

# Remittances and Development

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Winds of Change: New Ideas in International  
Development

# A Road Map

- Remittances and development
- Contrast: Foreign aid
- Questions:
  - What are the similarities and differences?
  - What are the impacts on economic development?
  - What can we learn from these two phenomena?

# Remittances

- Remittances: transfers of money by foreign workers to their home countries:
  - About 200 million migrants send money back home
  - Around 1 billion recipients across the globe
  - An estimated \$300 billion was sent last year—nearly three times all public foreign aid budgets combined
  - The total amount has doubled in the past five years

# Remittances Compare to...

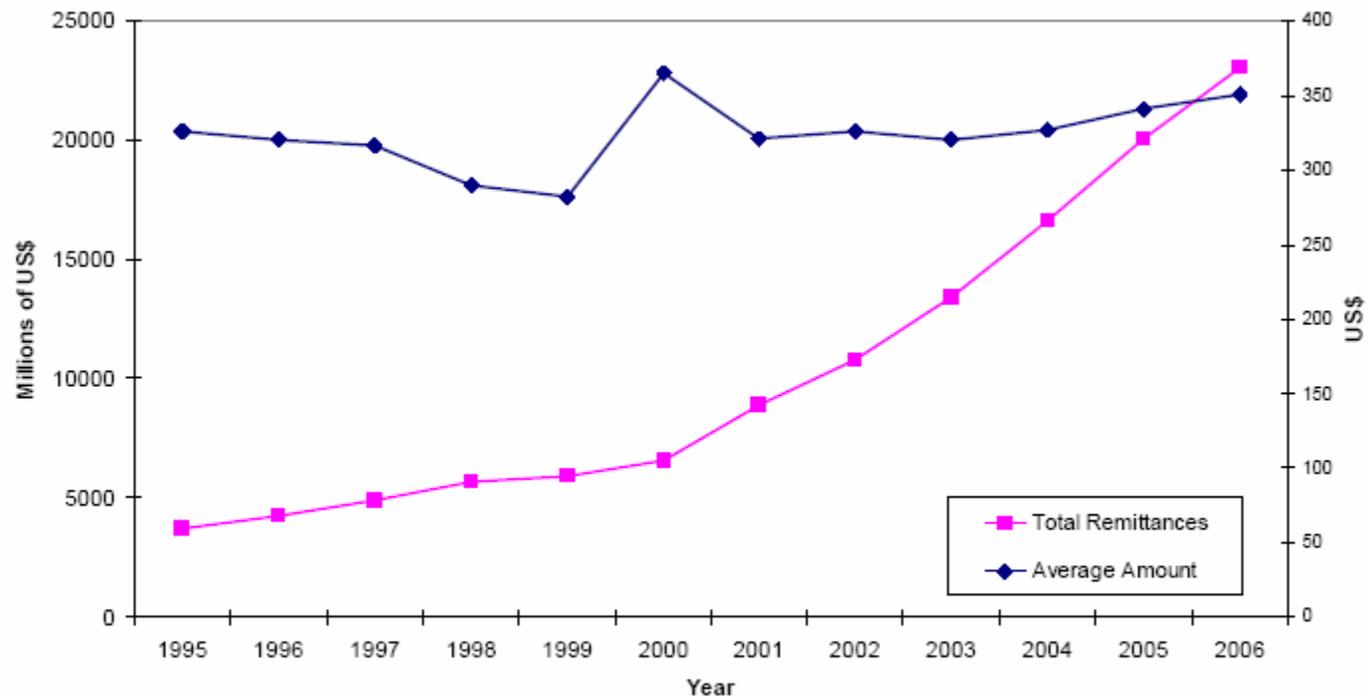
Private Remittances per Dollar of		
	Official Foreign Aid	Private Foreign Investment
Low income Countries	\$1.29	\$2.58
Lower middle income countries	\$3.59	\$0.76
World	\$2.61	\$0.36
India	\$31.43	\$4.07
Mexico	\$149.86	\$1.04
Morocco	\$5.98	\$5.49
Philippines	\$25.14	\$24.81

Source: Bernard Wasow, The Century Foundation

# Magnitudes and Importance

- Top receivers in 2006: India (\$25 billion), China (\$24 billion), and Mexico (\$24 billion)
- In 22 countries, remittances exceed a tenth percent of total GDP: Moldova (32 percent), Haiti (23 percent) and Lebanon (22 percent)
- Yet, studies are relatively recent
- The Mexican case

# Total Remittances and Average Amount of Remittance, 1995-2006



Source: Banco de Mexico, "Remesas familiares," Balanza de pagos, available at <http://www.banxico.org.mx/polmoneinflacion/estadisticas/balanzaPagos/balanzaPagos.html>, accessed 02/14/07.

# Composition of Remittance Flows to Mexico, 1997-2006

	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Total Remittances (millions of \$US)	4864.9	5626.8	5909.6	6572.8	8895.3	10749.0	13396.2	16612.9	20034.9	23053.8
Money Orders	35.5%	33.2%	24.5%	21.8%	9.0%	7.4%	12.1%	11.3%	9.3%	5.9%
Personal Checks	1.6%	1.1%	0.9%	0.1%	0.1%	0.1%	0.0%	0.0%	0.0%	0.0%
Electronic Transfers	54.2%	57.8%	66.6%	70.6%	87.5%	89.3%	85.9%	87.3%	89.3%	92.6%
Cash and In-kind	8.6%	7.9%	8.0%	7.4%	3.4%	3.2%	1.9%	1.4%	1.4%	1.5%

Source: Banco de Mexico, "Remesas familiares," Balanza de pagos, available at <http://www.banxico.org.mx/polmoneinflacion/estadisticas/balanzaPagos/balanzaPagos.html>, accessed 02/14/07.

# Mexico Remittances Facts: IADB and Banxico Surveys

- Twenty-five percent of recipients are concentrated in five Mexican states: Guanajuato, Jalisco, Michoacán, San Luis Potosí, and Zacatecas
- Michoacán was Mexico's top receiving state, with nearly \$2.5 billion
- Recipient households are predominantly poor: 73 percent are at the bottom three income quintiles
- 60 percent are females

## Mexico Remittances Facts: IADB and Banxico Surveys

- 54 percent of senders were either brothers or sisters (34 percent) or sons or daughters (20 percent) of the recipients. Only 27 percent of senders were spouses or parents
- In 2006 almost \$1 billion was used for “property acquisition” or “property renovations.”
- 14 percent of survey respondents said they use part of the money for savings and five percent reported using remittances for business operations
- 13 percent of recipients reported using some of the resources on education expenses.

# Remittances Empirical Evidence

- Research challenges: Data, Diversity and Causality
- Remittances are important for basic consumption
  - Effects on poverty rates: extreme poverty headcount is reduced by 39.9 percent and moderate poverty is reduced by 15.5 percent
  - Related economic effects on small communities
  - The big numbers effect: If 80 percent of the money sent to Latin America is spent on consumption, that leaves nearly \$12 billion for investment.

# Remittances Empirical Evidence

- Remittances increase school attendance and decrease employment of school age children
- Remittances help with home acquisition and home improvements
- Remittances have a modest positive effect on domestic investment
- Remittances have a modest positive effect on savings

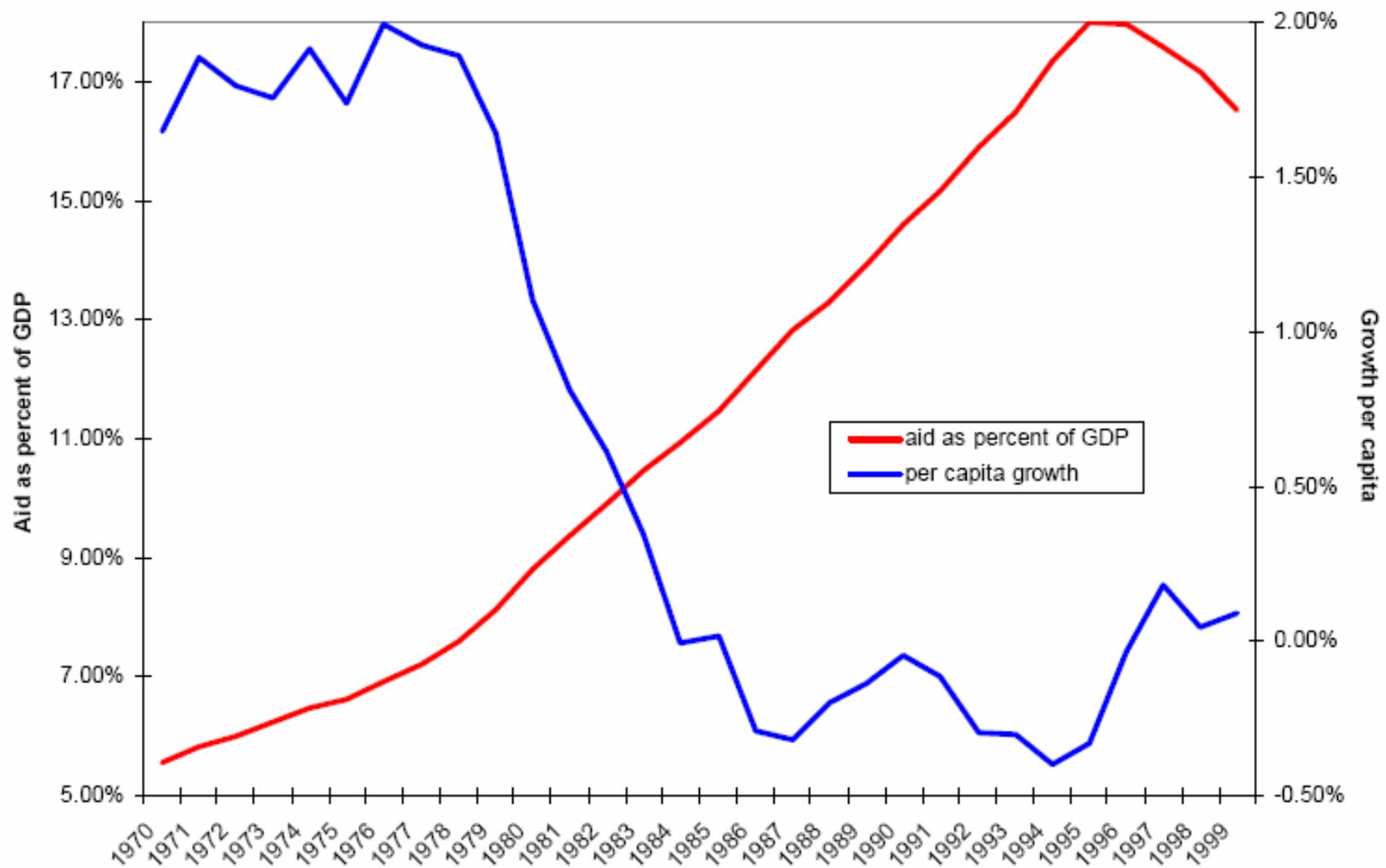
# Remittances Empirical Evidence

- Remittances increase the foreign exchange reserves, thus reducing government borrowing costs
- Remittances can also:
  - support an overvalued exchange rate
  - stimulate consumption and leisure while discouraging work.
- But, compare to what?

# Foreign Aid Facts

- Sub-Saharan Africa:
  - Official development assistance and official aid to SSA from 1980 to 2003 was \$345 billion
  - Subsequent debt forgiveness program for about \$40 billion
- More than 50 percent of Africans suffer from water-related diseases such as cholera and infant diarrhea
- More than 40 percent of women in Africa do not have access to basic education
- Economic growth?

Figure 2: Aid and growth in Africa (10-year moving averages)



# Foreign Aid Empirical Evidence

- Little, if any, evidence of a robust positive impact of aid on growth.
- No evidence that aid works better in better policy or institutional or geographical environments.
- No evidence that certain kinds of aid work better than others.
- Implication: Need to reconsider the way aid programs work.

Rajan and Subramanian (2005)

# Remittances vs. Foreign Aid: What is Different?

- Human connection
- Incentives: rewards and performance
- Evaluating progress
- Knowledge problem: needs and goals
- Transaction costs
  - International bureaucracy
  - Implementation and its challenges
- Accountability and corruption
- Economic related impacts
- Sending ideas back home

# Policy implications

- Economic prosperity requires:
  - Strong rule of law
  - Sound economic policies
  - Political stability
  - An independent judiciary system
  - Strong private property rights
  - Etc., etc.
- Remittances and foreign aid are not and cannot be a substitute for these important elements
- However there are some important lessons...

# Policy implications

- The importance of incentives
- Immigrants from poor and developing countries can be highly productive and prosperous
- No cultural, social, or historical factor can fully abolish the entrepreneurship spirit of free individuals facing adequate incentives:
  - Since 1997, the number of Hispanic-owned companies grew 82 percent; the fastest growth in the United States.
  - In 2006, Hispanic-owned businesses generated almost \$300 billion in annual gross revenue. Estimates suggest that by 2010 this figure will be more than \$450 billion

# Policy Implications

- Remittances phenomena will continue, given that the current cycle is:
  - Aging industrial economies need workers
  - People in poor countries need jobs
  - Moving is easier and cheaper
  - There are potential economic gains for both parts
- “Trade not Aid” may become “Immigration not Aid”