The Incidence of Remittances in Latin America and Effects on Poverty and Inequality

Jonathan Loritz
Master of Public Policy Candidate
Maryland School of Public Policy
International Security and Economic Policy
May 2008

Abstract

This paper analyzes large household data sets from El Salvador and Bolivia to investigate the incidence and effects of remittances on income. It finds that remittances to El Salvador do indeed decrease both poverty and inequality. This is most likely the result of geographic access for low-income households to the largest remittance source country in the world, the United States, which as resulted in a significant and growing migrant population. Conversely, in Bolivia remittances do not appear to have a significant effect on poverty or inequality and are much smaller in magnitude.

Although no two countries are quite alike, El Salvador appears broadly representative of remittances to Central America as a whole, which receives far more remittances relative to population and income than South America, represented by the case of Bolivia. The findings suggest that remittances may be a tool to reduce poverty and inequality in the most unequal region of the world if efforts are focused on Central America and the Caribbean. The United States, World Bank and Inter-American Development Bank can leverage remittance flows for development by enhancing data collection, promoting formal transactions mechanisms with lower costs, expanding financial access for both migrants and remittance recipients.

Introduction

Remittances have become an increasingly important capital flow and source of income for developing countries. Remittances are the earnings of migrants abroad that are sent to family, friends and communities in their home country for extra income to increase consumption and investment. Remittances are traditionally viewed as being a pro-poor capital flow – that is to say, of disproportional benefit to low-income households.

This paper assesses the validity of that claim by analyzing the incidence of remittances in El Salvador and Bolivia. It uses a case study approach to use geographic and historical factors to explain the differences between these countries and draw implications for policies to leverage remittance flows for development. Finally, policy recommendations will be provided based upon literature and application of the findings.

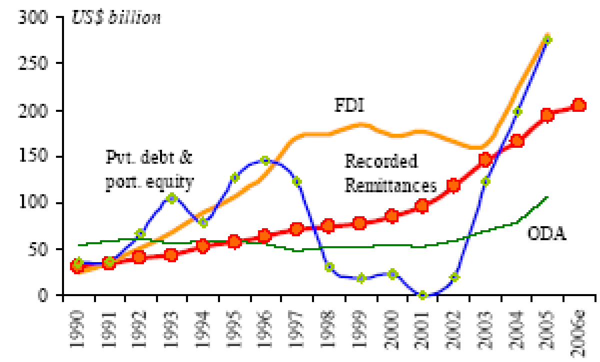
Background

International remittance transfers are recurrent payments by migrant workers who typically send money every month to their families in their home country. A World Bank international task force on remittances has defined these as *cross-border person-to-person payment of relatively low value.*[1] These small transactions have come to the attention of policymakers because in aggregate they can be quite large and have implications for migration, development and macroeconomic stability. The G8 countries, at their summit at Sea Island in June 2004, agreed to take action with developing countries to increase the efficiency of the international remittance system.

[1] CPSS/World Bank – Consultative report on remittances – March 2006.

Remittances have robustly increased over the past ten years with double-digit growth between 2000 and 2006. The World Bank (2007a) estimates that total remittances flows increased from USD600 billion in 2000 to USD1.6 trillion in 2007 – an increase of over 150 percent. Remittance flows have not only increased in magnitude since 2000 but have become greater than official development assistance. They are also stable compared to foreign direct investment and private debt and portfolio equity flows as shown in Figure 1.

Figure 1. Capital Flows to Developing Countries



Source: Ratha (2007)

Recorded remittance flows are currently only a fraction of total remittances, though the ratio has been rising. The process of sending money abroad has slowly become more formalized, and thus easier to measure, as international financial flows have been more carefully inspected and transaction costs have decreased. However, Freund and Spatafora (2005) estimate 30 to 75 percent of remittances remain informal and hence unrecorded. Informal channels include cash transfers based on personal relationships through business people, or carried out by courier companies, friends, relatives or oneself. These transfers remain one of the greatest challenges to remittance policy.

Remittances are also a global phenomenon. As international migrant stocks have increased, so too have financial transactions. China, India and the Philippines currently receive the greatest amount of remittances by value, primarily due to their large migrant populations. Yet as a share of GDP, smaller countries such as Haiti, Honduras and Jordan receive the most (World Bank 2006a).

The United States, Saudi Arabia and Germany are the three greatest sources of remittances. The United States is the source for 30 percent of global remittances, more than any other country, and Latin America receives 75 percent of all its remittances from the U.S., according to estimates by the World Bank (Ratha 2007a). But it also important to recognize that about 81 percent of remittances to Latin America from the U.S. goes to countries in Central America and the Caribbean.

This trend towards greater remittances is expected to continue. While economic downturns may slow the growth of remittances, globalization's effect on international migration and the international financial system is, and will continue to be, a powerful force. Continued global inequality and frequent instability suggests that migration will persist and remittances grow, further integrating the international financial system. Migrants' host countries will need to deal with the consequences of these global forces and many are engaged in studying remittances to better understand their causes and effects.

Migrants send remittances for a variety of reasons that are discussed by Solimano (2003). One motivation, altruism, reasons that migrants send remittances to improve the well-being of their families and communities in their native country. Conversely, the selfinterest motivation suggests that migrants view their home country as an obvious place to invest for higher rates of return and to secure an inheritance.

Two other motivations take the family rather than the individual as the unit of analysis. The implicit family contract theory proposes that families finance the costs of migration as a form of an investment or loan. In this scenario the migrant generates a higher yield abroad, in the form of remittances, improving overall family income. Finally, the co-insurance incentive to migrate explains that migration helps families diversify their economic risks by providing support during economic downturns or periods of instability. Migrants and their families are likely motivated by at least one, and possibly many, of these theories about migration and remittances.

The extra income received by households is used for consumption and investment to improve the quality of life. There is some concern that additional income may be used for luxury goods or cigarettes and alcohol but generally the increased consumption expenditures help families to eat better and access healthcare (source). A study of remittances to Ecuador shows that about 60 percent is spent on food, medicine, house rents and other basic commodities (Solimano 2003).

One of the most important development goals in Latin America is to leverage marginal income for saving and investment that enhances education and infrastructure for long-term growth (IMF source?). In a draft working paper Adams (2005) found that households in Guatemala that received remittances actually spent less at the margin on consumption, more on investment goods like health and housing, and 58 percent more on education. Similarly, Airola (2007) explored Mexico's biannual national household survey to examine the effect of remittance income on spending categories. He found that, on average, households with remittance income spent significantly less on food (including tobacco) but more on durables, health and housing than households without remittance receipts. But how do families actually obtain the money that their migrant family member has earned abroad?

Remittance Corridors

The financial system connecting home and host countries is often referred to as a remittance corridor. Some of the busiest include U.S. – Mexico, U.S. – Philippines and United Arab Emirates – India. Within each of these corridors there are a number of stakeholders including not only the senders and receivers but banks, money operators, central banks, development agencies and more. Corridor efficiency is a critical element when seeking to improve the benefits of remittances for the poor.

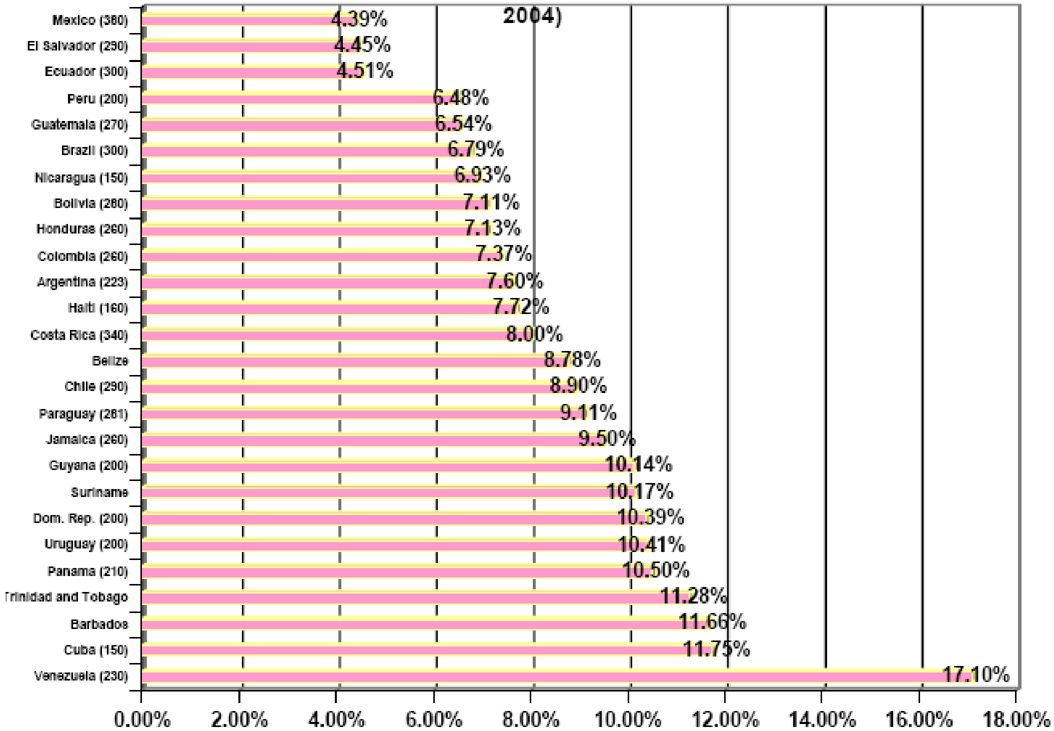
On the sending side, remittance corridors between the U.S and Latin America are frequently dominated by only a couple of money operators such as Western Union or King Express (source). In the receiving country, local unregulated institutions are sometimes the leading receivers of remittance flows, as is the case in Guatemala. In that country, more than 50 percent of remittance flows go to rural areas where financial access is low. Until recently many financial intermediaries were engaging in exclusive bilateral agreements creating a major barrier to entry for new money operators in the U.S.

This corridor was once characterized by informal cash couriers but the dominant remittance mechanism has gradually shifted to formal electronic transfers, largely as a result of new anti-money laundering and combating the financing of terrorism (AML/CFT) measures: the Patriot Act regulates bulk cash transportation into and out of the U.S. with a maximum of $1,000 (cite). Yet as of 2004, only 10 percent of remittance flows to Guatemala were sent through U.S. banks (source).

The average remittance to Latin America is under $300 (most recent WB source), sent an average of once per month. However, transactions fees can run as high as 20 percent of the value of the transaction, severely inhibiting flows or pushing transactions into the informal sector. Today the fee for sending $200 from the Maryland in the United States to El Salvador or Bolivia through Western Union is $27, or 13.5 percent.[2] Yet overall transactions costs have been falling Latin America, but unevenly, and the most for Mexico, El Salvador and Bolivia (Orozco 2004).

[2] Author's calculation, Western Union

Figure 2. Average Cost to Send Average Remittance Amount from U.S. to Home Country



Source: Orozco (2004)

How Pro-Poor?

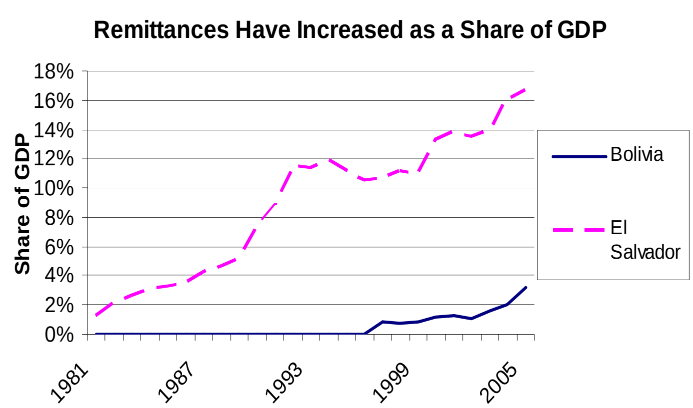
Experts sometimes claim that remittances offer the prospect of pro-poor financing for development (cite). Indeed, migrants willing to work in service or construction employment at lower wages than natives are presumably from lower– and middle–class households in their home countries so that their remittances should be expected to decrease inequality and poverty. Yet, the aggregate incidence is often more complex. The World Bank (2006a) admits that,”remittances sometimes go disproportionately to better-off households and so widen disparities.”

Looking particularly at India, China and the United States, there is evidence that many migrants are not poor. Many of these countries' best and brightest come to the United States to study or on H-1B visas.[3] These migrants may be more likely to come from wealthier families and have more earning power with their higher education levels. On the other hand, many of the rich who migrate eventually bring their families with them. And so it would seem that a series of factors determine the degree to which remittance flows are pro-poor.

Migration Patterns

El Salvador was chosen as the first country for analysis in this paper because it has one of the most stable remittance flows in the world (Ross 2007) that contributes about 16 percent to gross domestic product (GDP) and makes remittances likely to have a significant effect on poverty and inequality. El Salvador's high levels of remittance receipts appear to reflect its geographic proximity to the U.S. and the prevalence of networks of earlier migrants.

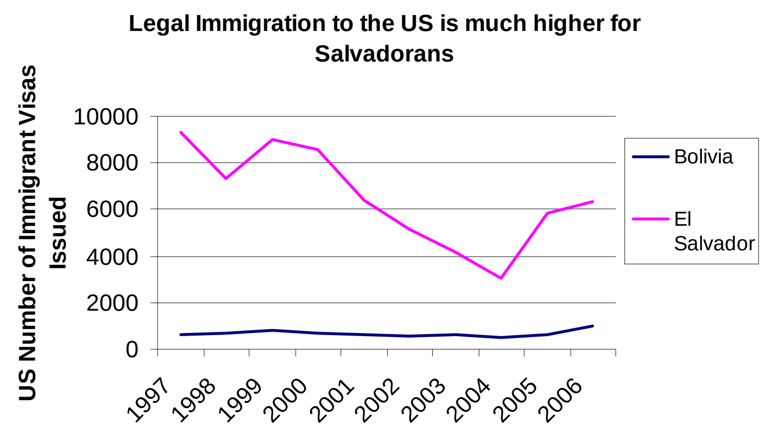
Figure 3. Remittance Growth



Source: World Bank World Development Indicators

[3] The H1B Visa is a United States nonimmigrant visa that allows a U.S. company to employ a foreign individual for up to six years and may lead to a Green Card. The purpose of the H-1B visa is to give U.S. employers the opportunity to hire foreign professionals if a U.S. citizen or resident is not available. In order for the H-1B visa to be issued, the job offer must be in a specialty occupation such as architecture, engineering, mathematics, etc.; No U.S. citizen or resident must be available for the job; and the petition must be submitted by the company (not the employee). The employee must have a bachelor degree, specialized skill and be able to read and speak English.

Figure 4. Visa Issuance



Source: US Department of State 2007.

During the 1980s many Salvadorans migrated illegally to the United States to escape violence and war. Once there, they laid down their roots and many had children who became U.S. citizens. In September 1990, the United States Government made El Salvador the first country to be granted Temporary Protection Status (TPS) – allowing 220,000 Salvadoran immigrants already in the U.S. to work legally. This status has been frequently extended, most recently until March 2009. This amnesty has helped Salvadorans to represent the third largest population (605,850) of foreign nationals in the United States after Mexicans and Indians (OECD 2005). This is in addition to 219,745 naturalized immigrants to the U.S. from El Salvador.

But El Salvador is not the only Latin American country to benefit from a extraordinary migration status. In 1999 Honduras and Nicaragua were designated for TPS due to the devastation resulting from Hurricane Mitch. Approximately 100,000 Hondurans and 6,000 Nicaraguans received the status which continues to be renewed at the request of the Honduran and Nicaraguan governments. These countries plus El Salvador are three of the only seven countries whose nationals currently have Temporary Protection Status.

Bolivian immigrants on the other hand are far less numerous than Salvadorans. Most that do leave the country venture for agricultural and service jobs in Argentina. Trekkers to the United States must overcome significant travel or visa costs so that they are much less likely to be illegal immigrants and more likely to be better educated and from wealthier families. Table 1 shows some characteristics of the migrant stocks from El Salvador and Bolivia despite similar poverty levels in each country.

Table 1. Poverty is Mutual but Migration is Salvadoran

	Bolivia	El Salvador
Stock of Emigrants (2005)	4.6%	16.4%
Tertiary Education Emigration (2000)	6%	31.5%
Poverty Rate at National Poverty Line (2004)	23.9%	20.4%
Primary Destinations of Emigrants	Argentina	US
	US	Canada
	Spain	Guatemala

Source: World Bank Migration and Remittances Factbook (2008)

The 2007 statistics on U.S. immigrant visas show how important a stock of existing migrants is to continuing migration. Almost all legal Salvadoran immigrants to the U.S. are eligible for visas because they have immediate relatives already in the U.S. or have family preference. This holds true for many countries as shown in Table 2.

Table 2. U.S. Immigrant Visa Statistics 2007

Foreign State	Immediate Relatives	Family Preference	Employment Preference	Diversity Immigrants	Total
South America					
Bolivia	680	155	82	90	1,008
Colombia	3,832	2,100	205	0	6,153
Ecuador	2,774	2,033	1,025	70	5,930
Central America and the Caribbean					
El Salvador	3,277	2,949	170	0	6,397
Guatemala	6,671	1,419	137	13	8,240
Honduras	2,233	1,382	127	2	3,749
Nicaragua	1,086	743	9	8	1,849
Dominican Republic	6,311	11,889	46	0	18,267
Haiti	10,225	7,453	20	0	17,698
Jamaica	4,496	4,079	103	0	8,732
Worldwide Grand Totals	224,187	139,753	15,706	44,349	448,969

Not all numbers may total due to omitted categories
Source: U.S. Department of State

Previous studies have found that the impact of remittances on poverty and inequality varies. In one, Martínez and Támola (2007) draw their data from a 2004 national household survey of Honduras and look at observable income, non-remittance income, and counterfactual income. The first measure includes all forms of income and the second measure is the same, less remittance receipts. However, the third is an appealing alternative to non-remittance income because it calculates the counterfactual scenario where migrants did not migrate. Instead of counting their income as zero, as is the case in non-remittance income, the authors impute incomes for the migrants based upon characteristic survey data. These three measures are then compared across poverty lines and Gini coefficients as shown in Table 3. The authors find that among all households the remittances appear to reduce poverty and have an ambiguous effect on inequality.

Table 3. Effects of Remittances on Poverty and Inequality in Honduras

	All households			Recipient households		
	Observed	Non-remittance income	Counterfactual	Observed	Non-remittance income	Counterfactual
Poverty headcount ratio	70.9	73.6	72	49.2	67.6	60
Gini	61.5	62.1	60.7	52.5	59.4	52.9

Source: Martínez & Támola (2007)

Hence there can be mixed effects among poverty and inequality depending on the sample and whether a counterfactual scenario is computed. Overall, the data suggest that remittances are more likely to be received by poor households and that remittances then have a poverty reducing effect.

Another recent study by Adams (2006) finds that remittances in Guatemala significantly reduce the poverty rate from 50 percent to 47.7 percent. This paper also uses counterfactual imputation as the comparison scenario to the observed data. It finds that poverty rates are similar between households receiving remittances and those that do not. In addition to reducing poverty the study also found that remittances ameliorated the depth and severity of poverty for those poor that were unable to surpass the national poverty line.

Finally, Acosta et al. (2006b) look at remittances, poverty, and inequality across ten different countries. However, their remittance estimates are drawn from estimates by the International Monetary Fund that use balance of payment statistics from national accounts. These are less accurate than household surveys to estimate remittance flows (cite). Also using a counterfactual scenario, they find different results in both Guatemala and Honduras using the same data sets as Martínez and Támola (2007) and Adams (2006).

In Honduras Acosta et al. (2006b) find that inequality decreases by 1.1 percent from 56.5 to 55.9 – about half the change found when comparing observed income with non-remittance income (2.3%). This is in contrast with the findings by Martínez and Támola (2007) who calculated a 1.3 percent *increase* in income inequality. In Guatemala, Acosta et al. (2006b) find that inequality decreases by 2.9 percent, more than calculated in the non-remittance income scenario (-1.8%).

For poverty, Acosta et al. (2006b) measure poverty at US$2 (PPP) per day which is a slightly different base than the national poverty lines used in Martínez and Támola (2007) and Adams (2006) but they still find results with their national account data that differ from the household survey results. In Honduras they find that poverty decreases by about 0.6 percent compared to the 1.5 percent found by Martínez and Támola (2007). In contrast, Acosta et al. (2006b) find the same decrease in poverty of 1.7 percent as Adams (2006) had for Guatemala.

While most countries exhibit the expected results in Acosta et al. (2006b), it is worthwhile to note that not all countries' data conformed to the expectation of reduced poverty and inequality after including remittance income and that the counterfactual scenario reduces the magnitude of this effect. In the next section, household survey findings will be presented for El Salvador and Bolivia.

Data

Remittance data collection and measurement have long been challenges for governments and researchers. Information on remittance flows can be estimated using one of several methods. Official balance of payment (BOP) statistics are used by many governments and researchers. This data has the benefit of being the most readily available estimate of remittances across countries and time but fails to capture informal flows and has significant margins of error (cite).

Household surveys are another method of estimating remittances. These can be incredibly detailed – both providing more information and making analysis more complex. Surveys are also more expensive to implement than BOP statistics so that the availability of survey remittance data is inconsistent and sparse across countries and time. However, where available, surveys provide superior detail to BOP statistics.

This paper simulates this analysis for El Salvador and Bolivia to confirm that remittances can help reduce poverty and inequality but may not have this effect in all countries. Data was obtained from national household surveys conducted in 2002 in each country. In El Salvador this was conducted by the Ministry of the Economy and in Bolivia by the National Statistics Institute.

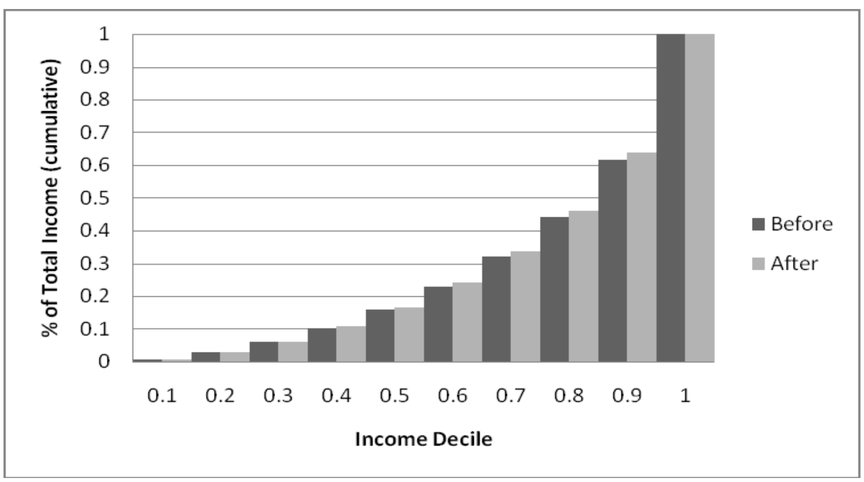
Findings in El Salvador

In El Salvador remittances are expected to reduce both poverty and inequality. The IMF World Economic Outlook (April 2008) reports El Salvador as having been the 8th poorest country in the Western Hemisphere by GDP per capita (PPP$4,761) in 2002. The survey data revealed the annual income per capita to be USD$1,238. El Salvador also has one of the highest ratios of remittance receipts: 23 percent of the population lived in a household reporting receiving international remittances. Of those receiving remittances, the average received was USD$724 per person annually. Although the magnitude of remittances is certainly significant in El Salvador, their effect on poverty and inequality depends crucially on their incidence.

As expected, remittances were found to be unevenly distributed across income quintiles: the top two quintiles received about two-thirds of all remittances to the country. Remittances accounted for between 10 and 20 percent of total income for all quintiles – 15.6 percent for the bottom quintile and 18.8 percent of all income for those in the middle quintile. This pattern suggests that the incidence of remittances is only somewhat more equal than the existing income distribution.

Looking at relative poverty the data reveal that the top quintile decreases its share of national income by about 2 percent and that the bottom 40 percent of income earners increase their share of income by 0.5 percent. The greatest gains go to the third and fourth quintiles which increase their income share by 1.5 percent. The impacts reduce inequality by about 3.4 percent as the Gini coefficient decreases to 49 from 50.7 when remittance income is factored into total income. Figure 5 shows the change in the distribution of income omitting remittance receipts (before) and with their inclusion (after).

Figure 5. Distribution of Income in El Salvador Before and After Remittances



Source: 2002 MECOVI

Comparing poverty rates before and after the inclusion of remittance income, absolute poverty (at the national poverty line) appears to decline by about 10 percent. However, this is without the support of a counterfactual scenario so that the true effect is likely smaller as in the case of Honduras considered by Martínez and Támalo (2007).

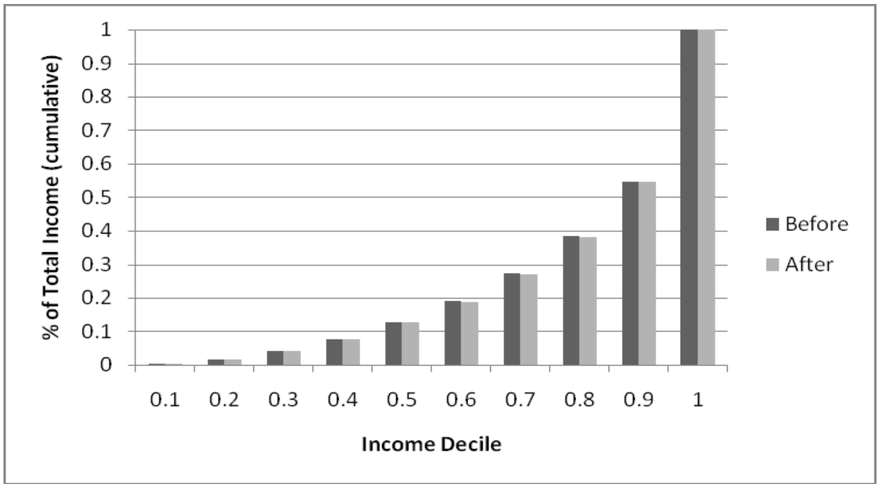
Findings in Bolivia

The same calculations are repeated for Bolivia to show that remittances have a much smaller effect, if any, on countries without access to a wealthy country as a remittance source. Indeed, the survey data bear out expectations.

Bolivia was the fifth poorest country in the western hemisphere by GDP per capita (USD$3,220) in 2002. The average annual income per capita in Bolivia was found to be USD$566 and only 3.4 percent of the population lived in households reporting remittance receipts. Most of those that did receive remittances reported receiving them monthly with an annual average of USD$248 per capita annually.

However, the top two income quintiles receive over 90 percent of all remittances to the country and remittances account for less than 2 percent of total income for each quintile. We know for a fact that Bolivia has a much smaller remittance flow than many other Latin American countries however this finding also suggests that remittances do not alleviate poverty or decrease inequality as depicted in Figure 6.

Figure 6. Distribution of Income in Bolivia Before and After Remittances



Source: 2002 ENCOVI

Comparing pre-remittance income to post-remittance income, we find that the change in relative poverty is insignificant: the total share of income by the top quintile actually increases by 0.3 percent and the Gini coefficient rises from 56.8 to 57. Similarly, the poverty headcount ratio at the national poverty line changes only an insignificant 0.27 percent.

The Two Cases in Latin America and the Caribbean

Contrasting El Salvador and Bolivia we find that remittance flows have great variation in both magnitude and incidence. There are several factors that are likely to be affecting this difference. First, and obviously, El Salvador benefits from its proximity to the United States. It was also the first country to receive temporary protection status from the US government, allowing it a large stock of poor migrants whom had migrated illegally to become legal workers. And so benefiting from these facts of geography and history, El Salvador receives greater levels of remittances than Bolivia.

Bolivia has had no comparable diaspora to El Salvador and other Central American neighbors that have suffered from civil war and natural disaster. Such extreme circumstances have provided migrants, rich and poor, from countries such as Haiti, Dominican Republic, Honduras, Guatemala and others with amnesty that has resulted in a remittance incidence that is decreases both poverty and inequality. Yet even in this scenario, optimal for pro-poor capital flows, the effects appear to be only mild. And so in the case of Bolivia, where access to the US and EU are limited to the educated or wealthy, remittance flows are also growing in magnitude but have very little impact on the poor and actually increase inequality overall.

Policy Implications

The field of study on remittances has been growing rapidly and improving its data efforts but data is still sparse. Efforts will need to continue to integrate remittance data collection into national surveys around the world. This will help to explore the impacts of remittances which the surveys from El Salvador and Bolivia, exhibited in this paper, show are not the same across all countries.

As the data improves and the field of literature grows, development and financial sector policymakers and practitioners will become more sophisticated in their remittance programming. This paper suggests at least a simple categorization of developing countries into “El Salvadors” and “Bolivias” to help refine policy choices to leverage remittances for economic and financial development.

The Bolivias are mostly South American countries that represent only a small percentage of remittances to Latin America such as Suriname, Ecuador and Peru. The flows to these countries are often even more unequal as the income distribution before remittances (Fajnzylber and López 2007). The findings from this paper, combined with much other literature in the field, suggests that remittance-related policy changes would have little effect on poverty or inequality in countries where migration and access to the United States or EU is limited. Until migration policies welcome poor, low-skilled workers from these countries, remittance flows in these corridors will continue to be dominated by the top quintile of income earners.

The Salvadoran case is broadly representative of Central America and the Caribbean. These countries, including *inter alia*, Guatemala, Nicaragua, Honduras, Haiti, Jamaica and Mexico, comprise the most unequal region in the world and generally have populations with low levels of education so that their migrants are often poor. The countries in this category also tend to have experienced crises and often as a result, have large migrant populations. Together this means that many of the remittance corridors to these countries are pro-poor and significant in value on a per capita basis. Interested institutions can and should engage to encourage the use of these private capital flows for economic and financial development.

Policy Recommendations

The findings of this paper and review of the literature yield many implications for governmental and multilateral institutions including ministries of finance and central banks and specifically, because the United States is the largest sender of remittances, the Department of the Treasury and Federal Reserve. All of the G8 countries also committed to improving remittance flows at their Sea Island summit in 2004 where they declared an action plan to:

- Facilitate formal financial transactions including financial literacy programs and cooperation with the private sector;
- Reduce the cost of remittance services through promotion, innovation and access;
- Encourage cooperation between remittance service providers and local financial institutions to strengthen markets and access;
- Encourage local development funds to enhance options for productively investing remittance receipts; and
- Support dialogue across the public, NGO and private sectors towards these goals.

Each action point is an important element to improving global remittance flows. Not only will their fulfillment assist migrants and their families but also help the G8 countries meet their goals of strengthening anti-money laundering and combating the financing of terrorism (AML-CFT) regulations; promoting financial access, growth and development in developing countries; and securing the stability of the international financial system. There are several policies that governments and institutions can adopt and actions they can take to enhance the impact of remittances in El Salvador and countries like it.

1. **Continue to support efforts to improve data collection.** This requires building domestic survey capacity Salvador and financially supporting national statistics offices in El Salvador and Central American countries, both directly and through multilateral institutions. Data collection will be further facilitated and data quality improved if formal remittance flows grow relative to informal flows.

2. **Increase the use of formal remittance mechanisms.** Doing so would have significant positive externalities including the improvement of international security by making legitimate informal remittances, which currently go unrecorded, monitored for AML/CFT purposes. This would help authorities in sending and receiving countries to monitor international capital flows for suspicious activity. It would assist institutions such as the IMF to better understand the effects of remittances on macroeconomic stability. Increasing the prevalence of formal remittance mechanisms is also likely to improve financial access for both remittance senders and recipients. Lowering transactions costs and strengthening Spanish financial literacy courses will help to make formal mechanisms more attractive to Latin American immigrants in host countries.

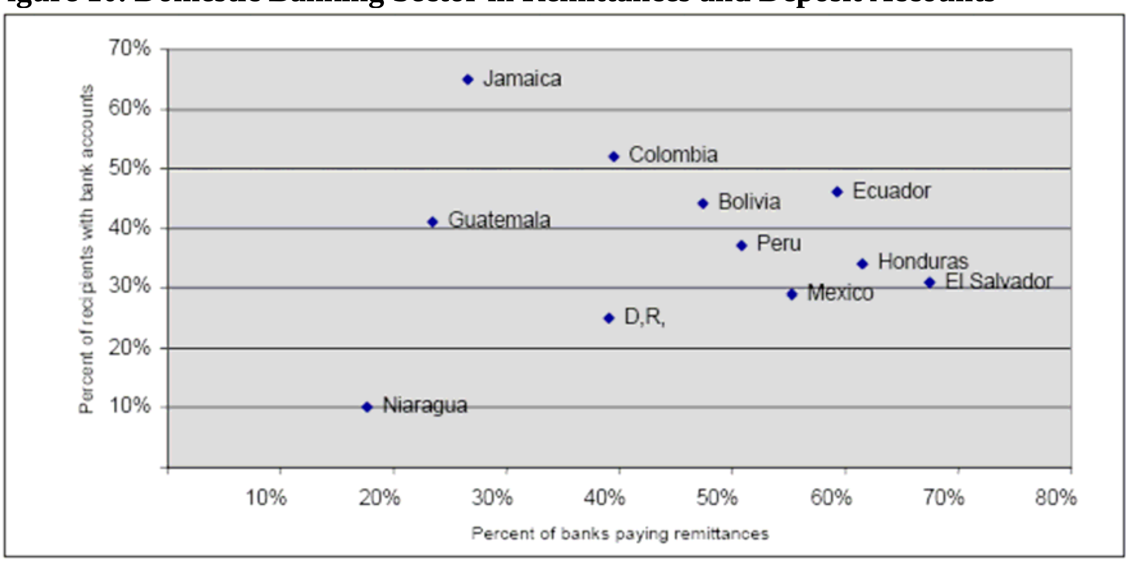
3. **Support efforts to decrease transactions costs of formal mechanisms.** Cost is an important determinant of remittance flows and the likelihood to transmit informally. Beginning with Central American and Caribbean countries, regulators can support fair prices by adopting transparency measures developed by the Committee on Payment and Settlement Systems to clearly disclose

transaction information. Specifically this includes the total amount paid, the amount disbursed, total fees and taxes, and the time and location of pickup availability. Regulators should also discourage exclusive partnerships between home and host country operators so as to improve competition and prevent monopoly rents on transaction costs. Lower transactions costs have been found to be associated with greater number of service providers, larger transaction sizes and larger annual remittances volumes (Orozco 2006).

4. Reassure commercial banks in their dealings with immigrants of non-regularized status. It is estimated that only 50 percent of Latin Americans in the United States have bank accounts (Orozco 2004). Even though U.S. banks are permitted to serve migrants that "have identity cards that comply with the minimum requirement at their [the banks] discretion" banks are currently reluctant to provide financial services for low-income migrants. Doing so could expose them to risks that government will find negligence in their responsibility to know their customers. Focusing on countries like El Salvador, host country governments and multilateral institutions should continue to work with foreign embassies to develop consular identification card programs like those that have been successful for Mexican and Guatemalan migrants. The lack of banks and bank accounts has a host of negative implications, from higher transmitting costs for remittances to lack of credit for home ownership to lower investment in productive enterprises – both at home and abroad.

5. Provide incentives for banks and remittance recipients to develop relationships in the home country. In El Salvador it is estimated that almost 85 percent of all remittances are transmitted by banks. The country also has one of the largest and most advanced financial sectors in the region, yet not unlike other developing countries the majority remittance recipients function entirely in the cash and barter segment of the economy. This inhibits economic growth and financial development. Aggarwal, et al. (2006) find strong support for the theory that remittances promote financial development. In most countries of the El Salvador type there is significant need to increase both banks' remittances and account services as shown in Figure 10. Having access to financing will help to promote productive investments in developing countries.

Figure 10. Domestic Banking Sector in Remittances and Deposit Accounts



Source: Orozco (2007)

REFERENCES

Acosta, P., Calderón, C., Fajnzylber, P., & López, H. (2006a). Remittances and Development in Latin America. The World Economy 29 (7), 957–987.

Acosta, P., Calderón, C., Fajnzylber, P., & López, H. (2006b). Impact of International Remittances on Poverty and Inequality in Latin America. World Bank. Washington, DC.

Adams, R. (2006). Remittances, Poverty, and Investments in Guatemala. International Migration, Remittances and the Brain Drain, Ed. C. Ozden and M. Schiff, 53-80. New York: Palgrave McMillan.

Adams, R. (2005). Remittances, Household Expenditures and Investment in Guatemala. World Bank Policy Research Working Paper 3532, Washington, DC.

Adams, R. (2004). Remittances and Poverty in Guatemala. World Bank Policy Research Working Paper 3418.

Airola, Jim. (2007). The Use of Remittance Income in Mexico. International Migration Review 41 (4), 850–859.

Fajnzylber, P. & López, H. (2007). Close to Home: The Development Impact of Remittances in Latin America. World Bank, Washington, DC.

Freund, C. & Spatafora, N. (2005). Remittances: Transaction Costs, Determinants, and Informal Flows. World Bank Policy Research Working Paper 3704, Washington, DC.

Martínez, C. & Támola, A. (2007). Honduras: The Impact of Remittances on Poverty, Income Inequality, and Social Welfare. Inter-American Development Bank, Economic and Sector Study, Washington, DC.

Organization for Economic Cooperation and Development (OECD), 2004, *Database on Immigrants and Expatriates*, (Paris: OECD).

Orozco, M. (2007). The Role of Remittances in Leveraging Sustainable Development in Latin America and the Caribbean. Inter-American Dialogue, Washington, DC.

Orozco, M. (2006). International Flows of Remittances: Cost, Competition and Financial Access in Latin America and the Caribbean—Toward an Industry Scorecard. Inter-American Dialogue, Washington, DC.

Orozco, M. (2004).

World Bank (2006a). Global Economic Prospects 2006. Washington, DC.

Ratha, D. (2007). Leveraging Remittances for Development. World Bank, Washington, DC.

Ratha, D. & Xu, Z. (2008). Migration and Remittances Factbook 2008. World Bank, Washington, DC.

Ross, Carl. (2007). “Slowing Remittances to the Caribbean & Central America -- Assessment and Implications.” Bear Stearns. New York, NY.