

# Skilled Immigration, Firms, and Policy\*

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## Abstract

This paper studies the macroeconomic general equilibrium effects of skilled immigration policy changes by explicitly taking into account the role of firm demand for foreign skilled labor. To this end, I develop a two-sector dynamic stochastic general equilibrium model with monopolistically competitive firms and heterogeneous workers. Unlike most previous studies that view immigration as a supply-induced shock, the paper models skilled labor immigration as an endogenous response to an increase in firm labor demand in the receiving economy. The model is calibrated to mimic the U.S. economy with its current immigration policy: Firms face hiring costs and there is an occasionally binding cap on the foreign skilled workers that can be hired each period. The results indicate that a less restrictive skilled immigration policy via an immigration cap increase leads to heterogeneous effects on skilled and unskilled workers — unskilled domestic workers gain but skilled domestic workers lose. However, the magnitude of the welfare impacts depends on the state of the economy at the time of the cap change and also on the structure of the labor market (presence of search frictions). This paper also evaluates the welfare and efficiency gain from moving toward an alternate skilled immigration policy with a market-driven allocation of permits for hiring skilled foreign workers. Such a policy increases welfare and brings the economy's allocation closer to the social planner's first-best allocation.

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