Beyond Levels: Immigration, Productivity, & Policy Design

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If Immigration Can Benefit the Economy, What is the Optimal Level?

The Economic Trade Off

- More workers leads to higher GDP (levels) but not necessarily GDP per capita

Living Standards: GDP Per Capita Matters

- Increase in L input: decreases (K/L) ratio: productivity pressures
- K investment can restore (K/L) ratio over time
- immigrants with higher average human capital than domestic population can generate increases in GDP per capita, even holding physical capital constant.
- Outcomes depend on
  - Capital deepening
  - Immigrant skill composition

If the goal is to improve living standards—what people experience day to day—then what matters is GDP per capita

But what if capacity can't keep up?

When Capacity Doesn't Keep Up

More People Leads to Demand for Housing and Infrastructure

- Housing supply adjusts slowly
- Infrastructure takes time to expand

Without investment, productivity—and GDP per capita—come under pressure

- Workers have less access to productive capital (decreasing K/L ratio)
- Labour not used efficiently
  - misallocated labour across locations
  - Longer commutes
- *Strain on public capital*: Congestion in transport and health systems reduces effective labour supply and human capital

GDP per capita can be rising—but if you can't get a hospital bed, it doesn't feel like living standards are improving.

Living standards depend on GDP per capita but also housing affordability and access to infrastructure and services

Immigration and Housing Costs

Causal Evidence Based on Shift Share IV

- Moallemi & Melser (2020): Immigrant inflow of 1% in local area leads to 0.9% increase in (median) housing prices
- Erol & Unal (2023): Local population inflow of 1% in local area leads to 0.5-0.7% increase in (median) housing prices
- Consistent with international evidence

Grattan Institute (2024): Cutting Migration has Modest Effects

- Permanent migration set at 160,000 annually would lower rents by 2.5% over 10 years
- Net overseas migration constant at 190,000, housing costs would be 4% lower and 6% lower if NOM were constant at 160,000

Grattan Institute (2018): Supply is the Key to Affordability

- Increase of 1% to housing stock, leads to house prices 1-3.5% lower
- Sustained 50,000 new homes each year for decade would lower house prices by 5-20%

Housing supply reforms have 3–5 times the impact of cutting migration.

Lower migration may ease housing pressure—but may reduce GDP per capita if it reduces productivity and scale

Why Immigrant Composition Matters

Higher skilled immigrants can raise productivity-not just labour supply

- ***Human capital deepening***: can generate increases in GDP per capita, even holding physical capital constant
- ***Skilled Labour-Capital Complementarity***: skilled labour raises marginal productivity of capital
- Skilled migrants raise ***innovation activity***
- Australian & International evidence: local inflows of skilled immigrants raise local innovation activity
  - Crown et. al (2020): increasing the share of foreign-born graduates increases local area patents
  - Hunt et. al (2010) for US and Blit et al (2020) for Canada

Immigration Policy drives GDP per capita

- Selection on skills (human capital)
- Retention policy (innovators, graduates)
- Supporting capital investment (capital-skill complementarity)

Does the current system achieve this? How to design the system to deliver better outcomes

Issue: Skilled Occupation Lists Are a Poor Selection Tool

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Permanent migration is being used to target short-run shortages—not long-run productivity

- does not necessarily select those with greatest potential for positive productivity spillovers and economic growth
- is a poor proxy for long run productivity and adaptability
- admits immigrants that would otherwise not be admitted under a (pure) human capital selection.

occupation lists do not necessarily reflect `skill shortages'

- skill shortages often defined at current wage levels, rather than reflecting `market forces'

High potential productivity immigrants are more occupationally mobile [Clarke (2026)]

- Occupational mobility converts potential into realised productivity

Occupation list may generate `perverse' selection :

- `most' skilled may not necessarily become the primary applicant
- occupation list contains less skilled male-dominated occupations and more skilled female dominated occupations

Migration program should focus on skills for success in Australian labour market (education; language skills, Australian employment, together with `settlement policy')

Issue: Underutilisation of Skills I

Retention Policy

Onward migration can have a considerable impact upon both the number of immigrants as well as the overall level of skill through selective onward migration.

- Low overall hazard of exit after 10 years but more educated immigrants more likely to leave
- higher hazard of exit for the most skilled immigrants associated with a greater hazard of exit to countries directly competing with Australia for skilled immigrants (Canada, North-West Europe, United Kingdom, and the USA).
- Potentially loosing the exact immigrants with the greatest potential for positive productivity spillovers, innovation
- Policy drives exit: out-migration flows not particularly sensitive to labour market conditions in Australia

Migration policy should enhance

- Faster and more certain pathways to PR
- Targeted retention of high skilled immigrants

Issue: Underutilisation of Skills II

Underutilisation of Skill of Secondary Applicants

- Many secondary applicants are highly skilled and educated
- Face limited access to occupations and credential recognition barriers (higher rates of over-education)
- Strong gendered effects: primary applicant women perform well in the labour market (employment) and are relatively better matched (lower rates of over-education)
- Reduced productivity associated with misallocation of (selected) human capital

Migration policy should treat households (couples) not individuals as units of selection

- Improved credential recognition pathways and skill assessments for secondary applicants
- Settlement policy for secondary applicants

Align Temporary and Permanent Migration

System misalignment

- Temporary migration driven by short-run demand by employers and universities, not necessarily selecting on long run potential
- Permanent migration (mostly) based on static occupation lists
- Weak link to long run productivity

Reform: Align PR with demonstrated contributions and long-run potential, not skill shortages. How?

***Differentiate onshore and offshore selection*:**

- Onshore: select on realised outcomes (employment, earnings)
- Offshore: select on long run potential (education, adaptability, innovation potential)
- ***Improve (skill) utilisation within households:*** better use of the skill of secondary applicants

Strengthen pathways from temporary to permanent: \`reward' contributions, not just entry characteristics

What Determines the Optimal Level of Immigration?

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Not just how many, but who, how and whether the system keeps pace

Human Capital

- (immigrant) selection matters
- Skill utilisation matters

Productivity and Innovation

- Retention and better matching of highly skilled immigrants

Capital

- Capital investment must keep pace: housing and infrastructure

Align migration with productivity and investment—not short-run demand

Immigration policy is not just population policy—it is productivity policy.