



# Workers' Remittances and the Real Exchange Rate: A Paradox of Gifts

CATALINA AMUEDO-DORANTES

*San Diego State University, San Diego, CA, USA*

and

SUSAN POZO \*

*Western Michigan University, Kalamazoo, MI, USA*

**Summary.** — We test the impact of workers' remittances on the real exchange rate using a panel of 13 Latin American and Caribbean countries. The analysis reveals that workers' remittances have the potential to inflict economic costs on the export sector of receiving countries by reducing its international competitiveness. Our findings raise concerns parallel to those raised by Dutch Disease or Resource Boom models, where resource discoveries result in real exchange rate appreciation and shifting of resources from the traded to the nontraded sectors of the economy.

© 2004 Elsevier Ltd. All rights reserved.

*Key words* — workers' remittances, real exchange rate, foreign aid, panel data, Latin American and Caribbean area

## 1. INTRODUCTION

Workers' remittances, the repatriated earnings of migrant workers, have grown to be an important source of foreign exchange earnings for many countries. The figures in Table 1 compare the magnitude of these flows in 1987 to the flows experienced 10 years later for a sample of Latin American and Caribbean countries. In almost all cases, we observe that workers' remittances relative to national income have grown significantly over the past decade. For example, while workers' remittances in El Salvador amounted to about 4.3% of national income in 1987, they had grown to over 10% of El Salvador's income by 1997.

Additional evidence of the increasing importance of workers' remittances is displayed in Table 2. The level of workers' remittances expressed in US dollars is compared to the magnitude of foreign aid and service exports, other important sources of foreign exchange for developing economies. It is interesting to note that the foreign exchange "earned" via remittances rivals, and often exceeds, foreign

exchange earnings obtained through the more traditional sources. In over half of these cases, transfers in the form of workers' remittances exceed gifts in the form of foreign aid and, in about a third of the cases, remittance income approaches or surpasses the level of income earned from service exports. Given the rising share and rising importance of workers' remittances, we ask: what are the macroeconomic impacts of these transfers of purchasing power and of wealth?<sup>1</sup> In this paper, we attempt to better understand the effect of remittance flows by exploring how they affect the real exchange rate.

The notion that transfers may have significant effects on receiving economies was originally debated by Keynes (1929) and Ohlin (1929) in what has been dubbed the *transfer problem*. The upshot of this debate (which extends to the present) is that the theoretical welfare impacts are ambiguous, depending on various characteristics of the sending and

\* Final revision accepted: 26 February 2004.

Table 1. *Workers' remittances as a percentage of national income<sup>a</sup>*

Country	Year 1987	Year 1997
Argentina	0.00	0.01
Belize	5.88	2.84
Bolivia	0.01	0.03
Colombia	1.76	0.62
Dominican Republic	4.90	7.62
El Salvador	4.36	10.70
Guatemala	0.00	2.30
Honduras	0.71	3.55
Jamaica	2.04	15.86
Mexico	1.11	1.40
Nicaragua	0.00	8.90
Peru	0.38	0.70
Trinidad & Tobago	0.06	0.60

<sup>a</sup> Obtained from World Development Indicators CD.

receiving countries (Djajić, Lahari, & Raimondos-Møller, 1998).

A parallel body of empirical research has attempted to ascertain the broader macroeconomic impacts of foreign aid on receiving countries. These empirical macroeconomic studies have not however resolved the question of how these economies are affected by aid from a macroeconomic perspective (Burnside & Dollar, 2000; Cassen, 1994; White, 1992). Contradictory results regarding their impacts are obscured by the various econometric issues that confound the true impact. In particular, the endogeneity of the receiving country's income and the decision by donors to extend foreign aid has not normally been addressed,

making appropriate conclusions about the impact of aid difficult to ascertain.

Like the earlier literature, this study attempts to measure the effect of transfers on receiving economies, although from a different angle. While accounting for the impact of *public* aid, we focus on how *private* aid in the form of workers' remittances affects the real exchange rate in receiving economies.<sup>2</sup> In addition, we correct for the endogeneity of workers' remittances, as well as for the endogeneity of other regressors, in order to properly assess their impact.

In considering the impact of workers' remittances on the macroeconomy, we are motivated by Obstfeld and Rogoff (1996), who argue that a positive transfer of resources to a country hurts its competitiveness in world markets by reducing the range of goods it exports. The reduction in competitiveness takes place because the transfer increases the country's real exchange rate. Therefore, letting  $q$  represent the real exchange rate (with a rise in  $q$  representing real exchange rate appreciation), letting  $W$  symbolize transfers in the form of workers' remittances, and letting  $X$  stand for a vector of other determinants of the real exchange rate, we posit that workers' remittances will appreciate the real exchange rate or:

$$q = f(W, X), \quad (1)$$

Countries receiving greater transfers of workers' remittances will experience appreciating currencies, all other things equal. There are various channels by which the receipt of

Table 2. *Workers' remittances, foreign aid and service exports in US dollars in 1997<sup>a</sup>*

Country	Workers' remittances	Foreign aid	Service exports
Argentina	41,000,000	94,970,000	4,510,000,128
Belize	18,950,000	14,160,000	137,840,000
Bolivia	232,954,906	698,400,000	246,690,000
Colombia	483,000,000	194,540,000	2,163,000,064
Dominican Republic	1,326,000,000	70,970,000	2,446,599,936
El Salvador	1,337,521,024	272,470,016	291,677,408
Guatemala	456,500,000	263,000,000	588,800,000
Honduras	220,000,000	296,830,016	334,900,000
Jamaica	659,200,000	71,070,000	1,714,599,936
Mexico	5,626,999,808	99,080,000	11,399,999,488
Nicaragua	200,000,000	410,100,000	167,600,000
Peru	400,000,000	393,460,000	1,540,999,936
Trinidad & Tobago	44,567,528	32,960,000	546,461,312

<sup>a</sup> Foreign aid represents official foreign aid receipts, obtained from *WDI*. Service exports were obtained from World Development Indicators.

متن کامل مقاله

دریافت فوری ←

**ISI**Articles

مرجع مقالات تخصصی ایران

- ✓ امکان دانلود نسخه تمام متن مقالات انگلیسی
- ✓ امکان دانلود نسخه ترجمه شده مقالات
- ✓ پذیرش سفارش ترجمه تخصصی
- ✓ امکان جستجو در آرشیو جامعی از صدها موضوع و هزاران مقاله
- ✓ امکان دانلود رایگان ۲ صفحه اول هر مقاله
- ✓ امکان پرداخت اینترنتی با کلیه کارت های عضو شتاب
- ✓ دانلود فوری مقاله پس از پرداخت آنلاین
- ✓ پشتیبانی کامل خرید با بهره مندی از سیستم هوشمند رهگیری سفارشات