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Breaking out of poverty traps: Internal migration and interregional convergence in Russia [☆]

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ABSTRACT

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We study barriers to labor mobility using panel data on gross region-to-region migration flows in Russia in 1996–2010. Using both parametric and semiparametric methods and controlling for region-to-region pairwise fixed effects, we find a non-monotonic relationship between income and migration. In richer regions, higher incomes result in lower migration outflows. However, in the poorest regions, an increase in incomes results in higher emigration. This is consistent with the presence of geographical poverty traps: potential migrants want to leave the poor regions but cannot afford to move. We also show that economic growth and financial development have allowed most Russian regions to grow out of poverty traps bringing down interregional differentials of wages, incomes and unemployment rates. *Journal of Comparative Economics* xxx (xx) (2015) xxx–xxx. Sciences Po, Paris, France; CEPR, London, United Kingdom; National Research University Higher School of Economics, Moscow, Russia.

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1. Introduction

This paper is an empirical study of the barriers to labor mobility and of resulting geographical poverty traps. Labor mobility is one of the most important issues in economic development. Large differentials—both within and between countries—in incomes, living standards, productivity, public goods and other development outcomes imply high individual and social returns to migration (Human Development Report, 2009). However, the very fact that these differentials persist implies there are also substantial barriers to labor mobility. These barriers may be driven by high transportation, psychological or informational costs of moving. These costs are reinforced by the underdevelopment of financial markets. Even when returns to mobility exceed the costs of migration, potential migrants with low earnings and assets may not be able to finance their move. Essentially, these migrants are locked in geographical poverty traps.

An empirical analysis of such geographical poverty traps is a challenging task. By definition, we do not observe the actual costs of mobility for those potential migrants who cannot and therefore do not move. In order to quantify the barriers to

[☆] This paper is based on the background paper “Convergence Between Russian regions” for the World Bank’s Eurasia Growth Project.

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mobility, we need to estimate the change of migration in response to change in external circumstances that allows the breaking out of poverty traps at least for some potential migrants. This may involve a substantial decrease in migration costs, or progress in financial development, or an increase in income (keeping the moving costs constant).

In this paper we study interregional migration in Russia in 1996–2010 when both a breakthrough in financial development and rapid growth in income took place. Russia offers a unique setting for an empirical study of barriers to internal migration and of geographical poverty traps. First, it is a large and diverse country with a substantial potential for geographical labor reallocation. The initial allocation of labor at the beginning of the transition was far from the spatial equilibrium in a market economy. Before the 1990s, Soviet industrialization policies often pursued political or geopolitical rather than economic goals. Even when they reflected economic realities, allocation decisions were distorted substantially by central planning, price controls and subsidies. Not surprisingly, the transition involved moving millions of people between Russian regions. Second, Russia experienced a dramatic growth in incomes during the 2000s. According to the IMF data, Russia's GDP per capita in constant prices grew by 80% between 1996 and 2010.

We use a panel dataset of the gross annual migration flows between Russian regions in 1996–2010. We estimate the relationship between income at the origin region and gross migration flows controlling for region-to-region pairwise fixed effects, year dummies, income at destination, and time-varying characteristics of both origin region and destination region including population, provision of public goods, real estate market indicators and others. Controlling for pairwise fixed effects allows us to take into account the distance between origin and destination and other time-invariant variables that can affect the informational, cultural, or psychological costs of migration from region i to region j (e.g. due to historical affinity or differences in terms of language, religion, culture, or climate). Also, controlling for pairwise fixed effects automatically allows us to control for regional fixed effects, e.g. region i 's cultural or psychological propensity to move or region j 's attractiveness to migrants.

The presence of geographical poverty traps implies a non-monotonic relationship between the income at the region of origin and the migration outflows. If the incomes are low, financial constraints are likely to bind. Potential migrants with low income are willing to move but are unable to fund the costs of migration. Hence, the higher the income at the region of origin, the higher the migration outflows. On the other hand, for sufficiently high income, financial constraints are no longer important, and the effect of income on migration now works in the opposite direction. Indeed, controlling for income at destination, a higher income at home decreases the economic returns on migration.

In order to estimate a non-monotonic (hill-shaped) relationship between income and migration outflows, we use both semiparametric and parametric methods. We allow for a piece-wise linear and for a quadratic relationship between income and migration. All three approaches (semiparametric, piece-wise linear, and quadratic) deliver similar quantitative results. We find that the relationship between income and migration outflows is indeed hill-shaped; it peaks at about \$3000 per year (at 2010 exchange rate). We interpret the fact that the relationship is non-monotonic as evidence of the existence of poverty traps. We also argue that once incomes are above the threshold of \$3000 per year (which is true for almost all Russian regions in the late 2000s), financial constraints are no longer binding, so that the regions have broken out of these poverty traps.

While the relationship between migration and income is non-monotonic for income at origin, we find no such relationship between migration and income at destination. This is intuitive: income at destination has nothing to do with poverty traps. A higher income at destination is associated with higher migration. Moreover, consistent with standard predictions from migration theory (see, for example, [Moretti, 2011](#)), we also document that migrants tend to go from regions with high unemployment and worse public goods to regions with lower unemployment and better public goods.

We also run the estimations separately for subsamples of pairs of regions distant from and close to each other. We find that the non-monotonic relationship is driven by long-distance migration rather than migration to nearby regions. This is intuitive as costs of migration are likely to increase with distance. We also provide additional evidence using the data on the financial development of Russian regions. Unfortunately, these data are only available from 2001 (and some of the series start only in 2004). We find that financial development relaxes the financial constraints on mobility. In particular, the interaction term between the level of financial development and income has a negative effect on migration outflows. In financially developed regions, a higher income is more likely to have a negative rather than positive impact on migration. In other words, poverty traps are less likely to emerge in the regions with more developed financial markets.

Our empirical strategy assumes that while incomes push and pull migration flows there is no reverse causality. Migration could affect average income directly if the incomes of a large number of incoming or outgoing migrants were different from the region's average income. Essentially, we assume that differences in incomes are driven by local productivity shocks and that migration is too small to affect local labor market outcomes. While this assumption is often made in the literature on internal migration, it is especially likely to hold in our setting. Indeed, in Russia in 1996–2000, the average annual migration rate was only 0.5–1.0% of total population and therefore could hardly affect incomes and other socio-economic variables in the origin and destination regions. We also run a number of additional checks to rule out the effect of migration on incomes. In particular, we exclude regions with large cumulative net migration flows (above 10% or below –10% of population over fifteen years).

Our paper contributes to the literature on the effect of financial constraints on migration. The general theory of spatial labor allocation (see, for example, the survey in [Moretti, 2011](#)) predicts that migrants move from locations with lower wages, poorer amenities and expensive real estate to those with higher wages, better amenities and cheaper real estate. However, at least since the seminal paper by [Banerjee and Kanbur \(1981\)](#), the literature has suggested that in the presence of financial

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