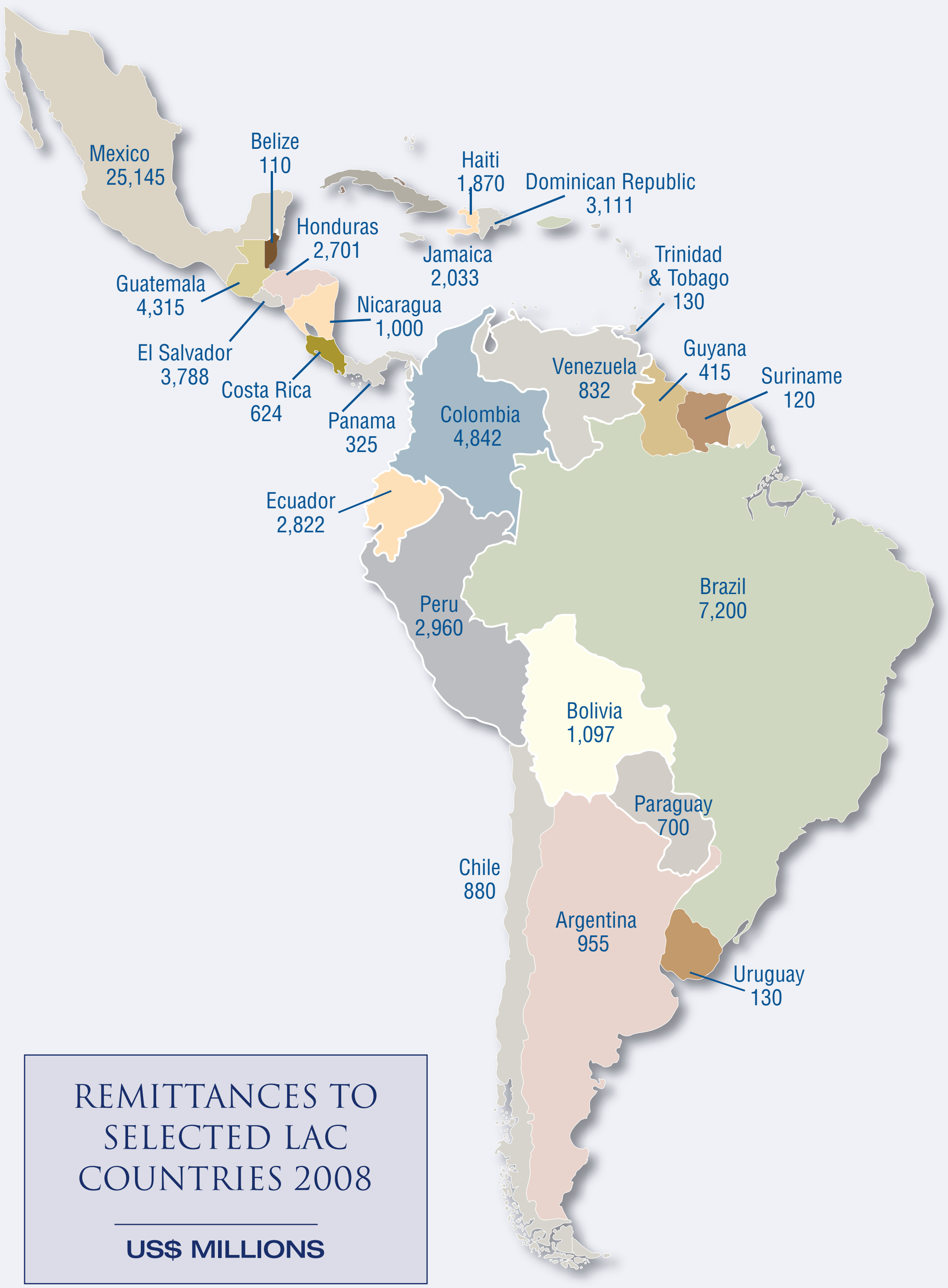

REMITTANCES TO SELECTED LAC COUNTRIES 2008

US$ MILLIONS

MULTILATERAL INVESTMENT FUND

INTER-AMERICAN DEVELOPMENT BANK
MULTILATERAL INVESTMENT FUND

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REMITTANCES 2008

REMITTANCES IN TIMES OF FINANCIAL INSTABILITY

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INTER-AMERICAN DEVELOPMENT BANK IDB

WORLDWIDE REMITTANCES TO LATIN AMERICA and the Caribbean (LAC) reached $69.2 billion in 2008, an increase of just under one percent over 2007.[1] Despite a series of challenges confronting migrant workers and their families in 2008, remittance senders proved to be remarkably resilient. The financial crisis, however, has raised new obstacles to migrant workers' ability to send money home. Given the recessions plaguing major destination countries such as the United States, Spain and Japan, remittances to the LAC region will decrease in 2009, marking the first downturn since the Inter-American Development Bank began tracking these flows in the year 2000.

Remittances are a vital source of funds for millions of households throughout the region, constituting more than half the income for approximately 30% of recipient families. The bulk of this money is used for basic necessities such as food, clothing and shelter, contributing significantly to poverty reduction. The balance is either saved or invested, allowing these families to advance on the road to financial independence.

In contrast with portfolio investments and foreign direct investment, remittances are an expression of a deeply rooted family obligation. Remittances actually increase during times of economic hardship or political instability, rising to meet the increased needs of recipient families. The 'counter-cyclical' nature of these flows is currently being challenged, as the global slowdown hits remittance senders and their families alike.

At the macroeconomic level, migrant workers continue to make an impressive contribution to their home countries. Seven of the region's nations receive 12% or more of GDP from their compatriots abroad, including Guyana, Haiti, Honduras, Jamaica, El Salvador, Nicaragua and Guatemala. In times of financial crisis the relative stability of these flows acts as a buffer while revenues from tourism, exports and foreign investment come under pressure.

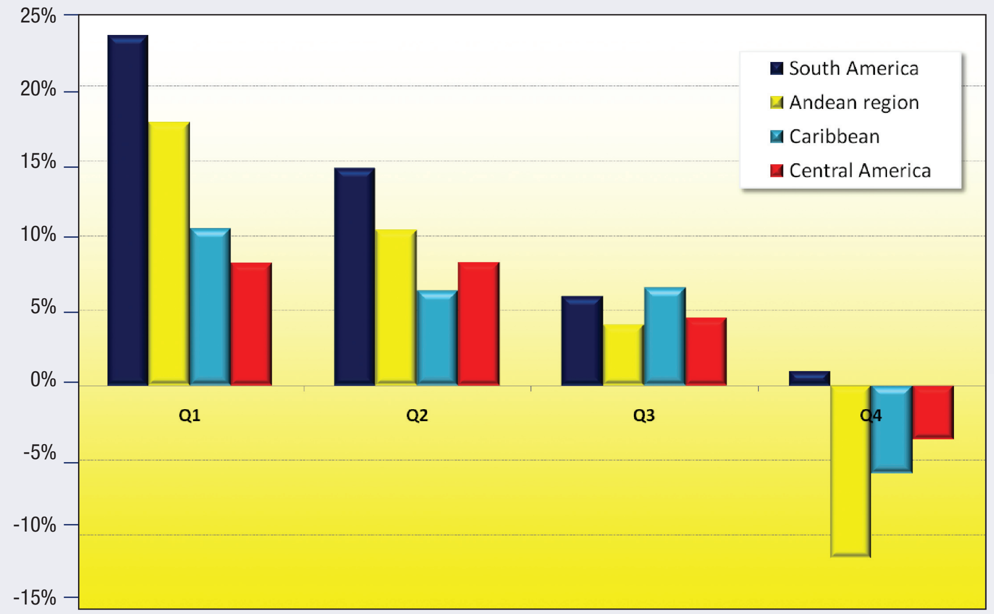
2008: REMITTANCES IN TRANSITION

Four factors contributed to a decline in the purchasing power of remittance recipients during the first three quarters of 2008: the economic slowdown in the United States, sharp spikes in food and fuel prices, a harsher climate against immigration, and a weakening U.S. dollar.

The slowing **U.S. economy** and a loss of jobs in sectors that attract immigrant labor, such as construction, have been mirrored in other countries with significant migrant communities from the LAC region. Spain, for example, is experiencing a construction bust similar to the decline in the U.S. housing sector. Japan, an important source of remittances to Brazil and Peru, has seen declining industrial production as export demand has slumped.

The main exception to this pattern has been the LAC region itself. Robust economic growth in LAC has meant that migration within the region plays an increasingly important role, resulting in a continuing rise in intra-regional remittance flows and a reduction in the dependence on traditional remittance sending countries. Another positive development is that **food and fuel prices**, which had significantly increased

REMITTANCE GROWTH TURNS NEGATIVE IN LAST QUARTER OF 2008



the cost of living, both in remittance sending countries and in Latin America and the Caribbean during the first half of 2008, have moderated as a result of the crisis.

Historically, the climate for **immigration** has tended to worsen during tough economic times. Despite anecdotal evidence of immigrants returning home, the vast majority are determined to wait for better times. Migration patterns are undoubtedly adjusting to the new economic conditions, as the lack of job opportunities prevents many from seeking work abroad. This is not likely to have a significant impact on remittance flows in the short-term, as the downturn has led to a lower inflow of migration but not to a discernable decrease in the stock of migrants sending remittances.

TURBULENT TIMES MEAN EXCHANGE RATES OF EVER GREATER IMPORTANCE

As opposed to the slow depreciation of the U.S. dollar during the first three quarters of 2008, since the onset of the financial crisis there has been a dramatic appreciation of the greenback against major Latin American currencies. This in turn has had effects on purchasing power and remittance transfer behavior.

In October 2008, immigrants from **Mexico, Brazil and Colombia** saw the value of a dollar sent home rise by 20-30% in local currency terms. As a result, financially savvy migrants capitalized on the situation, sending home remittances in record amounts. A strong dollar will go some way towards offsetting the effects of a decline in the volume of dollars sent to their homelands.

Dollarized countries and those with currencies pegged to the dollar are not affected by that trend. In the case of Central American countries, where remittances from the United States play a crucial economic role, this can be positive as it also insulates them against the risk of an eventual weakening of the dollar.

Andean countries with significant diasporas in Europe (principally in Spain), were hurt by a rapid decline in the value of the euro between July and October of 2008. As the euro has remained close to its October lows against the dollar for the first three months of 2009, the value of remittances to Andean countries that are more dependent on European flows is likely to decline.

These dynamics have very different effects, depending on specific exchange rate regimes and the countries from which remittances are sent. Since October 2008 remittance growth to the LAC region as a whole has actually remained positive in local currency terms, even while growth in dollar terms has declined. Together with slowing inflation, this has a beneficial impact on the purchasing power of remittance recipients.

THE FUNDAMENTALS

Remittances are private flows that go directly to the families that need them most. These flows are key to both poverty reduction and to attaining future financial independence for recipient families. At the same time, remittances make a significant contribution to the region's economies. Despite the decline expected in 2009, remittances will remain a far more stable source of foreign currency than other financial flows, while maintaining millions of people above the poverty line.

Migrant workers and their families are facing difficult economic times. As a result, remittance senders are using various coping mechanisms in order to provide for their relatives. By changing jobs, working longer hours, decreasing their consumption, and moving to respond to changing labor markets, migrant workers have been able to maintain their level of sending. Some are even tapping into their savings to meet the needs of their families back home.[2]

From a development standpoint, the puzzling question is why, even at a time of scarce liquidity, only a small proportion of recipients keep their money in deposit accounts. Most recipients pick up their remittances at a bank, but less than half of them have bank accounts. Paradoxically, this means that remittances are a largely untapped source of liquidity.

Financial institutions willing to meet the needs of recipient families could benefit from higher deposits, while at the same time granting recipients access to the kinds of services that can be used to build assets. It is in this vital area that the IDB is working; providing advice to governments on how to minimize the impact of the financial crisis on remittance recipients, while working with the public and private sectors to create an enabling environment which maximizes the developmental impact of these important flows.

International migration is fundamentally the result of developmental imbalances. The global crisis is certainly taking its toll on remittance senders and their families, but it has not altered the motives guiding the decision to look for better opportunities abroad, or migrants' commitment to send money home. For these reasons, once the global economy starts to recover, migration and remittance flows will pick up. In the meantime, remittances will remain a vital buffer to recipient families and nations alike.

[1] Due to a significant revision of previous remittance figures by the Mexican Central Bank, MIF remittance estimates have had to be adjusted accordingly. In 2007 the increase in remittances to Mexico raised the overall regional total from $66.5 to $68.6 billion.

[2] Orozco, Manuel. "Are Trends in Money Transfers to Latin America Shifting Downward" in FOCAL point http://www.thedialogue.org/PublicationFiles/FOCALPoint%20November%202008.pdf). November, 2008.