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The hub continent. Immigrant networks, emigrant diasporas and FDI

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ABSTRACT

This paper studies the relations between bilateral FDIs and immigrant networks of France, Germany, UK, Italy and Spain, and the emigrant diasporas of Italy and Spain. It focuses on skilled and unskilled immigrants and on ties with developing and developed countries. Results evidence two different network models: FDIs of UK, Germany and France are prompted by the ties of skilled immigrants, while those of Italy and Spain are only influenced by their respective diasporas. The disparity may stem from history. Differently from the findings of previous literature, the effects of networks with developing countries are similar to those with rich economies.

Trust matters. Modern technology allows instant, cheap communication. Yet although anyone can place a long-distance call, not anyone knows whom to call, or whom to trust. Ethnic networks can address this problem. 'The hub nation', The Economist, Apr 22nd 2010

1. Introduction

From the mid nineteenth to the mid twentieth century, Western Europe has been a land of emigration, while more recently it has become a major destination area for international migrants. In modern history, no other part of the world has had such large and varied movements of populations, first outwards and then inwards. The question is, how does this affect the European economy, and more specifically, does it influence its market interactions with the rest of the world?

Since formal barriers to international economic exchanges have gradually come down over the last few decades, informal impediments have become apparent. Recent literature has shown that these informal barriers are due to social, cultural and institutional differences between countries, and have significant negative effects on transactions (Trefler, 1995; Obstfeld and Rogoff, 2000). A counteracting force that tends to lower these invisible barriers are the migrant communities, which typically build links between their origin and destination countries. More precisely, they develop transnational networks where information on opportunities concerning the origin and destination economies circulates more easily and efficiently than through the international price system (reviews are in Rauch, 2001; Wagner et al., 2002).

While the empirical research has focused especially on the influence of networks on international trade (a partial list includes Gould, 1994; Head and Ries, 1998; Rauch and Trindade, 2002; Blanes, 2006; Wagner et al., 2002; Murat and Pistoresi, 2009b; Tadesse and White, 2008), some studies have analysed their impact on foreign direct investments (FDIs) (Gao, 2003; Tong, 2005; Buch et al., 2006; Murat and Pistoresi, 2009a). Both lines of research have provided evidence in support of the basic hypothesis that migrant networks smooth international economic transactions. Based on this evidence, Western Europe should benefit from the transnational ties built by its immigrant and emigrant networks.

This paper addresses this issue by investigating the relationship between migrant networks and bilateral FDIs of five European countries – France, Germany, Italy, Spain and the UK – with the countries of origin and destination of immigrants and emigrants. It contributes to the existing literature in a number of ways. First of all, it considers not just immigrants but also the emigrant diasporas of two countries – Spain and Italy – that have maintained strong and

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traceable links with their nationals abroad. Secondly, it separately measures the effects of different groups of migrants, disaggregated along two main dimensions, the level of educational attainment (skilled and unskilled individuals) and the income level of the origin (immigrants) or residence (emigrants) countries. Finally, it takes into account the issue of exogeneity, which is often overlooked by papers on the topic.

The skills-based distinction arises from the observation that FDIs are by nature complex operations; especially when compared to trade, investments abroad involve a higher degree of complexity, more costs and risks, and are affected by larger informational asymmetries. We therefore hypothesise that higher levels of skills and educational attainment can be required to influence FDIs with respect to trade, and make a distinction accordingly. Among others, El Yaman et al. (2007), Javorcik et al. (2006), Docquier and Lodigiani (2009), Docquier and Rapoport (2007) and Kugler and Rapoport (2007) find evidence in support of this hypothesis.

An implicit assumption of networks theory is that for migrants to be able to influence economic decisions and international transactions, they must possess sufficient resources and reside in the destination country for a long enough period of time. Dunlevy and Hutchinson (1999) find that immigrants from the poorer countries of Europe did not exert the expected pro-trade effect on the USA bilateral trade during the late nineteenth and early twentieth centuries. They did not, in the authors' explanation, because of their lack of economic and social empowerment. Following this line of research, we split the stocks of immigrants and emigrants into OECD and non-OECD networks and separately test their effects on FDIs.

Our main findings are as follows. First: two main transnational network models seem to be at work. In one, concerning the UK, France and Germany, as expected, the links of immigrants prompt bilateral FDIs, while in the other, concerning Italy and Spain, FDIs are influenced by the diasporas' networks and immigrants have weak or nil effects. This disparity may follow from the past histories of international migration and economic expansion of the two groups of countries, one more based on colonialism, the other on labour emigration. To the best of our knowledge, these are novel results (on Italian FDIs, Murat and Pistoresi, 2009a). Second, the splitting of immigrant stocks into skilled and unskilled individuals reveals that when present, the influence on FDIs of networks mainly depends on their skilled members. Unskilled immigrants mostly have non-significant or even negative effects. This applies to the first group of countries, UK, Germany and France. These also are original results, which add evidence to the findings of the literature cited above on skilled immigrants and FDIs. Third, differently from the results of Dunlevy and Hutchinson (1999), the influence of immigrants from less developed countries is as strong as that of immigrants from richer economies. The same holds for emigrants. This may be due to investment's decisions abroad being more sensitive than trade to the information provided by individuals with an effective control over resources, be they skilled immigrants or well-established members of the diaspora. In our data, the latter are first, second and third generation emigrants whose income levels, especially in the non-OECD group of countries, often are above average. Finally, in most cases endogeneity concerns are ruled out, FDIs appear to be caused by networks and not vice versa.

The paper is structured as follows: Section 2 presents the main issues and the descriptive statistics; Section 3 describes the empirical model; Section 4 illustrates the data; Section 5 shows the main results of the regressions and in Section 6 we offer our conclusion. Appendix A contains the list of partner economies considered in each dataset, while Appendix B contains the detailed regressions for each country.

2. Migrant networks, diasporas and investments abroad

Western Europe has a relatively short history of immigration. It became noticeable in the UK, France and Germany as of the Fifties and Sixties in particular, and has rapidly increased since then. Initially, immigrants arriving into the UK were mainly from the Commonwealth, those arriving into France were mainly from Southern Europe and the former colonies, and those arriving into Germany were mainly from other European countries and the Middle East. Immigration in Italy and Spain is a more recent phenomenon, but it has grown so rapidly over the last two decades that the share of immigrants in terms of the overall population is now quite significant.[1] Today, Western Europe attracts migration from all over the world.

Table 1 contains some descriptive statistics, based on the data used in our empirical analysis, related to the latest census year in each country. Among the countries we investigate, Germany has the biggest immigrant community, with almost 6.4 million individuals, while Italy has 1.1 million. The country with the highest number of skilled immigrants is the UK, with nearly one million highly educated immigrant individuals, representing 33% of the foreign-born population. Italy, on the other hand, has only around 123,000 skilled immigrants, making up 13.8% of the immigrant population.

When we disaggregate immigrants according to their country of origin's membership to the OECD, we see that in France and in the UK, the immigrants' native countries are equally divided into OECD members and non-member states. Germany has the largest OECD share, while the opposite occurs in Italy and Spain, where non-OECD immigrants are the vast majority. Less than 10% of the latter are highly skilled, in Italy. Conversely, the share of skilled individuals among the immigrant population from non-OECD countries in the UK is more than three times as high.

Emigration from Europe occurred in the past. For about a century and until World War II, people from the UK, France and Germany emigrated following their countries' colonial and economic expansion abroad.[2] Mass migration from Italy and Spain, on the other hand, occurred because of the lack of work opportunities at home. It mainly took place between 1870 and 1970 in Italy, while in Spain it persisted until the 1980s, at which point it gradually subsided (Del Boca and Venturini, 2005). Unlike the former three countries, Italy and Spain have built and still maintain close links with their diasporas. Emigrants and their offspring can maintain citizenship of their home countries and hold the right to vote in parliamentary elections. Also, since 2006, Italian emigrants have their own parliamentary representatives. The governments of both countries keep detailed official records of the diasporas, which include the years of registration of emigrants and their progeny in each foreign country of residence. The use of these data makes this paper's analysis on emigration feasible.

Regarding any potential correlation between immigrant and emigrant flows, the data show that they are independent variables through both time and space. As depicted in Table 1, 78.5% of Italians abroad reside in OECD countries, while 18.1% immigrants are from the OECD; 46.2% of Spanish emigrants are in OECD countries, while 25.2% immigrants are from OECD). The correlation

[1] Foreign individuals represent the 5.6% of the total population in France, 8.2% in Germany, 4.6% in Italy, 9.5% in Spain and 5.2% in the UK (OECD International Migration Outlook, 2005).

[2] Emigration from the three countries had different characteristics. People that permanently emigrated from the UK during the last centuries have mostly merged with the host country populations. At the other extreme, the existence of old German communities abroad is still quite perceptible but their institutional links with the homeland are weak. The same applies to French emigration, with the further difference (relatively to the first two countries) that it was never a mass movement (Sowell, 1996).