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Entry Earnings of Canada's Immigrants over the Past Quarter Century: the Roles of Changing Characteristics and Returns to Skills

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Abstract

We examine whether the factors associated with the rise in the Canadian born - immigrant entry earnings gap played different roles in the 1980s, the 1990s, and the early 2000s. We find that for recent immigrant men, shifts in population characteristics had the most important effect in the 1980s when their earnings gap expanded the most, but this “compositional” effect diminished in the 1990s and early 2000s. The effect of changes in returns to Canadian experience and education was small for men, but stronger for women in all three periods. During the early 2000s the IT bust, combined with a heavy concentration of immigrants in IT-related occupations, was the primary explanation of the increase in their earnings gap. Furthermore, returns to foreign experience declined in the 1980s and 1990s, but recovered moderately in the early 2000s. In contrast, the relative return to immigrant education declined in the early 2000s.

Keywords: Immigrants, entry earnings, decomposition, Canada

JEL Code: J31 and J61

Executive Summary

Many studies have documented the deteriorating labour market performance of recent immigrants since the late 1970s. This deterioration has continued despite the improved macro-economic condition in the early 2000s and increases in the educational attainment of immigrants. A considerable amount of research has focused on factors associated with this deterioration, including changes in immigrants' source regions and socio-demographic composition, a broad deterioration in labour market outcomes for new labour market entrants, and declining returns to foreign work experience. However, no consensus has been reached regarding the relative roles of these factors and whether their effects have changed over time.

In this paper we intend to contribute to the literature in three ways. First, we update the research on the factors associated with the decline in immigrant entry earnings by using the most recent census data. Secondly, we examine the varying impact of compositional shifts and changing returns to skills (education and experience) on the entry earnings gap for recent immigrants *separately* for three distinct periods, the 1980s, 1990s, and early 2000s. The third contribution is methodological. We use a flexible model specification that can simultaneously capture the effect of a host of potential variables, reflecting both compositional shifts and changes in returns to various characteristics, on changes in the entry earnings gap. We also use a decomposition technique that takes into account possible overlapping effects of various explanatory factors.

We found that changes in population characteristics were the dominant factor affecting immigrant entry earnings gap during the 1980s. Of the three decades, this one witnessed the largest increase in the unadjusted earnings gap, at least for men, driven largely by a significant shift in immigrant source regions. Among male immigrants, the effect of such "compositional" shifts became trivial in the 1990s as rapidly rising education and continuing shift in immigrant source regions offset each other. In the early 2000s, the effect of compositional shifts on the gap was reversed; they tended to reduce the gap. For women, like males, the effect of compositional shifts was greatest during the 1980s, and then fell continuously through the 1990s and early 2000s.

We also found that the effect of changing returns to Canadian experience and education on immigrant entry earnings gap was generally small for immigrant men, particularly in the 1990s and early 2000s, but was stronger for immigrant women in all three periods. Rapidly rising returns to education, which were observed among both entering immigrants and the Canadian born over the 1990s, was actually in favor of immigrants. This is because the educational attainment of entering immigrants was rising much faster than that of the Canadian born, and as a result recent immigrants benefited more from the rising relative returns. For female immigrants, the effect of changing return to education on their entry earnings gap was generally small.

Rising returns to Canadian experience accounted for about one fifth of the expansion in the recent immigrant men's earnings gap in the 1980s, but the effect became trivial in the 1990s and tended to reduce immigrant men's earnings gaps in the early 2000s. For recent immigrant women, the large rise in the return to Canadian experience was among the most important factors contributing to their widening earnings gap throughout the whole study period. This large increase in returns to Canadian experience of course benefited the Canadian born more than entering immigrants, since they have much more Canadian experience.

We showed that it is difficult to directly estimate the effect of changing returns to foreign experience and immigrant education on the immigrant entry earnings gap. Like several earlier studies, we find that there was a decline in returns to foreign experience in the 1980s and 1990s. However, since changing composition and changes in returns to Canadian experience and education accounted for the vast majority of the increase in the gap for immigrant men, and all the changes for immigrant women over the 1980s and 1990s, it seems unlikely that changing returns to foreign experience played a large role. During the early 2000s, returns to foreign experience recovered marginally. However, returns to immigrant education fell significantly during this period. Therefore, changing returns to immigrant education seems a more likely explanation of the rise in the "unexplained" gap during the 2000s.

In the early 2000s the IT bust, combined with large concentration of male entering immigrants in this industry, appears to be the major explanation for the rise in their earnings gap. The IT downturn was also likely the primary reason for the large decline in the relative return to higher education among entering immigrants in this period.

By focusing the research on three distinct time periods, and observing the changing effects of major explanatory factors, the research paints a less pessimistic picture about the labor market performance of Canada's recent immigrants in the recent past. The largest increase in the gap was observed during the 1980s, driven largely by compositional shifts, most of which abated during the 1990s, and certainly by the 2000s. The shifts in immigrant source regions and language ability have stabilized and may not negatively affect trends in immigrants' earnings gap in the near future, barring some possible significant change in immigration patterns. Changes in returns to Canadian experience and education played a moderate role in the 1980s, but its effect has become small, at least for the earnings gap of recent immigrant men. The reason for the expanding earnings gap is unique in the early 2000s when the downturn of a single industrial sector (IT) affected a substantial share of recent immigrants. A similar event may not be repeated, although it remains to be seen what effect the recent recession of 2008-09 had on immigrants' relative earnings.