political activities an immobile individual builds up within the society in which he/she is residing (lobbying, political networks). Examples of leisure-oriented place-specific insider advantages can range from information about the "good-value-for-money" Italian restaurant to knowledge about the cultural events and the local housing market. Society-specific leisure-oriented insider advantages capture the utility increase a decision-maker and his/her family get from having friends, being socially integrated, accepted and active at a certain place of residence. These insider advantages result from a locational investment in social capital that encompasses a wide range of human contacts, from family relations and friendships to membership of clubs and political parties. Mobility generally leads to a loss of most of these assets and requires new investments in obtaining a "ticket to entry" at a new place of residence (Fischer et al. 2000).

The empirical experience of the old EU clearly shows that people's social and cultural ties to their local environment are an important obstacle to intra-EU migration. Most people want to live, work and stay immobile where they have their roots. People usually prefer the status quo to an unfamiliar or insecure change. The simple abolishment of legal impediments to migration is usually insufficient to overcome individual (microeconomic, social and cultural) obstacles to migration and to overshoot the value of immobility. Intra-EU labour migration has proved to be mainly demand-determined: it usually depends to a major extent on the needs and employment opportunities in the immigration countries.

In the EU, trade has reacted much faster and more elastically to economic integration than labour. The removal of formal and informal protectionist obstacles led to a strong increase in intra-community trade. The equalisation of good and factor prices expected on the basis of the neoclassic Heckscher-Ohlin-Samuelson international economic theory thus materialised through trade rather than through the increased mobility of labour. To an important degree, trade has so far replaced the economic demand for internal migration in the EU.

It might be that empirical evidence from the previous lifting of mobility restrictions does not apply to the EU enlargement to the East. However, we believe that we have good theoretical arguments (i.e. the neoclassical trade theory of the Heckscher-Ohlin-Samuelson models and their factor-price-equalisation-theorem) and strong empirical evidence that again, as in all the years before, the improvement in the standard of living in Eastern Europe due to full EU membership will invoke a very effective anti-migration impact. Rather sooner than later, the intra-EU migration of relatively poorly qualified workers might follow a migration substituting the neoclassical Heckscher-Ohlin-Samuelson pattern. Trade and capital flows will more or less replace the need for strong migration flows of rather unskilled workers. It is cheaper to move standardised products and machines than people. However, the migration of relatively highly qualified workers might follow the Ricardian (or New Growth) pattern of a self-feeding, dynamic core-periphery process. People with skills and knowledge might go to the centres that make them more attractive for capital and skilled workers in a next round. Rich agglomerations and poor periphery regions might be the long-term consequence. Thus welfare tourism might then be the end but certainly not the beginning of an intra-EU mobility story.

Conclusions

This paper has briefly reviewed some available evidence and noteworthy arguments as to why the European Union Directive 2004/38/EC is unlikely to change the current intra-EU mobility patterns significantly or to boost the welfare migration of EU nationals. The evidence presented revolves around two general observations. First, EU citizens have been rather immobile until now and migration between EU Member States has not yet become a means of stabilising asymmetric shocks in Europe. Second, the observed migration flows are mainly triggered by labour market conditions, such as income differentials or higher unemployment rates, especially in the regions of origin. Therefore, EU nationals changing their residence inside Europe are a positively selected group both in terms of their personal characteristics (such as age or education) and of their labour market performance (participation and employment rates, as well as wages).

Moreover, the theoretical arguments for immobility discussed above make a continuation of these observed patterns, even after the full implementation of the Directive 2004/38/EC, the more plausible. Not only will Europeans stay predominantly immobile, but those who move are more likely to be attracted by differentials in economic conditions between regions than by the variation in welfare provision across countries. This is in line with predictions based on neo-classical migration models, which underline the self-selective nature of migration: only the highly motivated will have incentives to overcome mobility barriers, and they will choose among potential destinations by maximising the returns to their human capital. Higher wages, uneven income distributions and flexible labour market conditions are therefore more attractive for this group than welfare payments.

Finally, it is precisely the much debated case of migration from Eastern Europe following EU enlargement that provides one more rationale in our argumentation. Although some authors have used the higher propensity of East Europeans to migrate in order to predict a flood into those EU-15 countries which provide the more generous welfare benefits, a refined look at current patterns disproves this notion. While previous econometric studies found some small effects of welfare magnets on the migration decisions of EU-15 nationals, these are levelled out in the case of East-West migrants. Apart from income differentials and labour market conditions, there are particularly strong network effects and social interactions (like learning or herding) that determine the dynamics of migration flows and thus entirely offset any effects of variations in welfare institutions. However, the interaction between the social dynamics of migration choices and welfare provisions is not yet fully understood and will remain on the research agenda in the near future.

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