



**The Political Economy of Remittances:
What Do We Know?
What Do We Need to Know?**

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THE POLITICAL ECONOMY OF REMITTANCES: WHAT DO WE KNOW? WHAT DO WE NEED TO KNOW?

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Abstract

Private remittances are becoming an increasingly important part of the financial landscape of many developing countries. Indeed, for some such countries, these flows are the single most important type of international capital inflow—public or private—and they have become an importance source of purchasing power and foreign exchange. The growing importance of remittances has stimulated a great deal of discussion among scholars and policymakers. However, most studies tend to be rather narrow and microeconomic in scope, and fail to understand remittances within a broader political economy context. This contrasts with studies of other international capital flows such as official development assistance, direct foreign investment, private bank loans, and portfolio investment where political economy concerns have long been a central concern. This paper draws together findings from the rapidly growing multi-disciplinary study of remittances; identifies what we know, what we do not yet know, and what we still need to know about their economic, political and social consequences; and argues that there are a range of important political economy concerns raised by these flows. The paper concludes that the political economy effects of remittances are complex, contradictory, and not amenable to generalizations across the developing world, and that there is still much that we need to know about them.

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1. INTRODUCTION

Inflows of private remittances are becoming an increasingly important part of the financial landscape of many developing countries and, indeed, of entire regions. In 2007, recorded inflows of remittances to developing countries are estimated at US \$251 billion [World Bank (WB-DPG), 2008]. For developing countries as a whole, remittance inflows in 2007 dwarfed inflows of official development assistance (ODA), and were about half as large as both net inflows of foreign direct investment (FDI) and private debt and portfolio equity. In many countries, remittances outstrip ODA, net exports, tourism receipts, and FDI. Remittances are less volatile than other international private capital flows, are counter-cyclical, and bypass the state and official aid bureaucracies.¹

In light of their empirical significance and features, it is understandable that a growth industry in the study of remittances has emerged alongside the growth in these flows themselves. Remittance studies have been taken up by policymakers and officials of multilateral institutions, by those working with non-governmental organizations and on behalf of migrant communities, and by social scientists—particularly development economists and anthropologists. In this literature, we principally find efforts to map remittances and to measure and leverage their microeconomic contributions. A widespread presumption in recent literature is that remittances are beneficial.² Recent literature also presumes that policy should mainstream remittances so that they flow through formal financial channels and that there are important reasons for reducing the costs of sending and receiving remittances.

Nevertheless, a vast body of literature in the fields of finance and economic development and international capital flows has largely ignored remittances. Indeed, to date, my own work in these fields has generally noted the existence of remittances, but then has proceeded to ignore them entirely. Scholarship on finance and development and international capital flows has focused on what have long been seen as the important and double-edged international flows—namely, ODA, private loans, FDI and, from the 1990s onward, portfolio investment (PI). These types of international capital flows have long been studied by political economists and development economists, not least because of the controversies in which they are implicated. In the case of ODA, we find controversies over tied aid and critiques of the international aid bureaucracy; in the case of foreign loans, we find debt overhangs that lead to debt crises, bailouts, and structural adjustment programs that are conditioned by the International Monetary Fund; in the case of PI, we find speculative bubbles that increase the risk of financial crisis and the possibility of bailouts with attendant negative effects on national policy autonomy; and in the case of FDI, we find foreign ownership of domestic assets or strategic resources, the repatriation of profits to foreign investors, and the possibility that

¹ The latter attribute is particularly important to skeptics of the state and aid bureaucracies [Adelman, 2003].

² This view of remittances contrasts with earlier work in this field (in the mid-1980s to the mid-1990s) that largely saw these flows as unproductive insofar as they were seen principally to fuel consumption, some of it wasteful and conspicuous, and much of it import-dependent. This pessimistic view is summarized in Durand, Kandel, Parrado, and Massey [1996] and Brown [1994:347-48].

foreign investors exercise undue influence over national policy. Thus, each of these international capital flows is associated with diverse risks and channels by which external actors can constrain domestic policy autonomy [see Grabel, 1996].

In this paper, I attempt to bring remittance studies into contact with the kinds of political economy concerns that have traditionally characterized scholarship on international capital flows to the developing world, but which have largely been ignored in the remittance studies literature.³ This paper draws together findings from the rapidly growing multi-disciplinary study of remittances; identifies what we know, what we do not yet know, and what we still need to know about their economic, political and social consequences; and argues that there are a range of important political economy concerns raised by remittances.

To foreshadow the conclusion, there is still much that we would want to know about remittances. Nevertheless, at this preliminary point, we can already see that the political economy effects of remittances are complex, contradictory, and not amenable to generalizations (as is the case with other international capital flows to the developing world). Thus, we should not be disappointed or surprised to learn that remittances do not have uniform or unambiguous political economy implications for developing countries. What we perhaps should be wary of are general policy proposals that seek the promotion and management of remittance flows as a means to the advancement of economic development.

2. EMPIRICAL LANDSCAPE

In what follows, I provide a brief survey of the chief empirical trends and characteristics of remittances.

A. Measurement

Remittances are the financial resource flows that arise from cross-border movements of people [Kapur, 2004: p2]. They have therefore grown alongside the growth in migration flows over the last quarter century.⁴

³ There are a few exceptions within remittance studies— for instance, Burgess [2007], Julca [2007], Kapur [2004], and Nayyar [2008] examine some political economy issues raised by remittances. Dilip Ratha of the World Bank has generated authoritative and wide-ranging empirical studies that are principally responsible for the explosion of interest in remittances by academics and policymakers.

⁴ See Ratha and Xu [2008] and WB [2008b] for data on migration trends. See Burgess [2007] and Nayyar [2002, 2008] for discussion of the political economy and root causes of the increase in migration flows. The former study places particular emphasis on migration to the USA from Latin America and the Caribbean, and the latter looks at migration from the developing world more broadly. There are many factors that explain the increase in migration from the developing world. Most important among them are the social and economic dislocation associated with neo-liberal reform and structural adjustment programs, the fallout of financial and economic crises on living standards, the problems caused by failed states and/or political and civil strife in numerous nations, and policies and conditions in wealthy nations that have encouraged lower-skilled groups to seek temporary employment and higher-skilled groups to seek permanent employment.

The current consensus among remittance researchers is that the most comprehensive measure of recorded remittances is the sum of the following three items that appear in the IMF's annual *Balance of Payments Yearbook*. (1) Unrequited transfers/worker remittances refer to money sent by migrants (i.e., those who work abroad for more than a year) to family and friends on which there are no claims by the sender; (2) migrant transfers refer to the net worth of migrants moving from one country to another; and (3) compensation of employees refer to funds sent abroad by temporary workers (i.e., those who work abroad for less than a year).⁵ The data on recorded remittances that appear below utilize this measure.⁶

B. Data Problems

There are numerous, well-documented problems with the coverage, quality and comparability of recorded remittance data [Ratha, 2003:Annex; WB, 2006:Appendix 4A.1; Kapur, 2004: 3-4]. For instance, many countries (such as the Philippines) do not distinguish between migrants and temporary workers in collecting data; inflows and outflows of remittances across countries do not match when summed together, as is the case with balance of payments data more generally (e.g., in 2007, world inflows of remittances are estimated at \$337 billion, while world outflows total \$238 billion); many countries do not report remittance data at all (in 2003 there were about 87 such countries)⁷; only 28 countries report the three flows that collectively constitute remittances; and data reported by different multilateral institutions varies rather considerably. The World Bank [2007:fn3] reports on numerous efforts underway to enhance the quality of remittance data, such as those involving the Luxembourg Group, a group comprising representatives from the UN, IMF, and World Bank.

In addition to problems with recorded remittance data, there is the more vexing issue of unrecorded remittances. These may be transmitted through a variety of informal operators (some of which may be ethnically or religiously based) or can be hand carried by travelers. Estimates place the true size of remittance flows at 50% or more above reported levels [WB, 2006]. The World Bank [2006:fn8] illustrates the magnitude of the unrecorded data problem with the following observations: a household survey in Spring 2005 revealed that 42% of remittances from Belgium to Senegal and 55% from Belgium to Congo and Nigeria went through informal channels; anecdotal evidence suggests that nearly 70% of remittances from France to Mali take place through informal

⁵ Note that Chami et al. [2008] take a different view as to how remittances should be measured, namely, that only the first of these three items constitute remittances.

⁶ Note that item 1 is recorded in the current account under "current transfers," item 2 in "capital transfers" in the capital account, and item 3 in the "income" subcategory of the current account.

⁷ Some of the countries that do not report remittance data at all are Afghanistan, Angola, Bahamas, Bahrain, Bhutan, Burundi, Canada, Central African Republic, Chad, Congo, Cuba, Democratic Republic, Equatorial Guinea, Iraq, Kuwait, Liberia, Singapore, Somalia, Taiwan POC, Turkmenistan, United Arab Emirates, Uzbekistan, Vietnam, Zambia, and Zimbabwe [WB, 2006:fn32]. This is consequential for researchers for obvious reasons. Kapur [2004:3] notes that gaps in the data exist in some countries (like Afghanistan, Haiti and Liberia), where remittances play an essential role in supporting household consumption and providing social insurance, and countries with large diasporas like Cuba and Vietnam report zero remittances.

channels; in the Philippines, 40% of remittances are hand carried by migrants during visits home; and nearly 42% of remittances from South Africa are estimated to be sent through informal channels.

It is hard to say exactly how the use of informal remittance channels has been affected by changes in banking, security, and immigration regulations since September 11, 2001.⁸ On the one hand, recorded remittances to some countries may have increased dramatically as a consequence of a number of factors.⁹ These factors are as follows: tightened oversight over financial flows; closure of some informal channels; reductions in the cost of sending remittances via formal channels in wealthy countries; enhanced data collection efforts; financial innovation and competition that has stimulated new cross-border banking partnerships, cooperation between formal banks and microlenders, and the use of cell phones and the internet as vehicles for remittances; sheer growth in the number of migrants and in their incomes; and the increased value of total remittances from Europe and Japan that is due to the depreciation of the dollar¹⁰. On the other hand, it is possible that migrant communities in many countries might be relying more on informal channels for sending remittances because of privacy concerns and the uncertain and hostile climate that they face.

Finally, it is worth noting that some flows that approximate remittances will never show up in the data as such. Examples of flows that function as a kind of remittance include in-kind transfers of consumer goods and direct payments on behalf of family members for insurance premiums and school fees [Solimano, 2004]. It is also the case that migrants make deposits to bank accounts in their country of origin so that their remaining family members can draw on their remittances without paying the high fees associated with international money transfers. Non-resident bank accounts are permitted in many countries, such as Bangladesh.

C. Trends and Characteristics

⁸ The USA Patriot Act is the most relevant of the post-9/11 policy changes. Under this legislation, anyone sending less than US \$1,000 through financial institutions and money transfer companies must present identification (identification cards issued by foreign governments are acceptable), and transactions above US \$3,000 require the collection of information on identification, address and occupation of sender and receiver. This legislation also allows the consular identification card issued by the Mexican government to be used as a valid form of identification to open a bank account with a financial institution. But many financial institutions, especially large commercial banks, still do not accept consular identification cards. The legislation also requires that the identities of senders and recipients of remittances be checked against the Office of Foreign Assets Control list (which includes known or suspected terrorists). For further details on this legislation, see Cirasino, Guadamillas, and Salinas [2008].

⁹ E.g., recorded remittances to Pakistan from the USA increased from \$80 million in 2000 to \$779 million in 2002. Financial controls implemented after September 11 disrupted the highly efficient, but informal network of the hawala (i.e., transfer) that many migrants used to send money home, leading them to switch to formal remittance channels [Migration Policy Institute, no date].

¹⁰ The appreciation of the euro relative to the dollar raised the value of remittances by 7% between 2001 and 2005 [Mohapatra, et al., 2006].

In 2007, inward remittances to developing countries are estimated to have reached \$251 billion, which is more than eight times the level in 1990, and more than double the level in 2002 (see table 1).

Table 1. Migrant Remittances to Developing Countries (US\$ billion, current dollars)*

INFLOWS	1990	2000	2002	2004	2006	2007	Change 2002-07	Remittances as a share of 2006 GDP (%)
-All developing countries	31	84	116	163	226	251	116%	2.0%
By country income group:								
-Low-income countries	5	8	15	20	29	33	120%	5.0%
-Middle-income countries (MIC)	26	76	100	143	197	218	118%	1.8%
-Lower MICs	16	53	71	95	127	140	97%	2.3%
-Upper MICs	10	23	30	48	70	78	160%	1.4%
By regions:								
-East Asia and the Pacific	3	17	29	39	53	59	103%	1.5%
-Europe and Central Asia	3	13	14	23	39	47	236%	1.7%
-Latin America & the Caribbean	6	20	28	42	57	61	118%	1.9%
-Middle East & N. Africa	11	13	15	23	27	29	93%	3.9%
-South Asia	6	17	24	29	40	44	83%	3.5%
-Sub-Saharan Africa	2	5	5	8	11	12	140%	1.7%

*Workers' remittances, migrant transfers and compensation of employees. Source: World Bank, Development Prospects Group (WB-DPG), [http://siteresources.worldbank.org/INTPROSPECTS/Resources/334934-1110315015165/RemittancesData_Jul08\(Release\).xls](http://siteresources.worldbank.org/INTPROSPECTS/Resources/334934-1110315015165/RemittancesData_Jul08(Release).xls)

1. Remittances by region

As is clear from Table 1 above, remittances have grown in all regions of the developing world, but most rapidly in Europe and Central Asia . Latin America and the Caribbean are the largest recipients of remittances. However, as a share of GDP, remittances are highest in the Middle East and North Africa.

Sub-Saharan Africa receives the smallest pool of remittances among regions of the developing world. However, the data for Africa as a whole are understood to be particularly inaccurate.¹¹ This is because of problems with reporting, because the formal banking system has low credibility and very limited reach (especially in rural areas), and because the costs of sending remittances through formal channels is extremely high [WB, 2007a; Julca, 2007]. Notwithstanding these inadequacies, Kapur [2004] rightly notes that the low level of remittances to the region over the last many years means that they cannot be expected to play an important role in ameliorating the region's economic problems.

Ratha et al. [2007] note that remittances to South and East Asia appear to be growing steadily, most likely because of strong demand for labor in oil-exporting Middle Eastern countries. They also note that remittance flows to Latin America and the Caribbean continue to increase; however, recently their rate of growth has been slowing markedly (and remittances to Mexico have declined since January 2008, see discussion in Ratha et. al [2008]). This change in Latin America and the Caribbean, and particularly in Mexico, is most likely due to the slowdown in the US' economy and recent changes in US immigration policies and politics that are impeding the flow of migrant workers and their ability to secure employment (and when successful in doing so, they may be less likely to use formal channels to send remittances because of privacy concerns).

2. Remittances by income level

As we can see from table 1, the majority of remittances do not flow to the poorest countries. Indeed, in 2007, low-income countries received only 13% of remittances to the developing world. In the same year a little over half of all remittances received by developing countries went to lower middle-income countries (\$140 billion), while the other half were divided unequally between upper-middle income countries (\$78 billion) and low-income countries (\$33 billion).

¹¹ The inadequacy of recorded remittance data for Sub-Saharan Africa has been widely noted. For example, Page and Plaza [2006] estimate that 73% of remittances to Sub-Saharan African countries were through informal channels. Ratha, Mohapatra and Plaza [2008] report that using this estimate, remittances to Sub-Saharan Africa would be more than \$30 billion annually. Julca [2007] notes that at least 80% of remittances in Uganda and Sudan are sent through informal channels, while for some African countries, remittances in-kind might be equal or higher than money remittances [Julca 2007, citing Sander and Maimbo, 2003]. Julca also notes that remittance figures at the regional or continental levels are distorted by the fact that some African countries do not report data on remittances, namely, Angola, Burundi, the Central African Republic, the Democratic Republic of Congo, Chad, Djibouti, Liberia, and Somalia.

Note that I do not deal in this paper with what have recently been termed institutional remittances, which include grants by US and European foundations, even though this type of remittance is becoming increasingly important to Sub-Saharan Africa (data are provided in Ratha, Mohapatra and Plaza [2008]).

In contrast, when compared to GDP and import income, remittances are relatively far more important to low-income than to middle-income countries. For example, remittances were equivalent to 5% of GDP in low-income countries in 2006, compared to 1.8% of GDP in middle-income countries in the same year. The top recipients of remittances in nominal terms in 2007 were four large countries, namely India (\$27 billion), China (\$26 billion), Mexico (\$25 billion), and the Philippines (\$17 billion) [WB-Development Prospects Group, DPG, 2008]. But as a share of GDP in 2006, the top five recipients of remittances were small, low-income or lower-middle-income countries—namely, Liberia (where remittances were equivalent to 109% of GDP), Tajikistan (36%), Moldova (35%), Tonga (32%) and Honduras (26%) [WB-DPG, 2008]. It is worth noting that remittances are far less concentrated in large developing economies than are other types of international private capital flows.

3. Remittances in relation to other international capital flows and sources of foreign exchange

In 2007, recorded remittances (\$251 billion) were the third largest net source of external finance to developing countries as a whole, after FDI (\$460 billion) and private debt and portfolio equity (\$543 billion) [WB-DPG, 2008] (see figure 1 below). In the same year, remittances were more than twice as large as ODA inflows (\$104 billion), and nearly 55% and 46% as large as FDI and PI, respectively. Indeed, in many developing countries, recorded remittances are the largest source of external finance of any sort [Mohapatra, et al., 2006: 1].¹² Over the last decade, remittances to developing countries have become an increasingly important source of foreign exchange and purchasing power. From 1996-2006, recorded remittances to developing countries have grown faster than other international private capital flows and ODA (see figure 1).¹³ Moreover, FDI and PI are very highly concentrated among larger developing countries. Indeed, in 2007, ten countries received 61% of the FDI and 96% of the portfolio equity that went to the developing world.¹⁴

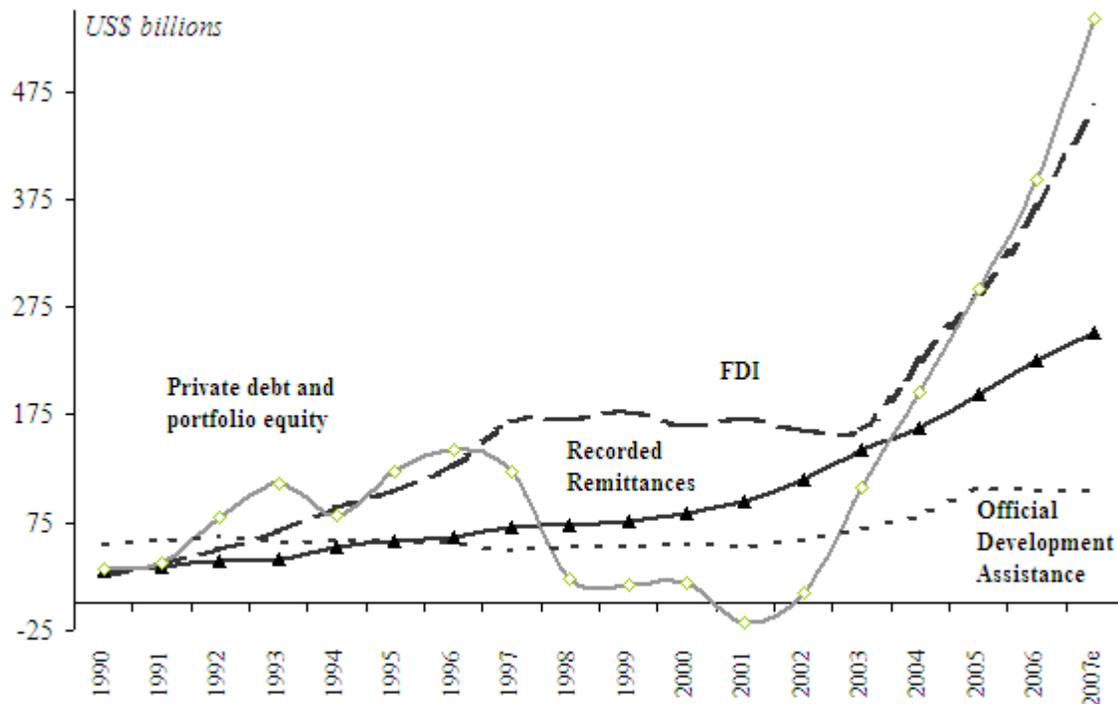
¹² If we adjust the data to include estimates of remittances sent through informal channels, total remittance inflows are likely to be larger than net FDI and PI.

¹³ From 1996-2006, net recorded remittances to developing countries grew by 264%, whereas FDI, private debt and portfolio equity, and ODA grew by 188%, 173%, and 86%, respectively.

¹⁴ The top ten recipients of FDI to the developing world in 2007 (in order) are China, Russia, Brazil, Mexico, Turkey, India, Poland, Chile, Ukraine and Thailand. In the same year, the BRIC countries (Brazil, Russia, India and China) alone received 41% of the FDI inflows to the developing world. The top ten recipients of portfolio equity inflows to the developing world in 2007 (in order) are China, India, Brazil, Russian Federation, South Africa, Turkey, Thailand, the Philippines, Indonesia, and Malaysia. The BRIC countries alone received 76% of the equity flows to the developing world in 2007. (Data on FDI and portfolio equity are from WB [2008a]). FDI and PI flows are also concentrated regionally within recipient countries.

Note that in 2007, the top four recipients of remittances are developing countries (in order, these are India, China, Mexico, the Philippines). These four countries received 38% of all remittances that went to the developing world in 2007 [WB-DPG 2008]. Romania is the only other developing country among the top ten recipients of remittances (and it is in tenth place, behind France, Spain, Belgium, Germany and the UK).

**Figure 1: Net international capital flows to developing countries, 1990-2007:
Remittances, private debt and portfolio equity, FDI, and ODA**



Sources: *Global Economic Prospects 2006* (World Bank), *IMF Balance of Payments Statistics Yearbook 2008*, *World Development Indicators 2008*, and *Global Development Finance 2008*.

Source: [http://siteresources.worldbank.org/INTPROSPECTS/Resources/334934-1110315015165/Fig1_NetCapitalFlows\(updatedJul08\).xls](http://siteresources.worldbank.org/INTPROSPECTS/Resources/334934-1110315015165/Fig1_NetCapitalFlows(updatedJul08).xls)

Data from the World Bank [2006:88] further illustrate the growing importance of remittances to purchasing power in developing countries. The Bank reports that in 2004, recorded remittance receipts were equivalent to about 6.7% of developing countries' imports and 7.5% of domestic investment. Remittances were larger than public and private capital inflows in 36 developing countries in 2004. The same study reports that remittances were larger than total merchandise exports in Albania, Bosnia and Herzegovina, Cape Verde, Gaza, Haiti, Jamaica, Kiribati, Lebanon, Nepal, Samoa, Serbia and Montenegro, and Tonga. In another 28 countries, they were larger than the earnings from the most important commodity export; for example, in Sri Lanka, they are larger than tea exports, and in Morocco, they are larger than tourism receipts [WB, 2006:88]. Moreover, in Mexico, remittances are larger than FDI. And for many small countries, especially island economies, remittances (along with foreign aid and tourism) have become the main sources of income [Kapur, 2004:10]. In Cape Verde, for instance, about 2/3 of all families receive money from abroad [Kapur, 2004:10].

4. Source countries

High income countries are the dominant source of remittances. In 2006, the USA was the largest source country with nearly \$42 billion in outward remittances [WB-DPG, 2007].

Outward remittances from developing countries are not inconsequential, however. In 2006, they amounted to \$44 billion [WB-DPG, 2008]. Ratha and Shaw [2007] estimate that between 9% and 30% of total remittance flows to developing countries originate in other developing countries, where at least half of all migrants from developing countries (roughly 74 million migrants) reside. Official data show that several developing countries (e.g., China, Malaysia, Kazakhstan, and the Russian Federation) are among the top 20 sources of remittances [WB, 2008b]. Anecdotally, outward remittances from India and South Africa are believed to be large, although this is not reflected in official data [WB, 2006:88-90].

Data on South-South remittances are thought to capture a much smaller portion of these flows than do the data on North-South flows. One reason for this is that the cost of sending remittances through formal channels from developing countries is even higher than sending them from wealthy countries [extensive discussion and data appear in Ratha and Shaw, 2007].

5. Stability, cyclicality and the insurance function

Remittances are less volatile than other international private capital flows (see figure 1 above), and they are counter-cyclical. This contrasts with other international private flows that tend to be strongly pro-cyclical.

Remittances are a form of self-insurance in developing countries. The insurance function is reflected in the tendency of migrants to send more remittances to their countries of origin following downturns in the economy, crises, natural disasters, and/or political/civil conflicts [Ratha, 2007].

There is also some evidence that remittances may remain stable when there is an economic downturn in the sending country [Ratha, 2003:163]. This is very likely due to the fact that remittances are driven by familial bonds and social obligations. The motivations for sending remittances confound some analysts who seem driven to feats of econometric gymnastics aimed at demonstrating that remittances are principally (or, at least, significantly) the outcome of rational, wealth maximizing investment motives on the part of migrants rather than the outcome of familial obligations [e.g., Alper and Neyapti, 2006; Buch and Kuckulenz, 2004; Lueth and Ruiz-Arranz, 2006]. This is very much a minority position in the literature. Most analysts suggest that remittances are driven by altruism or by implicit social contracts within families. These implicit social contracts mean that migrants provide support—even over several decades—to those family members that remain at home. Alternatively, these implicit contracts imply that migrants and their families co-insure each other, such that the migrant provides assistance to the family at home, and the family at home stands ready to provide care in the event that the migrant is suddenly deported or falls ill.¹⁵

¹⁵ See Solimano [2004] for an excellent summary of this debate.

3. THE STATE OF KNOWLEDGE: THE ECONOMIC, POLITICAL AND SOCIAL EFFECTS OF REMITTANCES

We now turn to the diverse and cross-cutting economic, political and social consequences of remittances. Here I draw together what we have come to know about remittances, what we do not yet know, and what we still need to know. Drawing on the most recent scholarship, I highlight areas of consensus among researchers and identify those areas where further investigation is warranted, particularly by researchers interested in the political economy issues raised by remittances.

1. Poverty

There is consensus in the empirical literature that remittances reduce poverty through its direct effect on the income (and hence, on the consumption) of recipients.

The direct effect of remittances on poverty is particularly important following crises and conflicts, as we saw in section 2.5 above.¹⁶ Numerous studies support this finding; for instance, Yang [2003] presents evidence that households with overseas migrants in the Philippines did substantially better following the Asian financial crisis than did those with no family members abroad. The role of remittances in providing critical income support to households is incontrovertible. Studies show that households that receive remittances attain higher living standards than those without family members living abroad [see Kapur, 2004:16]. Maimbo and Ratha [2005] find that remittances have a greater effect on poverty in rural areas of developing countries because most migrants come from rural regions, and hence, send funds back to such areas

That remittances have a direct effect on poverty through the provision of income is obvious. Once we move beyond this straightforward issue, we see that there are several matters concerning remittances and poverty that are less clear cut.

One area of debate concerns the magnitude of the direct effect of remittances on poverty. The most widely cited study of the subject by Adams and Page [2005] finds that remittances have a rather large direct effect on poverty. Using data from 71 developing countries, they find that international migration and remittances significantly reduce the level, depth and severity of poverty. They find that a 10% increase in per capita official international remittances is associated with a 3.5% decline in the share of people living in poverty. Equally notable is their finding that dollar for dollar the income remitted by migrants reduces poverty much more than does income generated by domestic economic activity. Another study of remittances to Latin America by Acosta, Calderón, Fajnzylber and López [2008] reaches a similar conclusion regarding the magnitude of the direct effect of remittances on poverty (through its effect on per-capita income in recipient countries). They find that for each percentage increase in the share of remittances to GDP in Latin America, the fraction of the population living in poverty is reduced by about 0.4%. However, the same study notes that the impact of remittances

¹⁶ We will see in section 3.4 below, the direct effect on poverty has important spillover effects to investments in human capital.

on poverty varies considerably across countries in Latin America insofar as it depends on initial levels of development and inequality and on the distributional attributes of the households and regions that receive these flows. For this reason they conclude that for Latin America as a whole the best that can be said is that remittances have a small direct effect on poverty.¹⁷ Other studies are similarly cautious on the magnitude of the direct effect of remittances on poverty. For example, a survey of the empirical literature by López-Córdova and Olmedo [2006] concludes that remittances reduce poverty, but that the effect may be small and is sensitive to the precise measure of poverty adopted.

As we will see in subsequent sections of the paper, remittances are also thought to reduce poverty through a rather large number of indirect effects on recipient economies, such as through their effects on long-term economic growth, access to working capital, labor markets in the countries that have sent migrants, and the accretion of human capital. We will see that much remains to be known about many of these indirect effects.

Most studies of remittances and poverty do not distinguish between its direct effect on transient poverty and its effects on structural poverty.¹⁸ As discussed above, empirical evidence makes clear that remittances directly reduce transient poverty via the provision of income. We would expect remittances to affect structural poverty through indirect channels. But, in fact, there is a great deal that we do not know about the indirect effect of remittances on structural poverty (as Kapur [2004] rightly acknowledges). For example, the extent to which remittances reduce structural poverty depends very much on “selection effects,” i.e., on the income and skill attributes of migrants themselves. Are migrants drawn from the poorest and lowest-skilled segments of the labor pool, and do those who migrate legally versus illegally have equivalent attributes? If migrants are chiefly drawn from the poorest members of society, for instance, then the receipt of remittances will raise incomes of the poorest families (and hence, will reduce poverty). Similarly, if migrants are chiefly drawn from the lowest rungs of the labor market, then the reduced labor supply in the home country will cause wages to rise for lower-skill workers at home. In this case, structural poverty will be reduced by the combined direct effects of the receipt of remittances and the indirect effect of higher wages available to the unskilled workers that are left behind.

There are good reasons, however, to believe that the significant up-front financial costs of migration may often deter migration of the poorest of the poor. Note that migration schemes involving some form of indentured servitude allow the costs of migration to be paid over time. Such arrangements might be seen as equalizing the opportunity to migrate at the cost of diminished freedom, but especially in the case of illegal migration, they might also so substantially increase the total cost of migration that they substantially undermine the benefits thereof.

¹⁷ Fajnzylber and López [2007] report similarly cautious results in another study of remittances and Latin America—to wit: remittances have a variety of quite modest economic effects which vary considerably across countries.

¹⁸ This point is made by Kapur [2004].

There is also the broader matter of the capability to migrate, using the term in the sense of Sen [1992]. It is reasonable to assume that those who are most likely to migrate, and hence to send remittances, possess a broad range of capabilities (such as the ability to function in a strange cultural environment away from family) that make them less likely to come from the very bottom rungs of society.¹⁹ If this is correct, then remittances may have the undesirable effect of reinforcing existing disparities in capabilities.

To date, research on selection effects and migration capabilities demonstrates that we cannot generalize about the attributes of migrants across countries. Empirical research finds evidence of positive, intermediate and negative selection effects in migration in a variety of national contexts. For example, Borjas [1987] finds evidence of a negative selection effect in migration from developed countries to the USA. By contrast, Funkhouser [1992] finds positive selection effects in emigration from Managua, Nicaragua. In the Managuan case, emigrants tend to be disproportionately more likely to have a secondary or university-level education, are more likely to have been employed in a white-collar occupation before leaving the country, tend to come from higher income households, and from households in which the remaining members are more educated than the country's population as a whole. In a general survey, De Hass [2005] argues that it is rarely the poorest who emigrate from the developing world.

Taylor [2006] argues that in those cases where the costs and risks of emigration are high, evidence suggests an intermediate selection effect in migration, such that the households most likely to participate in international migration are those in the middle of the income distribution. Niimi and Özden [2008] find that there is no singular type of selection effect at work across Latin American migrants. They conclude that most Mexican and Central American migrants are drawn from the lower end of the income and skill spectrum, whereas migrants from South America and the Caribbean tend to be proportionally more educated than those left behind.

There is evidence of heterogeneous selection effects in migration, though there is a need for further research on this issue, especially outside the Latin American context. In addition, the discussion of inequality that follows below suggests that researchers would do well to rethink their static conception of selection effects. As we will see, there is good reason to expect that positive or intermediate selection effects in the early stages of migration from a locality may create the conditions for later migration by those possessing lower skills or incomes.

2. Inequality

Given the results of the studies of selection effects in migration—both what they indicate about the diversity of selection processes and the gaps in knowledge that remain—it is unsurprising that the various scholarly studies of the distributional effects of remittances present a mixed picture [WB, 2006; Ratha, 2003; López-Córdova and Olmedo, 2006]. This stands in sharp contrast to the generalized claims that often appear in the policy and popular literature.

¹⁹ The discussion of the capability to migrate draws on DeMartino [2000: ch.7].

Some academic studies find that remittances widen inequality because they flow disproportionately to better-off households (because of the positive selection effects discussed previously). For instance, Rodriguez [1996, cited in Agunias 2006] finds that remittances worsen income distribution in the Philippines. Saith [1997] concurs, arguing that they also worsen inequalities between more prosperous regions, sectors and classes in the Philippines. Studies of Pakistan and Egypt by Adams [1998 and 1991, respectively] conclude that remittances increase inequality [cited in Agunias 2006].²⁰

By contrast, Taylor [1999] argues that remittances may have had an equalizing effect on the distribution of income among socioeconomic groups in Mexico. But the evidence from Latin America is mixed on this matter. Research by Acosta, Fajnzylber and López [2008a] finds that households with remittance income come mainly from the bottom of the distribution in some countries, such as Mexico and Paraguay, but from the top of the distribution in others, such as Haiti, Peru and Nicaragua. Hence, even within this region, the evidence indicates that remittances have radically different effects on inequality (and poverty).

Nayyar [2006] raises an important set of issues that have received scant attention in the empirical literature. These concern the interaction of selection effects, remittance proclivities of different groups, the nature of contemporary immigration policies in wealthy countries, and inequality. He states that there is some evidence that remittances from un- and semi-skilled migrants are significantly higher than remittances from the better educated, more skilled and economically advantaged. (This seems a reasonable assumption given that the families of poorer migrants are more likely to depend on remittances in the first place.) Contemporary immigration policies in wealthy countries favor highly skilled, educated emigrants. These policies have the effect of reinforcing positive selection bias in migration. The consequence of this augmented positive selection bias increases the possibility that remittances will worsen income inequality in developing countries (since remittances will flow to those who need them least). Nayyar [2008] also notes that guest worker programs and illegal immigration can reduce income inequality between countries since the less advantaged groups that tend to migrate through these means have high remittance proclivities, and temporary migrants often return home with their savings.

There is some research that attempts to place the distributional effects of remittances into a dynamic, temporal context [Stark and Taylor, 1986]. This work shows that remittances may increase income inequality in a particular village or region at the start of migration from that area. This is because pioneer migrants come from households that can shoulder the costs and risks of international migration [Taylor, 2006]. At this stage, then, remittances worsen the distribution of income within a particular community (and have relatively little direct effect on poverty). But the establishment of migration networks by a community's pioneers may ultimately reduce the information and relocation costs for poorer members of the community [Lucas, 2005: 39, cited in Agunias 2006]. As a migration network matures, poorer households will gain access to

²⁰ The finding for Pakistan is explained by the positive or intermediate selection bias in migration from the country, which Adams [1998] speculates is due to the high cost of financing international migration.

remittances and this may eventually reduce the degree of inequality (and poverty) within a community. Taylor's work on rural Mexico [2006] demonstrates this U-shaped temporal effect of remittances on inequality. In addition, Taylor [2006] shows that migration networks are more important to female than male migrants because women are more likely to be deterred from migrating by risky border crossings, uncertain prospects abroad and concerns for personal safety. Thus, the maturation of migration corridors may ultimately increase the opportunity of women to migrate.

Despite the intuitive appeal of this account, other studies of migration networks indicate that the matter is not so simple. Mature migration networks tend to take on a life of their own, such that remittances induce new waves of migration by family members left behind (e.g., see Van Dalen, Groenewold, and Fokkema [2005] on Morocco, Turkey and Egypt and DeParle [9/7/07] on the Indian state of Kerala). While this might be beneficial from the perspective of inequality (and opportunities) within a region, the migration-remittance-additional migration cycle can ultimately undermine the viability of what ultimately become largely deserted local economies.²¹

To date, the issue of the relationship between remittances and regional inequality remains largely unexplored in the literature. If migration patterns are path dependent, then remittances might induce or deepen regional inequality within a migrant-sending country. This returns us to the issue of differing migration capabilities, a factor that future research may find is self-perpetuating and which may therefore reinforce existing regional inequalities within developing countries. But future research may find that that the aggravation of regional inequalities within countries is a temporary phenomenon, especially if it turns out that the maturation of a migration network within a region reduces the cost of establishing new networks in other regions of the same country.

Another factor that warrants future research is the effect of remittances on racial, ethnic and gender inequalities within a country. If certain groups have a greater capacity to migrate (because of pre-existing migration channels, greater initial conditions of wealth, more experience living abroad, or a greater likelihood of acceptance abroad because of religion, race, etc.), then remittances may aggravate racial, ethnic or gender-based inequalities. The only mention of this issue in the literature concerns Cuba. Kapur [2004] notes that remittances to Cuba have a strong racial bias since the Cuban diaspora is mostly white, while the island is majority black. He also notes that remittances to the country have an urban bias: 20% of the population lives in Havana, but the city receives about 60% of the remittances to the country. Whether remittances aggravate racial, ethnic, gender and/or regional inequalities in other countries are issues that deserve further investigation by remittance researchers.

3. Consumption

²¹ A recent popular article on the Indian state of Kerala makes a point along these lines. It reports that one in six Keralite works overseas (with a large proportion of the workers going to the Gulf States), that the \$5 billion that Keralian migrants send home each year augment the state's output by around 25%, and that these remittances are a major factor in sustaining the high quality of life for which the state is known [DeParle, 9/7/07].

Not surprisingly, there is a consensus among empirical researchers that remittances are primarily used to finance basic subsistence consumption expenditures on food, rent and health care for households that are below a threshold level of income [WB, 2006; Congressional Budget Office, 2005; Kapur, 2004]. For example, Burgess [2007] reports that around 80% of remittances in Mexico are used for basic needs, Solimano [2004] cites research on Ecuador that finds that 60% of remittances are spent in this manner, and a survey in Latin America conducted by the Inter-American Development Bank reports that daily household expenses absorb 46% and 84% of remittances (respectively) received in Brazil and El Salvador [López-Córdova and Olmedo, 2006]. Support for subsistence consumption is critically important to sustaining poorer households because they lack access to insurance and credit, and are therefore immensely vulnerable to income shocks [WB, 2006].

The nature of the multiplier effects of remittance-financed consumption has received limited attention in the literature. Indeed, Julca [2007] is the only study that explicitly calls for the development of measures of the diverse multiplier effects of remittances on regions, sectors, etc. Kapur [2004] suggests that multiplier effects will be induced to the extent that remittances stimulate consumption of domestically-produced goods. Moreover, drawing on work by Desai et al. [2003], he suggests that consumption financed by remittances will increase domestic tax receipts.²²

In my view, there are several factors that might mitigate or even negate these multiplier effects. In many developing countries a large proportion of basic needs goods are imported.²³ In this case, the multiplier effect of consumption financed by remittances will be limited, and the increased consumption of imports can aggravate trade deficits. Moreover, many goods in developing countries (especially in rural areas) are purchased through informal vendors that obviously do not collect consumption taxes at the point of sale. In sum, we will only know whether the increase in consumption associated with remittances is beneficial on the macroeconomic level once research addresses the precise nature of the leakages, multiplier and tax implications of remittances.

4. Savings, private investment in physical assets and human capital, and the effect on state behavior in the developing world

There is unambiguous evidence that once basic needs are met, remittances are used for savings, debt repayment, consumer durables, land and housing purchases, small enterprise development and small-scale agricultural production, and education and healthcare [Lowell and De la Garza, 2000; Sander, 2003; Yang, 2003; Osili, 2006;

²² Taylor [2006] notes that research is beginning to address the productivity multipliers associated with remittances. In this work, it is assumed that international migration negatively effects production in migrant-sending households in the short run because of reductions in household labor supply. The opposite is true in the long run since the remittances that stem from international migration finance new types of investment that increase household productivity. This multiplier dynamic has obvious relevance to migrant-sending regions.

²³ This pattern has numerous structural roots. Not least among them is the termination of import controls under neo-liberal economic (particularly, trade) reform and the historical conditions that led many developing countries to concentrate production resources in a few goods destined for export.

Ratha, 2007, 2003].²⁴ A household survey of Latin America provides some evidence of the diverse uses of remittances in the region (comparative studies for other regions are not available at this time). It reports that 2% of remittance inflows are used for educational expenses in Ecuador and 17% are used for the same purpose in the Dominican Republic, 1% of inflows are used for business use in Mexico while 10% are similarly used in Brazil and Guatemala, 11% of inflows are used for savings in Guatemala, and 7% of inflows are used for acquiring property in Brazil [López-Córdova and Olmedo, 2006].

Many studies find that remittances contribute to household savings (once basic needs are met). In Pakistan, for example, household surveys indicate that in the late 1980s and early 1990s, the marginal propensity to save was higher for income from international remittances than from either domestic remittances (i.e., from urban to rural areas of the same country) or from income on rental property [Ratha, 2003]. Moreover, there is evidence that (holding constant for income) the propensity to save among households that receive remittances is higher than in non-recipient households [Kapur, 2004], and that households, in general, tend to save a larger proportion of remittance income than other sources of income [Adams, 2002].

There are numerous national studies that highlight the contribution of remittances to investment and entrepreneurship among small businesses and agricultural producers, e.g., in South Africa, Mexico, China, Egypt, Pakistan, Turkey, and countries across the Caribbean [WB, 2006:ch.5; Burgess, 2007, and citations therein]. Based on these country experiences, there is speculation that remittances increase access to working capital through two channels: directly through the provision of resources; and indirectly, by increasing the pool of capital made available by formal financial institutions. The indirect effect on the availability of capital is assumed to come about because a stable flow of remittances increases household creditworthiness by buttressing and stabilizing income [WB, 2006].

The importance of remittances as a source of working capital in Mexico has been widely studied. One analyst of the country states that “remittances are an essential source of [working] capital for many small enterprises” [Papademetriou, 2003, cited in Burgess, 2007]. Massey and Parrado [1998] find that around 21% of businesses in the six largest migrant-sending states in Mexico were initially financed with US earnings. Woodruff and Zenteno [2004] find that remittances are a significant source of capital for microenterprises in 44 urban areas of Mexico.

²⁴ We will not address here the issue of forced remittances wherein sending or receiving countries withhold a certain proportion of migrants’ pay for remittances. In most cases, programs of forced remittances seek to ensure that temporary migrant workers return home at the end of their contracts. But in some cases, the goal of such measures has been to steer remittances toward investment in the country of origin. To date, the contribution of remittances toward this latter goal has not been studied systematically.

The most widely known program of forced remittances, the US-Mexico Bracero program of 1942-64, was characterized by widespread fraud: \$30-50 million in forced savings were not returned to workers. See World Bank [2006:97] for details on the Bracero and other programs of forced remittances.

The role of remittances in supporting small enterprise development and entrepreneurship has also been demonstrated in studies outside the Mexican context.²⁵ For example, Brown [1994] finds that households in the South Pacific save and invest a significant part of their remittances domestically.²⁶ Dustmann and Kirchkamp [2001] show that half of all returned immigrants to Turkey become entrepreneurs, and that the capital for starting these businesses stems from savings and capital acquired abroad. McCormick and Wahba [2001] find that total overseas savings and time spent overseas have a positive and significant effect on entrepreneurship in Egypt. Many studies find that remittances reduce credit constraints and stimulate entrepreneurial activity [Durand et al., 1996; Funkhouser, 1992; WB, 2006]. One study, for example, finds that a 1% increase in remittances to 13 countries in the Caribbean led to a .6% increase in private investment relative to GDP. Adams [1998] finds that remittances have a more important statistical effect on the accumulation of rural assets in Pakistan than does total labor income.

Remittances also facilitate investment in housing. For example, Parrado [2004] shows that having been in the US during the previous year increases the likelihood of home acquisition by 1.2 times, and that every additional year of work experience in the US raises the likelihood of homeownership by another 2.8%. He also finds that households that receive remittances are more likely to own homes that are in better physical condition. The condition of housing is not a trivial matter, particularly in light of the finding of Duryea et al. [2005] that improved housing conditions play an important role in reducing infant mortality.

Remittances not only support savings and physical investment as we saw above, but they also support investments in human capital [Ratha, 2007]. Investment in human capital has potentially far-reaching and long-term economic and social benefits that may be difficult to quantify, but which are nonetheless critical.

Remittances are used to pay school fees, and hence enhance educational attainment. They have also been found to help families keep children in school even following shocks that lead to a decline in non-remittance income. For example, a study of El Salvador and Sri Lanka finds that children in households that receive remittances have a lower school dropout rate, and that households that receive remittances spend more on private tuition [Ratha, 2007]. A number of studies conclude that remittances improve educational attainment among children in recipient households. Cox Edwards and Ureta [2003] find that receipt of remittances lowers the probability that children leave school in El Salvador. Yang [2003, 2005] finds that remittances increase school enrollment rates for children in the Philippines. López-Córdova [2005] finds that illiteracy rates among

²⁵ Citations in this and the following paragraph are drawn from the extensive literature reviews in López-Córdova and Olmedo [2006], Grigorian and Melkonyan [2008:7-8], Roberts [2005], essays in Fajnzylber and López [2008], and Agunias [2006].

²⁶ Brown [1994] finds that even remittances-in-kind (e.g., vehicles, light machinery) are often sold by recipient families in their home countries. The receipt and sale of remittances-in-kind are part of what he identifies as an international business strategy on the part of transnationally dispersed households.

children between 6 and 14 years old are lower, other things constant, as the fraction of households that receive remittances rises in a given Mexican municipality. Hanson and Woodruff [2003] find beneficial effects of remittances on school enrollments in Mexico. Kapur [2004] argues that in those cases where remittances flow to poorer families, remittances can enhance girls' educational attainments by cushioning household incomes after an income shock (since school attendance by girls is disproportionately affected by shocks to family income). Research by Acosta, Fajnzylber and López [2008b] on Latin America finds that remittances help families overcome budget constraints that limit investments in human capital (though the extent to which this occurs varies from country to country).

There is also a compelling body of evidence linking the receipt of remittances to better health outcomes, particularly among children. This is especially important in the numerous developing countries where the public health system does not provide adequate treatment, preventative care or universal health insurance [López-Córdova and Olmedo, 2006]. For example, children in households that receive remittances in Sri Lanka have higher birth weights due to better health care [Ratha, 2007]. Ameudo-Dorantes and Pozo [2004] report that healthcare expenditures in Mexico rise in response to the receipt of remittances (and that such expenditures are more responsive to increases in remittance than to increases in non-remittance income). López Córdova [2005] finds that, holding constant for income, infant mortality across Mexican municipalities declines as the percent of households receiving remittances increases.

It is clearly important that remittances support investments in human capital and investments in small enterprise and agriculture. But these achievements must be placed into a broader historical context. It is widely known that the formal financial system and the state in the developing world have long under-invested in human capital and have under-served small business and agriculture. It may be that remittances now patch over the gaps in public funding and bank financing that have grown ever larger thanks to mis-guided shifts in economic policy.

What I have in mind is this: the problems facing small business and agriculture have become more severe in the neo-liberal era as states throughout the developing world have dismantled long-standing programs that provided at least some assistance to small firms and agriculturalists, such as through protection from international competition, price and technical supports, and the provision of working capital by the state or formal financial institutions at subsidized rates.²⁷ At the same time, formal financial institutions in many developing countries have turned their limited attention away from small business and agriculture and toward the kinds of speculative activities that have flourished in the era of financial liberalization. In this environment of what I call "speculation-led development" [Gabel, 1995], formal financial institutions have also

²⁷ Writing on Mexico, Burgess [2007: p. 12] makes a compelling point that has currency well beyond the country. She writes: "in rural communities [in Mexico], migration and remittances have become critical alternatives to the withdrawal of the state from the agricultural sector, particularly in poor, southern states... Not only did many rural workers lose their jobs, but those who maintained small farms lost their sources of credit or investment."

been released of their (admittedly weak) state-mandated obligations to provide support to small business and agriculture. It may be that efforts to capture the booming remittance market will eventually cause formal financial institutions to respond to their smaller customers (see section 3.8 below for discussion of the effect of remittances on the formal financial sector). On the other hand, it is also possible that remittances will allow states and financial institutions to continue to ignore the social and economic needs of their most desperate regions and communities.

States in the developing world have also long under-invested in human capital. But this situation, too, has become far more severe in the neo-liberal era when state support for education and public health has been curtailed radically, and privatization of many essential public services has made them out of reach for large swathes of the population. Remittances, therefore, play the role of partially filling growing, large shortfalls in resources available for working and human capital. Though the hard numbers have yet to be assembled, it is entirely reasonable to assume that these large shortfalls in support for small business, small agriculture and human capital could not possibly be filled by remittances. In this connection, it is worth recalling from our empirical survey in section 2.2 that the poorest countries do not receive the majority of these flows, and they remain rather concentrated in some parts of individual countries.

In this context, it is important for remittance research to investigate whether remittances actually create a form of what we can term a “public moral hazard” on the part of developing country governments. That is, by partially resolving important bottlenecks, do remittances actually encourage states in the developing world to ignore their traditional responsibilities because they perceive or hope that remittances will fill various voids in state expenditure? The possibility that remittances may induce or aggravate public moral hazard is a matter that deserves serious consideration. If we find evidence that states in the developing world curtail their support for activities such as healthcare and education then the question for remittance researchers is whether remittances ultimately have no *net* positive effect on human capital investment in the developing world. If this is true, then remittances may have the unintended consequence of facilitating a shifting of the burden for ensuring economic security onto the most insecure groups in society.

The critical relevant questions for remittance researchers are as follows. First, do governments in developing countries curtail their expenditures on human capital once their countries begin to receive high and stable levels of remittances? Do remittances have a *net* positive effect on human capital investment, or do they simply substitute for public support for human capital that is no longer available? Second and relatedly, if there is a public moral hazard, how great is it, and what are the factors that condition the size of this effect? The possibility that remittances may induce or aggravate public moral hazard is a matter that deserves serious consideration, as is the extent to which remittances induce changes in state behavior in ways that allow for risk shifting onto those already most vulnerable.

Note that the possibility that remittances can induce public moral hazards has received only scant attention in the literature to date. As we will see in section 3.6 below, there is

one type of remittance-matching program that bears on the question of public moral hazard. We will also see in section 3.14 below that some analysts have suggested that remittances may allow governments to maintain policy regimes that would otherwise not be viable. Russell's [1986] widely cited paper identifies various "private" moral hazards associated with remittances, including the creation of dependence and the erosion of good work habits on the part of households that receive remittances, but does not extend the analysis to consider how remittances change state behavior in harmful ways.²⁸

5. Long-term economic growth

The vast majority of studies find limited or contradictory evidence of a causal link between remittances and long-term economic growth [Ratha, 2007; WB, 2006; Agunias, 2006].

A few studies conclude that there is no evidence of a positive relationship between remittances and long-term growth. For instance, one recent large-scale study using data from 101 developing countries from 1970-2003 found no significant link between remittances and per capita income growth [IMF, 2005]. Chami et al. [2008] conclude as well that remittances have no statistically significant effect on GDP growth because they neither increase investment nor lead to a more efficient allocation of investment.

In contrast, several single-country studies and one regional study claim unequivocally that remittances do promote growth.²⁹ For example, Korovilas [1999] argues that the economic growth experienced by Albania during the mid-1990s rested largely on the inflow of remittances from Albanian's working in Italy and especially Greece.³⁰ Adelman and Taylor [1990] find that every dollar Mexico received from migrants increased GNP by \$2.69 to \$3.17 (with the range depending on whether remittances were received by urban or rural households). Solimano [2003] finds that remittances are positively associated with growth for Andean countries.

One widely cited study by Chami, Fullenkamp and Jahjah [2005] finds that remittances have a negative effect on growth. This study of 113 countries over twenty-nine years finds that remittances reduce growth, principally because they discourage work by

²⁸ Russell [1986: Table 1] also enumerates other negative effects, namely, increased spending on consumption goods (something she says can create "consumption envy"), an increase in inflation and an aggravation of the trade deficit due to the purchase of imported goods. She also identifies a large number of beneficial effects of remittances.

²⁹ It is worth mentioning that a few studies examine the complex links among remittances, economic growth, and levels of financial development. However, taking account of financial development does not reduce the ambiguity surrounding what we know about the growth effects of remittances. E.g., Giuliano and Ruiz-Arranz [2006] find that remittances increase economic growth in less financially developed countries because they ease existing liquidity constraints, meet credit needs of local entrepreneurs, and channel resources toward productive investment. In this case, remittances promote economic growth by increasing the level of financial development. Mundaca [2005] identifies a different causal link between remittances, growth and financial development. He finds that higher levels of financial development lead to better use of remittances which, in turn, promotes growth.

³⁰ However, as we will discuss in section 3.7 below, the economic boom fueled by remittances proved unsustainable.

recipients. (The effect of remittances on labor markets will be discussed in section 3.10 below). The findings by Chami et al. [2005] have been critiqued, though the study is still generally discussed in a favorable light [Agunias, 2006:34 reviews these critiques].

It is not likely that further empirical research will generate a consensus on the link between remittances and growth. This is because research must first resolve a rather large number of methodological and empirical issues that do not lend themselves to certainty, such as how to measure the diverse multiplier effects and leakages associated with remittances, how migration affects labor markets and hence wages in sending countries, the characteristics of emigrants and of the households that receive remittances, and whether emigration is a temporary response to an economic shock or is instead a permanent response to existing opportunities and constraints. The answers to these questions condition the effects that remittances will have on economic growth.

For example, if remittances primarily go to the poorest households, they will be used for subsistence consumption rather than investment. If emigrants are primarily drawn from the high-skill segment of the labor pool, then they may have a negative effect on economic growth (because output in the country of origin suffers, and because these workers cannot be replaced without training, an activity that requires both time and resources) [Solimano, 2004; Nayyar, 2008]. If emigration is temporary (or the commitment to send remittances only extends for a limited time), then remittances provide a transitory boost to consumption, investment and/or growth [Solimano, 2004]. But if commitments to send remittances are long-term in nature, then the effect of remittances may be more sustained. And, the extent to which remittances can raise economic growth in the short- or medium-term depends on whether the increase in consumption associated with remittances induces an increase in imports and/or inflation, and whether the departure of migrants reduces domestic output [Nayyar, 2008:22-24]. Further complicating research on the relationship between remittances and growth is the fact that the effects of remittance-financed investments in physical assets and human capital are necessarily indirect and long-term [Ratha, 2007].

Finally, the precise nature of the migration dyad will condition the effect of remittances on economic growth. If a greater proportion of total migration is South-South as opposed to South-North in nature, then remittances can be expected to have smaller effects on economic growth in migrant-sending countries. This is because there is some evidence that remittances that stem from South-South migration have smaller multiplier effects on the economy than do those associated with South-North migration [Ratha and Shaw, 2007]. The one study of the subject suggests that those who travel to other developing countries for work earn lower wages, are more likely to migrate for short periods, are subject to greater exploitation, and are more likely to be expelled than those who migrate to wealthy countries [Ratha and Shaw, 2007]. However, it is difficult to determine the true scale of South-South migration since so much of it is undocumented.

6. Public investment and the effect on state behavior in developing countries

There is unequivocal evidence that remittances support some public investment by providing capital for health clinics, land, wells, irrigation, equipment, and education in particular communities [Solimano, 2004; Kapur, 2004; see Ratha, 2003 for numerous examples].

Scholars and policy analysts have devoted a lot of attention to the role that remittances have played in financing public investment in Mexico. Organized “home town associations” of migrants have pooled and channeled remittances for public projects and small businesses in their towns of origin. The Mexican government tried to leverage these remittances through an evolving matching program. Beginning in 1993, the Mexican state of Zacatecas introduced the “two for one” (i.e., the *Dos por Uno*) program, in which both the federal and state government matched one dollar that home town associations contributed to development projects in Zacatecas.³¹ In 1999, the program expanded to include local governments and became the “three for one” (*Tres por Uno*) program, encompassing not just the state of Zacatecas, but also other Mexican states, such as Guanajuato, Jalisco, and Michoacan. In the Mexican state of Zacatecas, more than 400 public projects and small businesses (valued at \$4.5 million) have been capitalized by the state’s home town associations over an eight year period [Solimano, 2004]. In 2005, Mexican home town associations raised about \$20 million for development projects throughout the country, which was matched by \$60 million in Mexican federal, state and local government contributions [Orozco and Rouse, 2/1/07]. In El Salvador, the national development agency FISDL developed a similar program to match the funds of Salvadorean home town associations (called *Unidos por la Solidaridad*) [see Orozco and Rouse, 2/1/07; Burgess, 2007, and citations therein for details]³².

The Mexican government’s effort to leverage the contributions of its home town associations has been widely praised, though the match had to be suspended because the state budget for the program was depleted because so many associations applied for the match [Chi, 2008: p. 519]. However, some analysts suggest that there are often problems maintaining the public projects that are financed by remittances [Kapur, 2004], that the types of projects selected are not necessarily those that have the largest payoff to the public [Burgess, 2007], and that these projects might actually facilitate future migration instead of enhancing the economic vitality of the community itself (by providing job training that can be better utilized elsewhere) [Burgess, 2007; Kapur, 2004].

Home town associations are not just a Mexican and Salvadorean phenomenon. A study by Orozco and Rouse [2007] details the activities of associations of Mexicans, El Salvadoreans, Guyanans, Jamaicans, Ghanaians, Filipinos, and Malaysians living in Japan. At this time we do not have information sufficient to assess the contribution to public investment made by these associations. The only information that we do have pertains to Mexico. In Mexican home towns with fewer than 3,000 people, donations by

³¹ Discussion in this paragraph draws heavily on Orozco and Rouse [2/1/07].

³² Other partnerships in El Salvador are described in Orozco and Rouse [2/1/07], as is a program to leverage remittances that Western Union began in Mexico in 2005.

home town associations are equal to more than 50% of the money in municipal public works budgets; in towns with populations under 1,000 people, donations by these associations can amount to up to seven times the public works budget [Orozco and Rouse 2/1/07].

Some analysts have suggested that home town associations are not only a vehicle for financing public investment, but also are a means to reduce “remittance decay,” i.e., the tendency for remittances to be curtailed the longer a migrant is away from home [Kapur, 2004]. This phenomenon has not received much systematic study, and we therefore cannot say whether remittance decay occurs and, if so, whether collectivized remittance programs curb the phenomenon.³³

In sum, there is little that can be said about the significance of remittance-financed public investment across the developing world since we do not have a cross-country data set on the subject. Until such data are available, we can only assume that the effect of remittances on public investment is necessarily localized.³⁴

More importantly, it is vitally important that analysts investigate whether state-behavior in developing countries is influenced by remittance-financed public investment. Does private (i.e., remittance-based) financing of traditional sites of public sector investment create public moral hazard, as we suggested in our earlier discussion of private investment in physical assets and human capital (section 3.4)? That is, does the support by remittances for some types of public investment crowd out or crowd in public investment? If remittances catalyze public investment that would not otherwise occur, then naturally the net effect is positive (and perhaps substantial). But if remittances crowd-out public investment by inducing a public moral hazard, then their contribution may be marginal or even negative. To date, we are not in position to say much about whether the programs that some governments have introduced to increase and mobilize remittances actually represent a net increase in public financing for public projects. It may very well be that these new institutional forms mask a net reduction in public finance. Public moral hazard might unfold behind the backs of those sending and receiving remittances, rather than right before their eyes.

7. Remittances and economic stability

As discussed in section 2.5, there is unambiguous, plentiful evidence that remittances function as a shock absorber in low-income countries by providing critical income support after economic shocks, natural disasters and civil conflict [Kapur, 2004; WB, 2006]. As also noted, many studies find that remittances increase after these events

³³ One study of the subject by O’Neil [6/1/03] notes the existence of remittance life cycles that vary across cultures, countries and economic conditions. The study notes that Indian migrants in the USA generally stop remitting within one generation, whereas many Koreans in Japan continue remitting two generations after migration. In many cases, if one migrant in a family returns home or stops sending money, a replacement remitter often migrates

³⁴ This speculation is supported by Lindsay and Gerova [2004] who note that not quite 5% of Mexicans surveyed report having sent remittances for collective purposes. On this basis, they conclude that collectivized remittances to Mexico have little nationwide effect.

[Clarke and Wallstein, 2004], not least because they encourage people to migrate in the first place [Ratha, 2003].

For example, Yang [2004] found that remittances to Philippine households increased after the 1997 financial crisis. They rose as a share of personal consumption in response to the financial crisis in Mexico in 1995 and in Indonesia and Thailand in 1997; they continued to rise as a share of personal consumption after natural disasters in Bangladesh, the Dominican Republic, Haiti and Honduras; they increased in Albania shortly after the economic and political crisis of 1997, and fueled a recovery in the economy by 1998 [Korovilas, 1998]; they remained substantial during the civil war in Cote d'Ivoire, and increased in Sierra Leone after its conflict [WB, 2006:99-100, fn24]. Yang [2005] also finds that after a hurricane the increase in remittances compensates for 13% of the income losses in the year of the event and 28% of the income losses in the first four years afterwards. Remittances also increased during Hurricane Mitch in Central America, and they were a critical means of support for the vulnerable during Lebanon's civil war [Ratha, 2007; Kapur, 2004]. Remittances have also sustained consumption in Haiti and Somalia during periods of particular difficulty. These (and other) cases and data more generally provide strong evidence that remittances are counter-cyclical and function in part as a shock absorber and as a mechanism that facilitates adjustment to crises.

It is worth noting that shocks of any sort often cause significant currency depreciations and recessions. This necessarily increases the value of remittances sent in hard currency [Kapur, 2004] and thereby increases the benefit of having family members who migrate to hard rather than soft currency countries (i.e., wealthy versus developing countries).

Kapur [2004] notes that in the 1990s the Cuban government came to recognize the role of remittances as a crucial source of social insurance and foreign exchange. Previously, the government curbed remittances as they were thought to come from the country's largely politically hostile diaspora community. But in the early 1990s the government began to court remittances (through a variety of incentive programs to residents receiving dollars). This change in policy was brought about by the reduction in FDI and aid from the Soviet Union after its disintegration, the collapse in the world price of Cuba's principal export, sugar, and the tightening of the US embargo of the country.

The shock absorption role of remittances can mean life or death for vulnerable households in poor countries. In these countries governments may possess neither the material resources nor the political will to put shock absorbers in place for economically vulnerable and politically weak groups, especially in the context of a crisis.

The material support provided by remittances to the vulnerable during times of crisis is an achievement that can not be dismissed. But, in my view, the relationship between remittances and economic shocks is more complex than is generally understood.

One aspect of this complexity concerns the relationship between remittances and the neo-liberal reforms implemented in the developing world over the last thirty years. In this environment, states have curtailed the social programs and public institutional arrangements that traditionally helped the vulnerable to shoulder shocks (and, indeed, in some cases, reduced the likelihood of that these shocks would even occur). In the absence of public shock absorbers, remittances function as private mechanisms that displace the burden of adjustment to shocks onto transnationally-dispersed family networks.³⁵

Neo-liberalism also creates an environment wherein shocks of diverse etiology are more frequent and severe. This is because financial liberalization has increased the tendency toward financial instability; trade liberalization has displaced small farmers in the developing world; and the neo-liberal commitment to fiscal restraint and privatization has meant that states have eliminated many social programs that enabled the poor to sustain their basic needs [Chang and Gabel, 2004]. Thus, neo-liberalism increases the need for sturdy shock absorbers precisely when public mechanisms to do so have been retrenched.

A second complexity to consider is that though remittances do function as a shock absorber, they can also fuel financial instability within countries. The case of Albania is relevant in this connection, as Korovilas [1998] makes clear. He reports that remittances from Albanians working in Italy and especially Greece fueled the pyramid schemes in the country during 1995-96. These schemes attracted total deposits of \$1 billion-1.3 billion, which was equal to almost ½ of Albania's GDP in 1996. The collapse of the pyramids in January-February 1997 triggered the country's economic and political collapse. Interestingly, the crisis in the country was later stabilized through the remittances that were fueled by a new round of migration. This case suggests that there is a need for empirical research that examines whether remittances have induced speculative bubbles elsewhere.

A few cases also suggest that remittances can be a vehicle for transmitting instability or economic downturns across nations that are linked as remittance dyads. Any shock that causes remittances from a sending country to be reduced can ultimately undermine economic performance in the recipient country. Mutume [2005] describes precisely this dynamic between Burkina Faso and Côte D'Ivoire. The economy of Burkina Faso suffered when remittances to the country decreased dramatically following an economic and political crisis in Côte D'Ivoire, where many Burkinabè work. Kapur [2004:24] provides other examples of this type of co-variance. For example, conflicts in the Gulf States (including the Gulf War of 1991) have had negative effects on the economies that exported labor to this region, and the expulsion of Indonesian labor from Malaysia and Thailand during the Asian financial crisis exacerbated instability in SE Asia, increased tension between countries in the region, and weakened ASEAN.

³⁵ This point is different from (though not inconsistent with) that made by Burgess [2007], who argues that remittances are a reflection or symptom of neo-liberalism.

At the present juncture we are seeing similar downside co-variance between the USA and Mexico (and various countries in Central America). The slowdown of the US economy and the crises in the housing and financial sectors has resulted in a loss of construction jobs that were formerly occupied by migrants. Moreover, changes in US immigration policy have persuaded some potential migrants not to cross the border in the first place, has caused some to return home voluntarily, and still others to be forcibly deported.³⁶ Today anecdotal evidence suggests that the decline in remittances to Mexico associated with these changes in the US has been detrimental to living standards in many parts of Mexico [Malkin, 10/26/07].

The forced deportation of El Salvadorean migrants by the US government bears special mention in this connection. The issue has not been widely studied at this point, but anecdotal information on El Salvador suggests that changes in remittance patterns have affected the Salvadorean state in important ways. It has been reported that in 2004, 3500 migrants were deported to El Salvador by US Immigration and Customs Enforcement. In 2006, that number rose to 11,500, and in 2007, it rose again to 20,000.³⁷ Prior to the dramatic increase in forced deportations, one third of El Salvador's total population (of roughly 7 million) lived outside the country.

The remittances sent by these emigrants were important to the Salvadorean economy for the direct support they provided to the population. They were also important indirectly because they meant that the state did not need to provide healthcare, education and employment to the large proportion of the population that resided outside of the country. At present, state officials report that they are being overwhelmed by these deportees because they are making demands on the economy for jobs, education, and healthcare. In addition, slowing remittances to El Salvador have increased the rate at which residents have defaulted on their home loans since remittances were often used for mortgage payments. Thus, remittances are serving as an interesting and unexpected cross-national channel of contagion between the US' housing and financial crisis and the housing sector in El Salvador.³⁸

The Mexican and El Salvadorean cases suggest the need for future research that investigates the degree to which remittance dyads are vulnerable to co-variant shocks involving the transmission of economic contraction and instability across borders. The discussion of El Salvador suggests another direction for research on remittances and the state (that is distinct from our earlier suggestion that remittances may induce public

³⁶ The number of deportations from the USA has increased radically in the last few years. One report indicates that during fiscal year 2006 and 2007, the number of deportation proceedings went from 64,000 to 164,000 [Quirk, 2008]. In the 2008 fiscal year, that the number is expected to reach 200,000, an all-time high.

³⁷ All information on El Salvador in this and the next paragraph comes from National Public Radio (NPR) [4/9/08] and Bazar [2008].

³⁸ In addition, some of the deportees are bringing with them associations to US street gangs and organized crime (such as one Los Angeles street gang known as MS-13) resulting in the creation of transnational criminal networks in the Americas with concomitant problems for public safety. On the link between forced deportation and transnational gangs in the Americas, see Lopez, Connell, and Kraul [2005].

moral hazards). Future research should investigate whether the curtailment of remittances places particular burdens on states in developing countries at precisely the time that they can least afford to bear them.³⁹

In addition, future research might consider whether the vulnerability to co-variant shocks can be mitigated through policies that encourage the diaspora to disburse more broadly geographically. Diaspora dispersal can therefore be thought of as a hedging strategy. However, it must be acknowledged that the clustering of diaspora communities reduces the costs of migration, something that is particularly important to those groups (such as the poor) that may possess lower migration capabilities.

8. Financial services industry and the level of financial development

There is general consensus that rapid growth in the remittance market has begun to fuel changes in the financial services industry in both sending and recipient countries. These changes are seen by many analysts to be pushing formal banks to serve the “underbanked,” or “financially excluded,” who are the poor on both sides of the remittance transaction and small business people and agriculturalists in the developing world. In this connection, the Inter-American Dialogue [2006:14] concludes that remittances are a “critical first step on the pathway to credit for individual families...and reaching the goal of financial democracy for a nation.” In my view, it is still uncertain as to whether the various changes in the financial services industry fostered by remittances will ultimately prove beneficial for the underbanked.

Bankers increasingly recognize that there are substantial business advantages to capturing a share of the remittance market, a market that has traditionally been dominated by money transfer operators, such as Western Union. These operators have come under fire for their extremely high fees (that function as a regressive tax on migrants and their families) from sources ranging from former Federal Reserve chair Alan Greenspan, migrants’ rights groups, and the Mexican government. Under this pressure, the fees charged by money transfer operators and banks in wealthy-remittance sending countries have been lowered, and formal banks have made aggressive inroads into this market.⁴⁰

Banks in the USA (and elsewhere) have introduced a number of innovative products in order to capture a share of the remittance market, e.g., “Smart Cards” and new types of ATM, savings, and checking products [for details, see Dymski, 2004; Inter-American Dialogue, 2004 on initiatives in the USA; Mutume, 2005 on France]. Some banks in the USA have made it easier for migrants in the country to open bank accounts (and hence, to send remittances through formal banks) by accepting consular identification cards that are issued by the Mexican and Guatemalan governments. These cards are issued

³⁹ To date the literature on remittances has taken little notice of the political and social upheavals caused by the diminution of remittances due to forced deportations. Van Hear [6/1/03] briefly notes that the curtailment of remittances could lead to socio-economic or political upheaval and even the resumption or provocation of conflict. This is a matter that clearly warrants further exploration by scholars.

⁴⁰ Orozco and Lindley’s publication, *Migrant Remittances* [various issues] provides extensive coverage of this issue. It has been estimated that Sub-Saharan African countries could raise \$1 billion to \$3 billion by reducing the cost of international remittances [Ratha, Mohapatra and Plaza, 2008].

regardless of the legal status of the migrant. At the same time, however, the use of consular identification cards and other efforts to “normalize” the status of illegal migrants in the USA has fueled an aggressive backlash against migrants.

Changes in US banking, security and immigration regulations after September 11, 2001 (particularly, the Financial Action Task Force) have also had cross-cutting and uncertain consequences on the sending side of the remittance market. On the one hand, many informal operators have been closed due to security concerns, and formal operators (both money transfer organizations and banks) must adhere to new identification and reporting requirements. The closure of many informal operators and the reduction in the fees charged by formal operators and formal banks may have increased use of formal institutions by migrants. On the other hand, greater fears of deportation may well have pushed many migrants to rely on informal operators that function even further below the radar of immigration and security authorities. Such operators may be expected to charge substantially higher fees than formal operators.

Finally, it may be that a variety of innovations in other markets make money transfer operators and formal banks less central to remittance transactions. Telecommunications innovators and microfinance institutions are beginning to offer services that enhance access to and lower the cost of remittances. Pilot programs involve using the internet and cellular phones to send remittances; some microfinance institutions are also incorporating remittances into the mission [see Orozco and Lindley, various issues]. These innovations offer clear benefits to senders and recipients of remittances by lowering their costs significantly.

Business opportunities on both sides of the remittance market have been among the chief catalysts for the increase in cross-border bank mergers and FDI in banks in developing countries, especially in Mexico. Should this trend continue, it is possible that these investments will help to expand the portfolio of services offered by formal banks in developing countries [Kapur, 2004]. An article in a banking industry publication put the matter quite bluntly: “banks look to money transfers not only as a valuable fee earner, but also as a customer acquisition and cross-selling vehicle” [Bank Marketing International, 2006:14, cited in Dymski, 2004]. Efforts to expand the market for financial services could redound to the benefit of the underbanked in the developing world. A promising recent development along these lines is the emergence of North-South bilateral dialogues aimed at increasing the flow of remittances through formal channels by reducing costs on both sides of the transaction. Five such dialogues have had concrete results--namely between the USA and the Philippines, US-Mexico, US-Colombia, Germany-Turkey, and Canada-India [Martínez, 2005].

There are several complications to consider when thinking further about whether remittance-driven FDI and mergers in developing country banking systems will reduce financial exclusion. Some recent studies find support for the intuitive idea that foreign banks and large banks engage in “cherry picking”—lending only to the largest and most creditworthy borrowers--in some regions of the developing and post-Communist world [e.g., Crotty and Lee, 2005; Weller, 2001], whereas others find no support for this

behavior [e.g., Crystal, Dages and Goldberg, 2001; Clarke, Cull, Martinez Peria, and Sánchez, 2003; Epstein, 2008]. If future research substantiates the case for cherry picking, then remittance-driven FDI and mergers in developing country banking will not ameliorate financial exclusion unless perhaps changes in institutional behavior can be brought about via policy reform. We must also recall that banking systems in developing countries are already heavily concentrated. There is no reason to expect that banks operating in an even more concentrated environment will have an incentive to meet the needs of poorer consumers and small businesses. Relatedly, Julca [2007] argues that remittances themselves may reinforce existing patterns of concentration in the financial systems of developing countries since, in most cases, very few domestic banks monopolize the domestic market (e.g., six major commercial banks holds most of the remittance market in the Philippines).

To date, a few researchers have examined the issue of whether remittances promote financial development, which is most often measured by changes in the aggregate level of deposits in the formal banking sector and the amount of credit intermediated by these banks.⁴¹ For example, Aggarwal, Demirgüç-Kunt, and Martinez Peria [2006] find that remittances have a positive effect on financial development. Using data for 99 countries from 1975-2003, they find that the receipt of remittances is associated with an increase in the aggregate level of deposits and the amount of credit intermediated by local banks. Martínez Pería, Mascaró, and Moizeszowicz [2008] find that remittances increase bank deposits and bank credit in Latin America; Calderón, Fajnzylber and López [2008] find that remittances are more effective in increasing investment and enhancing growth in Latin American countries with less developed financial sectors. These results are encouraging. But we must acknowledge that an increase in the total amount of credit intermediated tells us nothing about which groups are the recipients of this new pool of bank loans, and whether the financial development that is fostered is pro-poor in nature.⁴²

9. Public sector borrowing costs and credit ratings

An interesting and unexpected effect of remittances is that they have been used in some countries to lower government borrowing costs and to lengthen debt maturities on public issues via complex transactions that securitize future flows of remittances. One study of the matter estimates that as of 2001, developing countries had \$4.3 billion per year of remittances that were suitable for future flow securitization, and a total of \$65 billion per year in total future flow receivables, involving oil exports, and credit card, airline ticket, telephone and credit card receivables [Ketkar and Ratha, 2001].

Recent studies have reported that Brazil, El Salvador, Mexico, Panama and Turkey have securitized remittances along with other future-flow receivables [Ketkar and Ratha,

⁴¹ Note that there is a large body of neo-classical literature (that I will not discuss here) that links increased financial development with increased economic growth across countries, firms and industries, and with reduced poverty and inequality [see review in Aggarwal et al., 2006].

⁴² See Epstein and Gabel [2006] on pro-poor financial policies.

2001, 2003; WB, 2006].⁴³ Mexico was the first country to use remittances in this manner in 1994 (having pioneered future flow telephone receivables in 1987). The volume of remittance securitization has grown rapidly since then. In August 2001, Banco do Brasil issued \$300 million worth of bonds with a five year maturity using future yen remittances from Brazilian workers in Japan as collateral. These bonds were issued on terms that were considerably less costly to the government than other Brazilian sovereign issues at the time, and the remittance-securitized bonds received a higher credit rating by Standard and Poors (namely, a BBB+ rating, compared to a BB- rating on non-securitized bonds). In the case of El Salvador, remittance-backed securities have received investment grade ratings, two to four levels above the country's sub-investment grade sovereign rating. Mexico, El Salvador, and Turkey raised about \$2.3b during 1994-2000 using this financing strategy. In 2004, over \$1b was raised through securitization of remittances.

Ratha, Mohapatra and Plaza [2008] note that the African Export-Import Bank has been active in facilitating future flow securitization since the late 1990s. The same study estimates that Sub-Saharan Africa could raise \$2 billion annually by securitizing future remittances (and a total of \$17 billion annually by securitizing total future flow receivables).

There are clear benefits to developing country governments of securitizing remittances. Enhancing a country's credit rating on sovereign debt provides the opportunity for longer maturities, lower borrowing costs and gives the government access to a wider ranges of investors because some, such as insurance companies, are prohibited from purchasing sub-investment grade bonds [Ketkar and Ratha, 2001; WB, 2006].⁴⁴ Moreover, there is some speculation that by improving a country's credit history, remittance-securitized debts enhance the government's future borrowing prospects as well [WB, 2006].

But even enthusiasts acknowledge that there are significant obstacles in the way of more widespread use of securitization in the near future. For example, Ratha et al. [2008] acknowledge that there are numerous risks and institutional constraints to expanding future-flow securitization in Sub-Saharan Africa. These obstacles include the high, fixed legal costs that are associated with structuring these deals, the inflexibility of securitized debt (which can undermine a nation's credit rating, and hence increase the cost of raising capital), and the provisions in many multilateral loan and guarantee agreements that prohibit the prioritization necessarily afforded to securitized debts over other types of debt, such as those owed to multilaterals [WB, 2006:103-04].

⁴³ See Ratha and Ketkar [2001] and WB [2006:103-04] for details on how these complex deals are structured.

⁴⁴ Though they do not discuss securitization, Chami et al. [2008] argue that remittances themselves can reduce country risk and improve the sustainability of government debt (by increasing the government's revenue base and reducing the marginal cost of raising revenue). However, they suggest that this benefit is pyrrhic insofar as it may induce governments to become more indebted and may reduce fiscal discipline. The latter argument points to another type of public moral hazard that Chami et al. [2008] associate with remittances.

In addition to the legal and institutional obstacles, we must also consider that securitizing future remittances can aggravate financial vulnerability in developing countries. The benefits of greater access to cheaper credit afforded by the securitization of remittances must be weighed against the costs of greater public sector debt burdens. This may increase the considerable repayment pressures and financial fragility already faced by developing country governments. The addition of inflexible securitized debt certainly stands to aggravate these risks, and may further narrow the policy space available to governments.

Moreover, in my view, the current crisis in the US' financial and housing markets highlight the risks and financial fragility induced by complex financial innovations like securitization that rapidly increase liquidity, even in mature financial markets. Indeed, one is reminded here of the wisdom of John Maynard Keynes' [1964: ch.12] concerns about the destabilizing effects of excess liquidity in financial markets, and of Hyman Minsky's 1987 observations about the macroeconomic costs incurred by acting on the view that "that which can be securitized, will be securitized" [cited in Minsky, 2008: p.2]. It is therefore essential that policymakers in developing countries proceed with extreme caution when securitizing remittances (and any other future financial flows).

10. Labor force participation and labor markets in remittance-receiving countries

A few studies find limited evidence that the receipt of remittances reduces labor force participation in recipient households. This phenomenon tends to be described in terms of moral hazard or a "culture of dependence" that develops once households come to expect remittances.

As noted in our earlier discussion of economic growth (section 3.5), Chami, Fullenkamp and Jahjah [2005] is the most widely cited study of moral hazard and remittances. They find that remittances discourage work effort on the part of recipient households that chose "leisure" over labor, and that the reduction in labor effort may translate into reduced economic growth.⁴⁵ A few studies have found that the negative effect on labor force participation is greater for women than for men. For example, Funkhouser [1992] finds evidence of a stronger negative effect on women's labor supply in Managua, Nicaragua (namely, that an increase in remittances received from zero to \$100 decreases the probability of labor force participation by 2.1% for males and 5.0% for females). Hanson [2005] finds support for this gendered phenomenon in Mexico, as does Amuedo-Dorantes and Pozo [2006] for women in rural Mexico. Acosta, Fajnzylber and López [2008b] find that remittances do reduce labor supply in Latin America, though mostly for individuals with low levels of schooling.

In my view, it is mistaken to think of the shifting work burdens that remittances may bring about as an instance of moral hazard. First, reduced labor force participation by some remaining family members (particularly, children and mothers without access to daycare) is at the heart of the bargain involved in the decision to send a family member

⁴⁵ Again, recall that this study has been widely criticized on methodological grounds. More recent work by Chami et al. [2008] maintains the view that remittances have a negative effect on work effort, but this new work does not find evidence that remittances reduce economic growth.

abroad to work. This might better be thought of as an altogether appropriate, integrated strategy for the household, rather than a strategy by some family members to take advantage of others. Second, there may be good reasons to celebrate a backward bending supply of labor by some family members, particularly in light of evidence that the incidence of infant mortality is reduced by declines in labor force participation by mothers [Duryea, et al., 2005], and other research that finds that remittances reduce labor force participation and increase schooling among children in the Philippines [Yang, 2003]. We should keep in mind in this connection that women face substantially greater work burdens than do men across the developing world, especially once work in the informal sector is properly taken into consideration. We might therefore welcome the leveling effects of remittances on household labor contributions.

Finally and alternatively, it is also possible that in some cases reduced labor participation by remaining family members may have little to do with personal choice and much more to do with structural factors. For instance, and as mentioned above, “employment deserts” may arise in communities or regions that experience large-scale migration and are left with no viable local economy. Relatedly, Kapur [2004] suggests that remittances create vast “migra-villages” whose subsistence comes to depend on remittances.⁴⁶ Research has not made clear to this point whether the employment desert/migra-village phenomenon is a short- to medium-term development (as De Haas [2005] suggests).

To date, the general effect of remittances on wage levels in the home economy has not been addressed by empirical research. Even when investigated, this matter is not likely to be resolved unequivocally since, as discussed earlier, we cannot generalize about positive, intermediate or negative selection effects in migration (as discussed earlier in sections 3.1 and 3.2). Another related matter that has not been addressed is whether the receipt of remittances increases the reservation wage of those remaining in the home country.

11. Brain drain versus brain gain

To date, there has been limited examination of whether remittance inflows and the possible accretion of skills garnered by working abroad (i.e., “brain gain”) ultimately offset the output and social losses associated with a reduction in a country’s supply of skilled labor (i.e., “brain drain”).

Two studies conclude that the benefits of brain gain partially offset brain drain [Ratha, 2003; De Haas, 2005, based on research by Adams, 2003].⁴⁷ This is because the country of origin may benefit over time from the networks and knowledge that skilled workers develop abroad [Ratha, 2003: 164, 168, fn12], and from the economically beneficial effects of the remittances, investments, trade relations, and attitudes that may

⁴⁶ The contradictory effects of remittances are further noted by Kapur [2004]. Remittances to some parts of Latin America finance the construction or purchase of new homes that largely stand empty because their owners live in the USA, and they also finance the improvement of schools that face declining enrollments as new rounds of migration are facilitated by remittances.

⁴⁷ Taylor [2006] mentions this as well, but does not elaborate on the argument.

accrue to the country of origin in the medium and long-run [De Haas, 2005]. De Haas [2005] also concludes that the prospect of moving abroad stimulates the incentive to study among those that remain behind, and that the export of skilled labor is seen by some governments as an export product that generates remittance inflows. In the latter case, he points to the example of the Philippines where national investment in nursing education is an integral component of the state's export and remittance strategy.

A few other studies reach the opposite conclusion on brain gain, drain, and remittances. Kapur [2004] and Nayyar [2008] argue that there are many reasons to expect that brain gain will not offset even partially the negative long-term economic effects of the loss of human capital embodied in a country's most educated workers. One reason for this is that capital flight generally precedes brain drain. Thus, a country loses not just skilled labor, but also financial capital, two factors that are essential to development [Kapur, 2004]. Moreover, the loss of a country's most educated and/or skilled workers reduces the productivity of those left behind, especially since the skilled labor that leaves the country cannot be replaced immediately without costly and time-intensive training [Nayyar, 2008].⁴⁸ In addition, the brain drain and the creation of economic deserts may provide a disincentive for governments in the sending countries to invest in transportable human capital, since the benefits of such investment will accrue primarily abroad.

There is today no clear consensus among the few analysts who have studied the relative costs of brain drain versus brain gain. In my view, the long-term economic and social effects of brain drain are unlikely to be offset fully by the beneficial effects of brain gain and the inflows of remittances associated with emigration by skilled labor. Not least are the difficult to measure but no doubt enduring social and political consequences of losing a country's most educated and skilled citizens. This loss may degrade the quality of civic life and political "voice" (in the sense of Hirshman, 1986) by removing those most capable of being efficacious advocates of governance improvements in the country. Making matters worse, De Haas [2005] suggests that remittances may give recipient families the means and incentive to withdraw from social and economic activities in their country of origin because they are economically insulated from its problems. If this is correct—if the exit afforded emigration also extends to the families they leave behind—then we may find in some contexts that those most dependent on public services and are left alone to fight for good governance. Finally, it also may be that more significant than any output losses directly associated with brain drain are the even larger opportunity costs associated with the unemployment or under-employment of the most educated segments of the population who remain behind in the employment deserts created by migration.

All of this calls for case studies that feature careful empirical research, to be sure. But as with so many of the matters before us, the pathways by which the brain drain and brain gain associated with migration and remittances affect development are terribly

⁴⁸ However, if the emigration of skilled labor is temporary rather than permanent, then it is possible that the enhancement of skills by migrants while abroad and the utilization of such skills on return may increase productivity and output in the country of origin [Nayyar, 2008:22].

complex, with effects that are both short-term and long-term, and direct and indirect. We should not anticipate clarity on this matter anytime soon, or uniformity in effects as we move from case to case.

12. The Dutch disease

The Dutch disease has traditionally referred to the currency appreciation caused by sudden, large capital inflows to a country with floating exchange rates. This appreciation can undermine export performance. There is some evidence that remittance inflows induce a Dutch disease effect, though there is still controversy about the matter. However, several governments—namely, that of El Salvador, Kenya, and Moldova—have expressed concern about the effect of large remittances on the exchange rate [Ratha, 2007].

Some analysts argue that remittances have induced strong Dutch disease effects [Fajnzylber and López, 2007; López-Córdova and Olmedo, 2006; Julca, 2007:9; Solimano, 2004:14]; others conclude that this effect is particularly important in small countries, where remittances are very high in proportion to the size of the economy [Kapur, 2004:20-1]. Evidence in support of a remittance-induced Dutch disease appears in Chami et al. [2008], in Ameudo-Dorantes and Pozo [2004], who find that a doubling of remittances resulted in a real exchange rate appreciation of about 22% in 13 Latin American and Caribbean countries between 1979 and 1998, in Rivera's [1999] work on El Salvador, in Bourdet and Falck's [2003] work on Cape Verde, in Hossain's [1997] work on Bangladesh, and in López, Molina, and Bussolo's [2008] work on Latin America.⁴⁹ Acosta, Lartey, and Mandelman [2007] find support for the Dutch disease in El Salvador, though they find that the negative effect on export competitiveness derives not only from the exchange rate effect of remittances, but also from the way that remittances influence labor markets. Lartey, Mandelman and Acosta [2008] report similar findings for a large sample of developing countries.

Other studies take the view that remittances induce smaller Dutch disease effects than do other types of international capital flows. It is argued that this is because remittances tend to be stable, persistent and grow gradually over time [WB, 2006:104]. Therefore, the effect on exchange rates is less significant than with other types of capital inflows that are prone to windfall effects and/or are cyclical in nature. One study stands as an outlier in the literature: Rajan and Subramanian [2005] find no evidence that remittance flows undermine growth by negatively affecting export competitiveness.

Obviously, the matter of whether remittances induce a Dutch disease effect warrants further empirical research. But, in my view, it seems reasonable to conclude that large inflows of remittances, especially over a short period of time, necessarily have the same effect on the exchange rate as do other surges in international public or private capital inflows.

13. Social effects on recipient countries

⁴⁹ Nayyar's [1994] work on India notes that remittances have effects on the exchange rate.

There are a few studies that discuss the contribution of remittances to social conditions in recipient economies. However, this is an area that has received far less attention than has been devoted to analysis of any single economic effect that we have thus far discussed.

I discussed earlier the creation of migra-deserts, a phenomenon that is associated with the migration-remittances-migration cycle (see section 3.10 above). At this juncture we should acknowledge that there are significant human costs associated with this cycle. These costs are borne by families that are separated geographically (often times over long periods), and by the children who are left behind to be cared for by relatives. Frequently it is mothers who migrate to wealthy countries to care for the children of others, for the sick, or for the elderly.⁵⁰ So resonant are the hardships borne by those left behind that they are a common feature of popular culture in places like the Philippines, where poetry and soap operas depict the stresses borne by separated families [see DeParle, 4/22/07]. Though it is important that research investigate the issue, it seems reasonable to assume that the social benefits of remittances (particularly, support for investment in human capital by poorer families) cannot outweigh the social harm associated with large numbers of missing parents in developing countries.

An important consideration that has received little attention in the literature is the effect of remittances on gender relations in developing countries.⁵¹ One study argues that the receipt of remittances may empower women by facilitating their involvement in politics at home [Weyland, 2004].⁵² However, two studies conclude that remittances may not necessarily empower women. Rudkin [1993] finds that remittances tend to go to men rather than to women. Mahler [2006] finds that female recipients are excluded by government officials in Mexico from deciding how collective remittances are to be spent, and that female migrants in the Philippines are disproportionately blamed for family disintegration while their non-migrant husbands who squander remittances are portrayed as sacrificing for their families.

Obviously, we know very little at the present time about the social effects of remittances. Examination of these (and, as we will see below, the political) effects of remittances is fertile ground for cross-disciplinary research that uncovers their complex and cross-cutting effects.

14. Political effects on recipient countries

As in the case of social effects, there is a great need for research that illuminates the diverse political consequences of remittances on recipient countries. To date, the scant body of research on the domestic politics of remittances has focused on four lines of inquiry.

⁵⁰ Enloe [2000] discusses the contradictions within the relationship between transnational dyads of mothers.

⁵¹ Citations in this paragraph are drawn from Agunias' [2006] survey.

⁵² Recall that we earlier discussed research that finds that remittances increase the ability of girls to remain in school (see above, section 3.4).

A first line of inquiry connecting remittances and domestic politics centers on the way that a few governments have tried to keep their diaspora community engaged through remittances (as well as through other types of international capital flows, such as FDI and PI).⁵³ Only the governments of the Philippines and Mexico have had an active policy that targets remittances. In the case of the Philippine government, it appears that a policy aimed at maximizing the inflow of remittances is being conflated with the articulation of a publicly-funded national development policy. The Philippine government seeks to maximize the income stream of remittances to households through various programs and services that facilitate international migration. Earlier we discussed the Mexican government's effort to promote collectivized remittances through matching programs aimed at increasing the contributions made through home town associations.

The Eritrean government has attempted to direct individual remittances into government channels. Since independence the country's diaspora has been asked to pay two percent of their income to the state as a 'healing tax.' During the conflict with Ethiopia, even greater demands were made of the diaspora. Indeed, Van Hear [2003] notes that contributions by the diaspora financed much of the conflict, an issue to which we return below.

Other countries have sought to harness the financial contributions of their diasporas through other channels. One such channel is through the sale of diaspora bonds, which Ratha, Mohapatra and Plaza [2008] define as a debt instrument issued by a country—or, potentially, by a sub-sovereign entity or a private corporation—to raise financing from its overseas diaspora. Diaspora bonds are often issued in times of crisis and often at a 'patriotic' discount. The Indian and the Israeli governments have for some time been selling diaspora bonds to support their budget and also to keep the diaspora engaged.⁵⁴ India and Israel have raised \$11 billion and \$25 billion respectively from diaspora bonds [Ketkar and Ratha 2007]. Other countries have been experimenting with such bonds. [See the discussion of diaspora bonds in Lindsay and Gerova [2004] and also see Ratha et al. [2008] for details on South Africa's Reconciliation and Development Bond (aimed at expatriate and domestic investors) and Ghana's Golden Jubilee Savings Bond (aimed at its diaspora)]. Ratha et al. [2008] estimate that Sub-Saharan African countries could raise \$5-10 billion annually by issuing diaspora bonds.

A second and related line of inquiry that connects remittances and domestic politics more directly focuses on the complex and contradictory role of this resource in supporting existing political and/or economic regimes, in contributing to internal political transformations, and in fueling some conflicts.⁵⁵ One study mentions that remittances

⁵³ With the exception of the discussions of the Ethiopian-Eritrean conflict and of diaspora bonds, the discussion in this and the following two paragraphs draws on Newland and Patrick [2004].

⁵⁴ See Lindsay and Gerova [2004] for discussion of many issues related to diasporas and economic development. See Newland and Patrick [2004] on the ways that China harnesses its diaspora to attract FDI and to open trade channels and Taiwan deploys the human capital of its diaspora.

⁵⁵ Except when noted, discussion of these issues draws on Agunias [2006].

enable migrants to serve active and important roles in national and village politics. It explains that migrants from the Dominican Republic have had an especially long history of political involvement with their country via large campaign donations. And remittances from the Philippine diaspora were thought to provide crucial support to pro-democracy forces that ultimately ended the regime of dictator Ferdinand Marcos.

In other cases, however, the political effects of remittances have been far from benign. Remittances have provided funding for civil and border wars (as we noted above in connection with the Eritrean-Ethiopian conflict) and have also provided crucial support for some secessionist movements. In the latter context, Seddon [2004, cited in Agunias, 2006] notes that remittances from the Sri Lankan Tamil diaspora contribute to the Tamil secessionist struggle, and that the Indian Hindu diaspora in the UK contributes money to extremist groups in India. There is much work that needs to be done not only to substantiate these claims, but also to investigate their broader relevance. In particular, it is important to know if remittances leverage the voice of diaspora communities (unduly) relative to those who remain at home.

Finally, Van Hear [6/03] mentions that curtailment of remittances due to forced deportation could fuel the resumption or provocation of conflict. This provocative suggestion is consistent with our earlier discussion of remittances as a possible vehicle for transmitting instability (see above section 3.7), but more research is clearly needed to substantiate a systematic connection between remittances and conflict.

A third line of inquiry on remittances and domestic politics concerns their effect on national economic policy choices. A study by Banuri [1986] suggests that remittances may make it more difficult or costly for governments to sustain particular policy regimes. Writing in the 1980s, when flexible exchange rates were not the norm in developing countries, Banuri [1986] argued that remittance inflows make it harder for governments to maintain highly valued exchanged rates and tariff barriers designed to protect investment and profits in the industrial sector. This is because remittances weaken capital controls and increase the size of currency black markets. For this reason, countries that receive large remittances will tend to adopt flexible exchange rates (despite any preference to the contrary by the government), and the economy's aggregate investment portfolio will shift toward agriculture and services and away from industry. Thus, in this case, remittances make it harder for a government to sustain a regime that protects national industry from international competition.

There are a few studies that suggest a different dynamic, that is, that remittances can actually protect national governments and particular sectors of the economy from the consequences of poor or misguided policy decisions. In this connection, Agunias [2006] likens remittances to continuous IMF bailouts with no strings attached. We can think of the protection that remittances offer to governments as the public sector equivalent of the social insurance function that they play for households (as we discussed previously in section 3.7). For example, in work on the Philippines, Aldaba [2004, cited in Agunias, 2006] argues that remittances insulate the economy from the negative impact of bad policies and from the need to correct economic imbalances. This is because the

government is able to count on annual, large infusions of foreign exchange from remittances. Russell [1986: p. 687] and Ecevit and Zachariah [1978: p. 37] mention that the support provided by remittances makes it possible for governments to overlook the problems of unemployment, underdevelopment and inequality that lead to migration. Glytsos' [2002, cited in Agunias, 2006] work on the Mediterranean argues that remittances insulate governments from the need to restructure their economies to adapt to changes in the world economy. Julca [2007:9] uses the term remittance disease to refer to the insulating effect of the consumption support provided by remittances. This support allows developing country governments to ignore the negative effects of changes in the composition of trade and production. For example, he argues that the income support provided by remittances protected the Mexican government from what might have otherwise been significant public unrest over the shift to higher priced imported corn.

In the theoretical model of Chami et al. [2008], the economic support provided by remittances reduces the state's incentive to pursue needed economic reforms. This is the case for two reasons. The support provided by remittances may give households less motivation to press for improvements in the economic environment. In addition, the countercyclical nature of remittances reduces the likelihood of financial crisis, an event that often forces governments to overcome reform inertia. In the view of the authors, it might be necessary for external actors, such as international financial institutions, to play a larger role in pressing governments to reform since the receipt of large volumes of remittances can otherwise liberate governments from this pressure. Were the theoretical arguments of Chami et al. [2008] to be substantiated by empirical research, then we might have to consider the possibility that remittances could create reform inertia, and could thereby serve as a rationale for policy activism by international financial institutions vis-à-vis developing country governments.

Future empirical research might uncover other ways that remittances may either compel governments to abandon particular policy choices, or may enable them to sustain policy regimes that might not otherwise be viable politically or economically.

A fourth and final line of inquiry on the politics of remittances concerns their potential to serve as an instrument of international relations. Kirshner's [1995] theoretical framework for investigating the ways that monetary power has been used to advance security-related or other non-economic goals might be used to study the power politics involved in the control of remittances. Cohen's [1998] work on the use of territorial currencies as a means to insulate a nation against foreign influence or constraint suggests another direction for research on the power politics of remittances. Kapur's [2004] brief discussion of three cases wherein the control of remittance flows figured into larger political strategies underscores the fruitfulness of research on the power politics of remittances. We describe these three cases to illustrate the kinds of connections that might be investigated in future research.

Earlier I discussed the Cuban government's concerns about the threat that it saw in the remittances from the country's politically-hostile diaspora. Whether this threat was

warranted or not is unclear, but the power of the perception itself indicates that it could be important to investigate if other governments have either courted remittances to sustain their power, or sought to reduce their flow because they might empower domestic opponents of the regime. Research on countries in the former Soviet bloc might be particularly interesting in this context.

Kapur [2004] also describes how remittances figured into the Israeli-Palestinian conflict. In September 2000, Israel began revoking the work permits of Palestinians. At the time, some 100,000 Palestinian workers from the West Bank and Gaza Strip crossed into Israel every day. In their place, Israel began importing workers from China, Thailand, Africa and the Philippines to work in agriculture and construction. The economic effects of the loss of remittances were devastating to the economies of the West Bank and Gaza (GNI per capita fell by 11.7% in 2001, and by a further 18.7% in 2002, while poverty levels jumped from 21% in 1999 to 46% in 2002). The drop in remittances had large indirect effects as well since the loss of income depressed demand for Palestinian goods, also led to a sharp decline in imports from Israel (and thus affected Israel adversely as well).

Finally, Kapur [2004] describes the way that freezing remittances figured into the US' post-9/11 strategy vis-a-vis Somalia. In 2001, the USA closed shut down the remittance channel of Al Barakat, a firm that was the dominant player in the country's remittance market, after labeling it the 'quartermaster of terror.' Since remittances to Somalia accounted for 25%-40% of the country's GNP, the effect of freezing the remittance funds in transit had devastating effects on the country's most vulnerable groups. Research that illuminates other cases wherein the control of remittance flows was part of a foreign policy strategy would be valuable.

15. Aid proclivities on the part of wealthy countries

To this point, I have examined the many issues raised by remittances entirely from the perspective of recipient countries.⁵⁶ A matter that has not yet received attention within the remittance studies literature is whether recent recognition of the empirical significance and counter-cyclical nature of these flows is having a behavioral effect on the aid proclivities of wealthy countries. It is at least possible that remittances provide a rationale or justification for governments that may already have political reasons to curtail ODA expenditures. If that is the case, then we would observe a reversal of the traditional "crowding out effect." Crowding out usually refers to the reduction in private activity induced by increases in public expenditure. If my supposition is correct, then remittances (i.e., a private capital flow) may well be discouraging ODA, a public flow.

All that we do know now about the matter is as follows. Net ODA to developing countries was stagnant from 1990-2003, and only began to increase modestly from 2003-06 (see figure 1 above). ODA has become increasingly unpopular politically in some wealthy countries, most notably in the USA. And finally, we know that skeptics of

⁵⁶ The only exception has been the discussion of the effects of remittances on the financial services industry, something that has influenced the pricing and business strategies of financial firms in wealthy remittance-sending countries.

ODA and of international aid bureaucracies have embraced remittances as part of what Adelman [2003] approvingly calls the new “privatized foreign aid”⁵⁷ and what the *Financial Times* (cited in Adelman) terms the “diaspora that fuels development.” In this view, remittances are superior to traditional (public) ODA because they have little to no overhead, they are not subject to misuse by state officials, and they efficiently and directly meet human needs in developing countries.

Admittedly, determining whether remittances have a crowding out effect on ODA will be difficult to demonstrate empirically insofar as assessment of this argument necessitates counterfactual information on the factors that influence ODA decisions. But given the concentration of remittances among developing countries (and even within regions of particular countries), and given all that we still do not know about the effects of remittances on recipient countries, we simply cannot conclude that they can play anything more than the role of supplementing other forms of development finance, including ODA.⁵⁸ In addition, consideration of the behavioral effects of remittances on donor governments also returns us to the idea that we explored earlier (in the discussion of new Dutch diseases) that remittances may provide political cover for decisions taken by state officials, in this case by officials in donor countries.⁵⁹

4. CONCLUSIONS

We have seen that there is still much that we need to know about the diverse economic, social and political effects of remittances. The evidence available to date on the effects of remittances remains sketchy in key respects. Given the nature of remittances, there will likely always be gaps and inconsistencies in the data, and these might be substantial relative to the reported flows. We will always therefore have to exhibit some caution when we draw conclusions about what is happening, and equally, about policy measures that are designed to promote the most developmentally beneficial use of remittances.

Nevertheless at this preliminary point, we can already start to see that the political economy effects of remittances are complex, contradictory, contingent upon many, many factors that vary from cases to case, and so are not amenable to generalizations. In this sense, remittances carry with them complexities that are no less significant than those that have been illuminated by the study of other types of international capital flows. Thus, we should be neither disappointed nor surprised when future research reveals that remittances do not have uniform or unambiguous political economy implications.

⁵⁷ Adelman [2003] argues that privatized foreign aid is the “third wave of foreign aid.” The other components of privatized foreign aid are gifts through foundations, corporations, private voluntary organizations such as the Red Cross, and religious group. Adelman makes a case for conceptualizing FDI and US research and development (in things such as agriculture and medicine) as other types of privatized foreign aid because of their contribution to living standards in developing countries.

⁵⁸ De Haas [2005] makes related critical observations.

⁵⁹ Indirectly related to this point is Burgess’ [2007] argument that remittances reinforce neoliberal policy and market-oriented approaches to development.

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