Latin American Economic Outlook 2010

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Latin American Economic Outlook 2010

Development Centre of the Organisation
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The Centre links OECD members with developing and emerging economies and fosters debate and discussion to seek creative policy solutions to emerging global issues and development challenges. Participants in Centre events are invited in their personal capacity.

A small core of staff works with experts and institutions from the OECD and partner countries to fulfil the Centre's work programme. The results are discussed in informal expert and policy dialogue meetings, and are published in a range of high-quality products for the research and policy communities. The Centre's *Study Series* presents in-depth analyses of major development issues. *Policy Briefs* and *Policy Insights* summarise major conclusions for policy makers; *Working Papers* deal with the more technical aspects of the Centre's work.

For an overview of the Centre's activities, please see www.oecd.org/dev.

FORE WORD

Foreword

2010 will be a critical year for Latin American economies. After being hit by the global economic and financial crisis, the economies of the region show signs of recovering. Considerable improvements in the macroeconomic fundamentals and the quality of economic governance in recent years have allowed several countries in the region to use fiscal and monetary stimulus in a sustainable way. Furthermore, the strength of financial systems has been instrumental in averting financial crises that unfortunately had been the norm rather than the exception for the region during previous periods of international economic turmoil. Nevertheless, volatile commodity prices, scarcer inflows of portfolio and investment capital and slowing migrants' remittances pose important challenges for many countries.

On top of these uncertainties for 2010, the key long-term challenges for public policy in Latin America and the Caribbean – the very challenges that inspired us to launch this annual report three years ago – remain the same: achieving socially and environmentally sustainable development and creating opportunities for all by promoting growth, combating poverty and reducing inequality. Additionally, most Latin American countries still need to address long-term competitiveness issues if they are to achieve a sustainable increase in living standards. This means pursuing structural reforms, boosting innovation and avoiding protectionism.

With the OECD *Latin American Economic Outlook 2010*, the OECD Development Centre makes another contribution towards this agenda. Building on the OECD's analytical expertise on best policy practices, this year's report explores the macroeconomic implications of the crisis in Latin America. It also covers issues of investment and recent migration patterns in the context of the crisis.

The need to resist the call for protectionism is underscored in this year's edition. Indeed, the *Outlook* concludes that Latin American countries with larger financial and commercial flows have built up greater resilience to external shocks. In order to succeed, nonetheless, they need to diversify exports, hedge their financial portfolios, insure their revenues against terms-of trade risks, build up reserves and balance their public accounts.

This year's *Outlook* also highlights the importance that people and capital flows related to international migration will play in the region's recovery. Though remittances are generally more stable than other resource flows to Latin American economies, receipts in the region will drop for the first time in many years in 2009. Poor households that rely on this source of income will particularly feel the pinch. The report does an excellent job in identifying the implications of these new trends for the development of the region, paying special attention to the effects of migration and remittances on labour markets, financial deepening and social protection.

The recommendations put forward by the *Latin American Economic Outlook 2010* provide guidance for OECD and Latin American governments to make the most of migration by working together and improving co-ordination. In particular, governments in countries of immigration should adjust their migration policies and upgrade their integration frameworks so that migration can contribute to meeting future labour needs in the context of ageing population. Along these lines, new policies should include mechanisms to discourage irregular flows and facilitate legal channels; they should also extend social benefits to immigrants and facilitate portability across borders. For countries of emigration in Latin America and the Caribbean, the report offers practical insights on how remittances can better promote development by formalising currently informal flows of money. It argues for

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more access to, and stronger competition in banking services, better regulatory frameworks and active policies to engage diasporas with incentives to send money home, either privately or through government-sponsored mechanisms.

The continued research and policy dialogue activities carried out by the OECD Development Centre through the OECD *Latin American Economic Outlook* series have contributed to bringing OECD experience closer to Latin America, while at the same time raising the visibility of Latin American issues among our member countries. As we have all learned in recent months, every crisis offers an opportunity. If Latin America takes the right measures it could certainly emerge reinforced from the recent turmoil. This *Latin American Economic Outlook 2010* provides a useful and valuable compass in that undertaking.

Angel Gurría
OECD Secretary-General

Acknowledgements

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The writing and production of LEO was co-ordinated by Christian Daude. The Americas Desk is headed by Jeff Dayton-Johnson, under the supervision of Javier Santiso, the Development Centre's Director and the OECD Chief Development Economist. Rita Da Costa provided substantial research support for most chapters. Ángel Alonso Arroba, Francesca Castellani and Caroline Paunov commented on various draft versions and provided feedback throughout the whole process. Béatrice Melin provided instrumental assistance in the preparation of the publication. Special thanks go to our editor, David Camier-Wright, who helped to turn the original manuscript into a readable report.

Most chapters draw additionally upon the work of a far-flung network of colleagues. Without their support and commitment, this book would not have been possible. Many of these contributions take the form of text boxes in the pages that follow. Rui Esteves, Oxford University, and David Khoudour-Castéras, Centre d'Etudes Prospectives et d'Informations Internationales (CEPII), provided a text box for the macroeconomic overview chapter, as did Ángel Melguizo, OECD Development Centre's Americas Desk, who also contributed the subsection on fiscal stimulus packages. Rolando Avendaño and Rita Da Costa provided a text box for Chapter 1; Natalia Bajuk and Gregory Watson, Inter-American Development Bank's Multilateral Investment Fund, provided a text box for Chapter 2. Chapter 3 benefited from Rita Da Costa's contributions on diaspora networks. Chapter 4 includes substantial inputs on mobile banking by Laura Recuero Virto, OECD Development Centre's Europe, Africa and Middle East Desk. Chapter 5 includes a text box by Rui Esteves and David Khoudour-Castéras. Finally, Chapter 6 features text boxes by Ángel Melguizo and Iliana Olivié, Real Instituto Elcano, and draws upon a background paper by Francisco Alba, Colegio de Mexico.

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Preface

The OECD *Latin American Economic Outlook 2010* is released at a critical moment for Latin America and the Caribbean. On the heels of the first unambiguous contraction of GDP in 25 years, a considerable drop in foreign trade and investment and a surge in unemployment, the region's economic outlook for 2010 is already substantially positive. However, the one million dollar question is to what extent Latin America's economic pragmatism of the past decade will translate into the necessary stability to focus on the many development challenges the region faces in a still uncertain global economic scenario.

Once more, this year's *Outlook* focuses attention on Latin America's long-term development challenges, rather than on short-term fluctuations that frequently distract our everyday attention from the underlying issues at stake. After exploring fiscal policy issues in our 2009 *Outlook,* and underscoring ways that tax revenues and public spending could do more to combat poverty and inequality, this edition of our annual flagship publication on Latin America turns its attention to another of the region's main challenges: maximising the contribution that migration and remittances can make to improve the well-being of so many Latin Americans affected by this phenomenon.

With more than 20 million Latin Americans living outside their country of birth – almost 5% of the region's total population – the effect of the global crisis on migration patterns and the numerous immigrants already living abroad will be a major one for most Latin American economies. Indeed, immigrants are already among the hardest-hit labour force groups in most OECD countries, with their unemployment rates increasing more rapidly than among natives, mainly as a result of their over-representation in sectors particularly affected by the downturn (e.g. construction, tourism). By examining the implications of global people, money and idea flows for employment, social protection and financial development, we hope to generate concrete proposals about how both sending and recipient countries can benefit from migration.

This year's OECD *Latin American Economic Outlook* includes two important new features that respond to the feedback and recommendations readers provided regarding previous editions. First, the publication contains an opening macroeconomic overview; naturally, this year's macro overview analyses the effects of the global economic crisis on the region, with a focus on structural dimensions. In addition, the report also includes specific country notes analysing recent migration trends and policies in the six Latin American states belonging to the Governing Board of the OECD Development Centre – Brazil, Chile, Colombia, Costa Rica, Mexico and Peru – as well as Argentina and the Dominican Republic, who are currently negotiating their accession. These country notes, as well as similar information for other countries in the region, will be available on the report's website.

The macroeconomic overview argues that, contrary to the general belief that greater exposure to trade and capital flows makes an economy more vulnerable, larger financial and commercial flows have resulted in many cases in the building up of resilience to withstand the crisis, allowing most Latin American countries to better confront the shock. By looking at the current account and financial links, we have produced new exposure and resilience indexes comparing the current crisis to that of 1981-1982.

The conclusion is straightforward: the region weathered the most recent shock from a much better position, allowing many countries to use fiscal and monetary tools to stimulate demand without

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compromising macroeconomic fundamentals. Some of the best practices in the world in terms of fiscal policy are indeed located in the region, with countries like Chile being a benchmark in this field even for many OECD countries. Nonetheless, the report rightly points out that successful countercyclical policies are those that take into account long-term development perspectives while striking a balance between creating high-quality jobs and spending on the most vulnerable segments of society.

The OECD *Latin American Economic Outlook 2010* reaffirms the OECD Development Centre's commitment to provide a bridge between the OECD and Latin America. This commitment is reflected at the institutional level, with the aforementioned six Latin American countries already participating in our daily activities as members of our Governing Board. It also translates into a growing set of policy dialogue activities that include seminars, expert meetings, briefing sessions with public officials and dissemination events that ensure the outreach and visibility of our work. The *Paris International Economic Forum on Latin America and the Caribbean*, co-organised with the Inter-American Development Bank and the French Ministry of Economy, Industry and Employment, is a good example of how we raise the profile of Latin American issues in OECD member countries. The recent participation of former Chilean President Ricardo Lagos and Dominican Republic Minister of Economic Affairs, Planning and Development, Juan Montás, in our Development Centre Governing Board meetings also illustrates this growing exchange of experiences with high-level officials from the region.

Since its launch in 2007, the OECD *Latin American Economic Outlook* has painstakingly built up and relied upon collaboration with other leading actors and institutions working on the region's development. Beyond the annual presentation of the report at the Ibero-American Summits, we have developed ongoing working relations with governments, academics, business leaders and representatives of civil society, including international organisations such as the Inter-American Development Bank, the Organization of American States, the United Nations Economic Commission for Latin America and the Caribbean, the Iberoamerican General Secretariat, the World Bank, the International Monetary Fund, the Andean Development Corporation and the Central American Bank for Economic Integration, among others.

In a similar vein, we recently launched *INNOVAlatino*, a groundbreaking three-year initiative benchmarking and assessing the various dimensions of innovation in Latin America, in close collaboration with the INSEAD Business School and the Telefónica Foundation. The first report of this new project will be presented next May, at the 6th European Union – Latin America and Caribbean Summit taking place in Madrid. These flagship publications and studies are accompanied by a whole range of research activities, such as the recently published working paper *Revisiting Political Budget Cycles in Latin America* (Nieto Parra and Santiso, August 2009). In 2008 alone, the Development Centre's Americas Desk published three working papers, seven policy insights, three policy briefs and five articles in specialised journals and magazines.

As a meeting ground for OECD and the emerging economies, the OECD Development Centre is fully committed to advancing our understanding of the processes and changes that are shaping a new world. Together with our forthcoming *Global Development Outlook*, which will map the shifting geography of the global economy and its impact on development, the work of our regional desks focusing on Latin American, African and Asian affairs is aimed at finding innovative solutions to the global challenges of growth, poverty and inequality.

We sincerely hope that this OECD *Latin American Economic Outlook 2010* contributes to this endeavour, providing new ideas on how to build a stronger, cleaner and fairer Latin America.

Javier Santiso
Director and Chief Development Economist
OECD Development Centre
October 2009

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Acronyms and Abbreviations

AEB	Asociación Española de Banca (Spanish Banking Association)
AML	Anti-Money Laundering regulations
ATM	Automated Teller Machine
BLS	Bureau of Labor Statistics
CAEI	Current Account Exposure Index
CARICOM	Caribbean Community
CECA	Confederación Española de Cajas de Ahorros (Spanish Confederation of Savings Banks)
CFT	Combat the Financing of Terrorism regulations
CIDE	Centro de Investigación y Docencia Económicas
CPI	Consumer Price Index
CRA	Credit Rating Agency
DHS	Department of Homeland Security
DIOC	Database on Immigrants in OECD Countries
DPR	Diversified Payment Rights
ECB	European Central Bank
ECLAC	Economic Commission for Latin America and the Caribbean
ECODAR	Encuentro de Cooperación Diáspora Argentina
EMBI	Emerging Markets Bond Index
EU	European Union
FDI	Foreign Direct Investment
Fed	Federal Reserve
FLACSO	Facultad Latinoamericana de Ciencias Sociales (Latin American School of Social Sciences)
FRI	Fiscal Resilience Index
GDF	Global Development Finance online
GDP	Gross Domestic Product
HH	Herfindahl-Hirschman
HP	Hodrick-Prescott
IDB	Inter-American Development Bank
IFS	International Financial Statistics online
IMF	International Monetary Fund
IRCA	Immigration Reform and Control Act
KYC	Know Your Customer

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MERCOSUR	Mercado Común del Sur (Southern Common Market)
MRI	Monetary Resilience Index
MTO	Money Transfer Operator
NAFTA	North American Free-Trade Agreement
NELM	New Economics of Labour Migration
NGO	Non-Governmental Organisation
NHS	National Health Service
ODA	Official Development Assistance
PPP	Purchasing-Power Parity
SAWP	Seasonal Agricultural Workers Programme
Sedesol	Secretaría de Desarrollo Social (Social Development Secretariat)
SEDLAC	Socio-Economic Database for Latin America and the Caribbean
SELIC	Sistema Especial de Liquidação e Custodia (Special System for Clearance and Custody)
SIM	Subscriber Identity Module
SPS	Sistema de Pensiones Solidarias (Solidarity Pensions System)
TARP	Troubled Asset Relief Program
TED	Treasury Bill-Eurodollar (spread)
TEI	Total Exposure Index
TFP	Total Factor Productivity
TOT	Terms of Trade
TRI	Total Resilience Index
UNCTAD	United Nations Conference on Trade and Development
USSD	Unstructured Supplementary Services Data
WAP	Wireless Application Protocol
WDI	World Development Indicators
WEO	World Economic Outlook

EXECUTIVE SUMMARY

Executive Summary

Latin America has not escaped the global economic crisis, but it has stood up to it with a new resilience. Every country in the region has suffered the effects of the downturn and overall gross domestic product is expected to shrink 3.6% in 2009. However, it is already apparent that Latin America is rebounding from the shock more rapidly than the majority of developed economies. Most importantly, it is doing so without compromising its significant progress towards its long-term development goals. The rate of recovery is expected to be substantial in 2010, even if short of the typical growth rates of over 5% that characterised the bonanza of 2004-08. The duration of the global recession will be only one factor in determining future growth rates and at least as important for each country will be its capacity to stimulate its economy through sustainable policy efforts. In many countries, moreover, changing patterns of international migration and remittances will also affect the depth of the crisis and the menu of available policy options.

MACROECONOMIC OUTLOOK: NO TRADE-OFF BETWEEN INTERNATIONAL EXPOSURE AND RESILIENCE

Contrary to prevailing wisdom, Latin American countries that have opened their markets to international competition during the last decade have not proved more vulnerable to the current global economic downturn. This is a striking achievement and one that contrasts sharply with the experience of these countries in past international crises. Since the early 1990s most of Latin America has moved away from the false sense of security that protectionist policies provided and begun instead to reap the long-term benefits of globalisation. The key element this time is that trade and financial openness have been accompanied by the building of resilience mechanisms that bolster the ability to withstand negative shocks.

Comparing measures of exposure and resilience demonstrates how over the last 30 years Latin America has learned some of the hard lessons of the debt crisis of the 1980s. The current account demonstrates how countries in the region are increasingly – and willingly – exposed to a more globalised world through ever larger trade and remittance flows, but also that they have diversified both the composition and destination of their export baskets. A similar trend is observed in the financial realm: while financial openness and exposure are higher than during the crisis of the 1980s, all Latin American economies have built their resilience by running more sustainable deficits, extending the maturity profile of their public debt, and building foreign reserves against potential liquidity shortages. Additionally, most domestic banking systems have during the last five years increased their level of provisions for non-performing loans and kept out of the speculative games that have proved so damaging elsewhere.

The downturn highlights as never before that the key determinant for Latin America's long-term growth is responsible and sustainable policy management. In most of the region the crisis of the 1980s prompted the adoption of fiscal and monetary policies that led ultimately to unsustainable debt burdens, inflation and a generalised loss of institutional credibility. In a crisis the pressure is to boost the size of a stimulus package – and so its benefits for short-term performance – but this must

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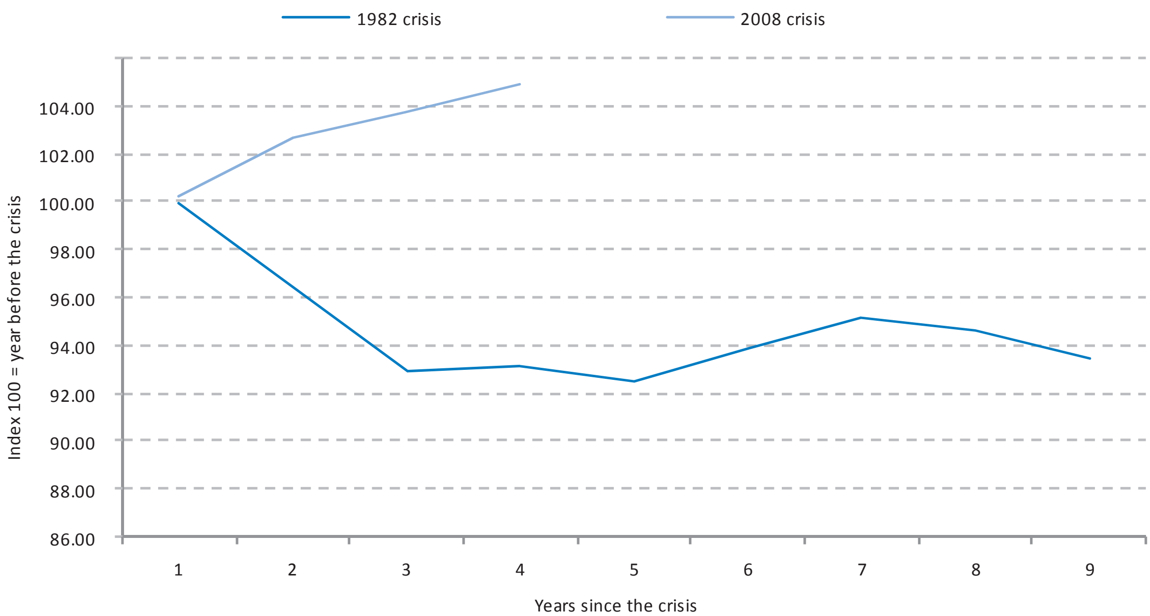
always be weighed against the long-term sustainability of such policies. Thankfully, responsible and credible policy making in Latin America since the 1990s has created substantially more headroom for effective and sustainable fiscal and monetary stimulus than was the case in the 1980s. Chile, which wisely chose to accumulate significant fiscal resources during the boom in copper prices, is the best placed. Peru and Mexico follow closely, with Brazil and Colombia coming next.

Monetary authorities in most Latin American countries have worked hard to build credibility in recent years and are now rewarded with a more robust monetary-policy tool kit. Central-bank authority and integrity are increasingly anchored in responsible policy making rather than *de-jure* exchange-rate regimes or price controls. Policy makers can mobilise reserves to address liquidity shortages, rather than watching them haemorrhage in vain attempts to protect the value of the domestic currency. Inflation targeting in countries such as Brazil, Chile, Colombia, Mexico and Peru has proven particularly effective in building institutional strength.

The need to direct spending towards the more vulnerable members of society is paramount during a downturn. The latest GDP forecasts for 2009 and 2010 combined with well-accepted measures of the link between poverty and growth suggest that poverty could increase by close to seven percentage points by the end of 2010. This translates into almost 39 million people newly falling below national poverty lines and would almost entirely reverse the progress made during the five years before the crisis. Poverty reduction, of course, does not come only from growth but also from effective social policies broadly construed. Unfortunately, those countries that have made significant redistributive gains – notably Argentina – now lack the resources necessary to maintain the policies behind these gains. Here again, the priority must be to limit the damage caused by the global recession without compromising long-term sustainability.

Relative GDP Per Capita in Latin America and OECD countries: The 1982 and 2008 Crises



Source: OECD Development Centre calculations based on OECD *(*2009), Consensus Forecast (2009), and IMF WEO database (April 2009).

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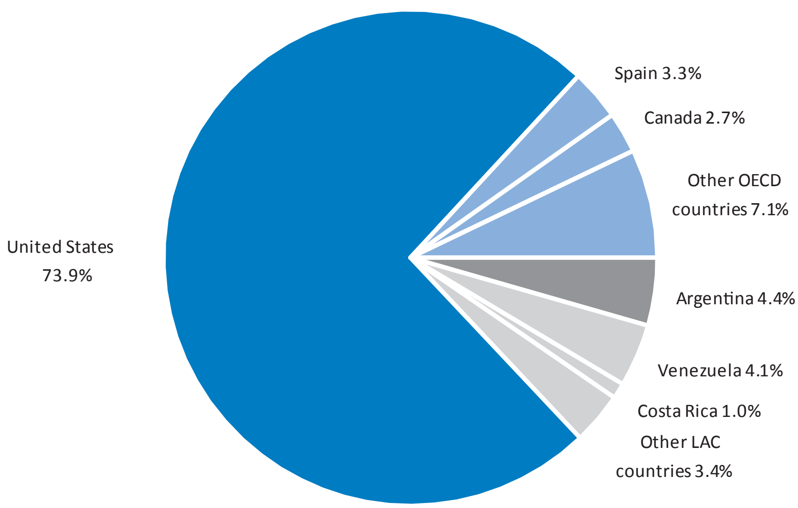
INTERNATIONAL MIGRATION WILL BE A KEY FACTOR IN THE REGION'S ECONOMIC RECOVERY

International migration has moved to centre stage in public-policy debates. The economic crisis has already had its effects on migration flows and trends. Many communities of Latin Americans living abroad are among the hardest hit by job losses in OECD countries, a result of their concentration in sectors particularly affected by the downturn, such as construction and tourism. Growing unemployment has also hardened public sentiment in many destination countries, putting immigration policies under review. Migrants from Latin America and the Caribbean are frequently at the centre of such debates given that they represent close to 25% of the foreign born in OECD countries.

The ability of governments to tap into international migration's potential for development may be a new tool to help the region to surface from the current crisis. The decision to migrate and choice of destination are usually associated with improved earning opportunities, family reunification and the presence of existing migrant communities. A better understanding of these motivations and their interactions will lead to policies which maximise the many positive effects of this phenomenon and minimise its (fewer) negative impacts. Policy makers should consider the complex nature of migration, which implies not one but three types of flows: of people, of the money they send home as remittances, and of ideas propagated through migrant and diaspora networks.

Latin American and Caribbean Migrants by Country of Destination
(Percentages, circa 2000)



Source: OECD Development Centre calculations based on OECD (2008), Database on Immigrants in OECD Countries and the 2000 round of national censuses in Latin America (processed with ECLAC Redatam+SP online).

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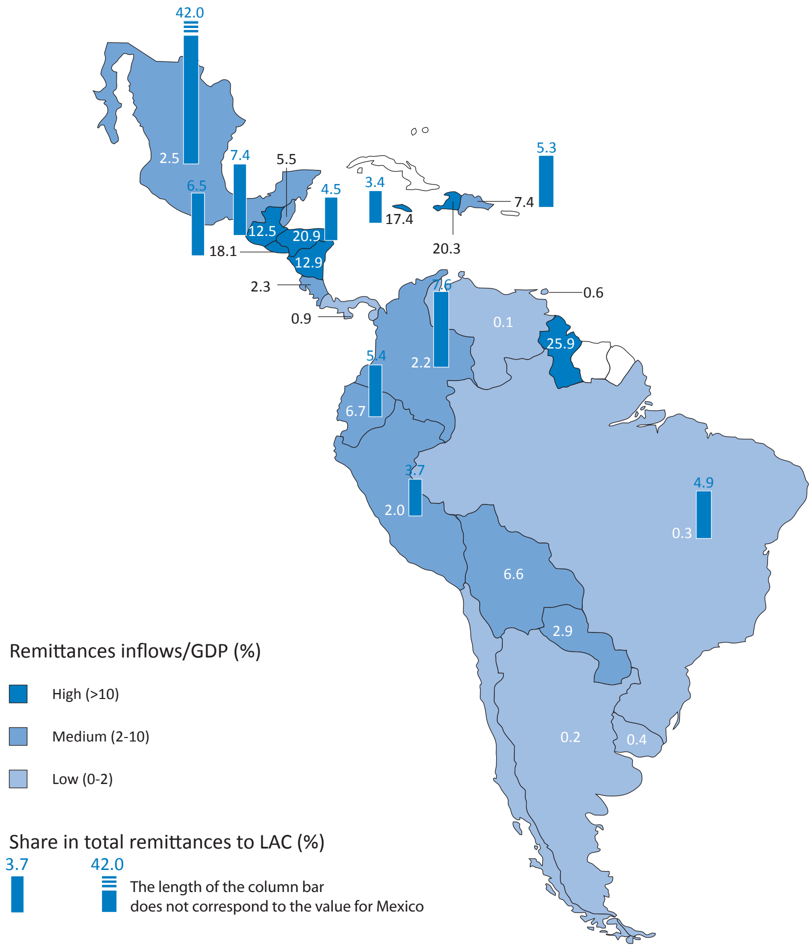
18 INCREASING COMPLEXITY OF MIGRATION, BUT DECREASING MONEY FLOWS

Workers' Remittances to Latin American and Caribbean Countries



Note: a) Remittances are measured using the estimates of workers' remittances in the balance of payments current transfers account. *b)* Three different clusters have been identified (high, medium and low). *c)* The columns correspond to the ten countries having a higher share in total remittances to LAC – Mexico (42.0), Colombia (7.9), Guatemala (7.4), El Salvador (6.5), Ecuador (5.4), Dominican Republic (5.3), Brazil (4.9), Honduras (4.5), Peru (3.7), Jamaica (3.4).

Source: OECD Development Centre calculations based on IMF International Financial Statistics and Balance of Payments Statistics databases.

StatLink http://dx.doi.org/10.1787/715776403060

More than 20 million Latin American and Caribbean people reside outside their country of birth. Some three-quarters are in the United States; many of the remainder are in Argentina, Venezuela, Spain and Canada. Intra-Latin American migration to other Latin American countries is also increasingly important; including Central Americans moving to Mexico, Colombians to Ecuador and movements in both directions between Paraguay and Brazil. Increasingly, too, migration has ceased to be a one-way street: many migrants go home, and many circulate back and forth over time.

Migrants are also less and less uniform. Although the average education levels of Latin American migrants are lower than the average in the countries they go to, there is substantial variation from one corridor to another: while more than two-thirds of Mexican-born adults in the United States have only primary education, nearly three-quarters of South Americans in the United States have secondary or tertiary education. Similarly, the gender breakdown of migrants varies between corridors. Flows to the United States, for example, tend to be disproportionately male (56%, compared with 50% of migrants worldwide). Heterogeneity is seen too in the socio-economic condition of remittance-receiving households: families receiving remittances in Mexico, for example, are mainly at the bottom of the income distribution, while in Peru the richer the household the larger the share of remittances received.

The most pressing financial concern is the decline of remittances as a result of the economic crisis. According to August 2009 estimates from the Inter-American Development Bank (IDB), remittances to the region will decline 11% in current US dollar terms. The money sent home by migrants is a sizeable flow – accounting for more than 10% of GDP in a number of economies, particularly in the Caribbean and Central America – so this first decrease since the IDB began monitoring remittance flows in 1999 will be crucial for the region. The impact will be most immediately felt by many migrants' families back home who tend to use remittances to supplement consumption. Contrary to the general belief, this remittance-funded consumption can be quite productive and translate in practice into an investment in human capital: the ability to keep kids in school longer, for example, or to spend more on health care.

At the macroeconomic level, remittance inflows are still far less volatile than other flows, notably foreign direct investment and export earnings. How they respond when economic conditions deteriorate back home, however, varies from country to country. In some countries worsening conditions appear to encourage their migrants abroad to send more home, but in others the reverse seems to be the case. Similarly relevant in the current context is the correlation between remittances and economic conditions in the migrants' destination country.

MIGRATION IS POSITIVE FOR WAGES AND GROWTH DESPITE CONSTRAINTS ON MOBILITY AND RETURN

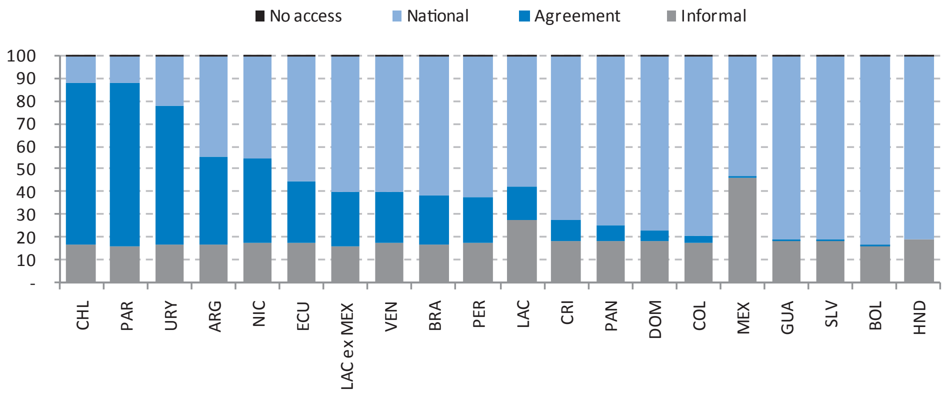
One of the ways migration affects economic development in Latin American countries is through labour markets. The evidence so far is scant but nonetheless suggests that emigration can increase wages for those who remain at home, as has happened for better-educated workers in Mexico in recent decades. At the same time, there is concern in many countries – particularly in the Caribbean and Central America – that highly skilled emigration to OECD countries is causing a "brain drain", though in fact this may be more a symptom than a cause of development problems.

For economies that receive immigrants, migration does not exert a downward pressure on local wages or employment, as is usually thought. The prevailing explanation is that immigrants and native-born workers often do not compete for the same jobs; migrants are frequently clustered in construction, agriculture, tourism and home care. Evidence shows this pattern of non-competition is repeated in Latin American countries of destination, such as Argentina, Costa Rica and Venezuela. Moreover, immigration can contribute to economic dynamism, something amply demonstrated by the Spanish economic boom: the influx to Spain of 4.5 million immigrants is reckoned to have accounted for as much as a third of the country's economic growth between 1996 and 2006.

The current crisis has prompted the re-emergence of measures to encourage return migration. These appear to have learned some, but by no means all, of the lessons from the European induced-return programmes of the 1970s. Their success may also be undermined by the blunting of any incentives to return when economic conditions are also poor in migrants' home countries.

A more structural impediment to international labour mobility – and an important obstacle to return migration – is the absence of "pension portability". Too often when migrants cross a border they lose their accrued pension benefits or have to bear tremendous (if sometimes hidden) costs. The construction of a network of bilateral agreements between countries covering Latin American and Caribbean migrants is a work in progress, but should have a positive effect on return migration to the benefit of both origin and destination countries.

20 Pension Portability Regimes in Latin America
(Percentage of total migrants by country of origin, 2000)



Source: OECD Development Centre calculations based on data from Avato *et al.* (2009).

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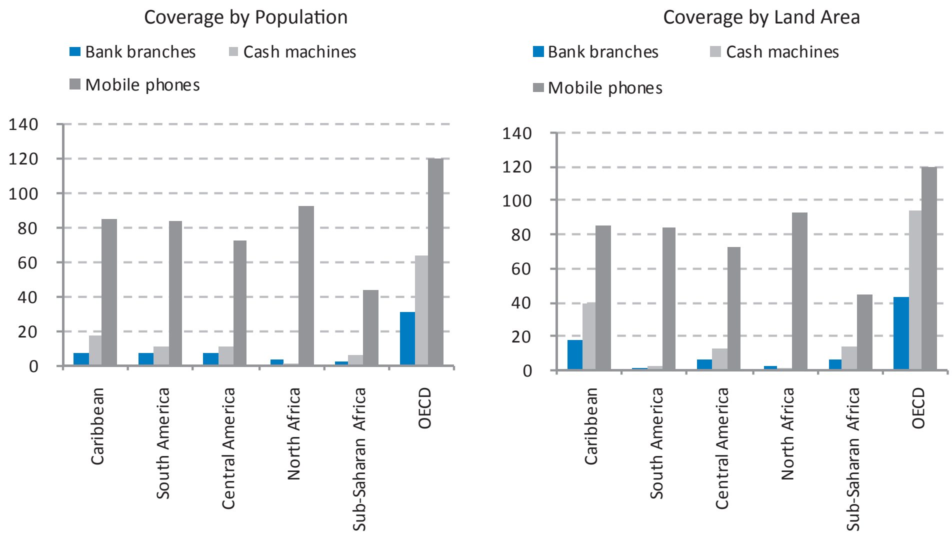
FURTHER FORMALISATION OF REMITTANCE FLOWS CAN ENCOURAGE FINANCIAL DEVELOPMENT

Migration is intrinsically related to financial deepening by means of remittances. The experience of former countries of origin in the OECD, including Greece, Italy, Portugal and Spain, stresses the importance of creating incentives for the use of formal channels in sending remittances. The incentives needed today are different, and useful examples can be found in existing successful programmes in the Latin America region such as the Mexican *Tres por uno*, the Colombian *Mi Casa con Remesas* and the Peruvian *MiVivienda*.

Some initiatives encouraging "bankarisation"of remittances offer interesting avenues for further action, but combating low financial literacy among those who have difficulty accessing financial services must remain a priority. Competitive and contestable markets in the money-sending business are essential to keep costs down and policy should work to foster transparency in the sector. Given the apparent importance of exchange-rate movements to both the senders and receivers of remittances, governments should consider initiatives which mitigate currency risk such as stabilisation funds to guarantee remittance proceeds in domestic currency. Thinking more broadly, other measures that can help formalise remittance flows should likewise be pursued. Mobile payments, for instance, are emerging in the region as an alternative to traditional bankarisation, thanks to their broad distribution networks and low sending costs; however their development is being hampered by the lack of a clear regulatory framework.

Distribution Networks – Demographic and Geographic Reach



Note: Geographic branch penetration and geographic ATM penetration refer to the number of bank branches and ATMs per 1 000 km^2, respectively. Demographic branch penetration and demographic ATM penetration are defined as the number of bank branches and ATMs per 100 000 people, correspondingly. For mobile phones, coverage refers to the number of mobile lines per 100 inhabitants.

Source: OECD Development Centre calculations based on Recuero Virto (2009).
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REMITTANCES CAN ALSO BOOST CAPITAL MARKETS

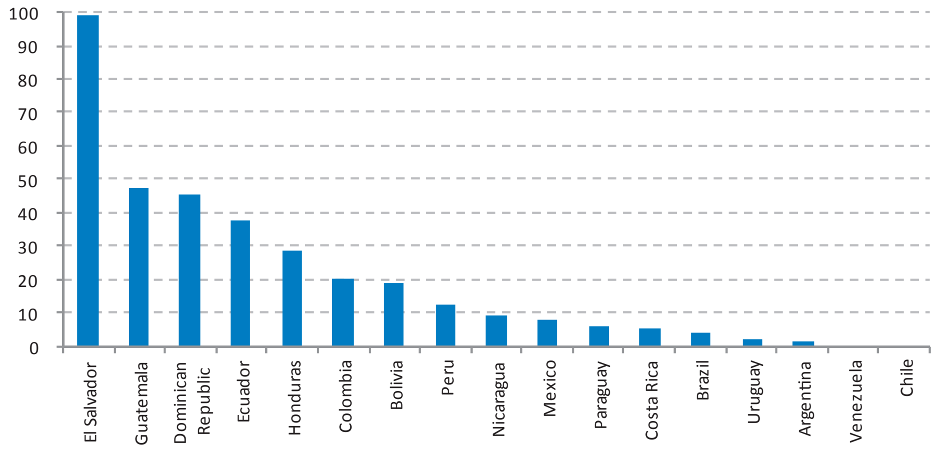
Remittances can act on a wider stage than the retail financial markets and their potential to enhance the development of Latin America's capital markets remains largely untapped. In many Latin American and Caribbean economies, low levels of domestic savings or underdeveloped private capital markets make foreign lenders more reliable suppliers of capital than domestic sources. Remittances could provide a new source of macro financing for the region, not only by putting more money on the table, so to speak, but also by being used to improve sentiment in the capital markets.

Remittance flows can be harnessed in two ways to provide immediate access to capital: the securitisation of future flows of remittances (and other resources), and diaspora bonds. For the securitisation of future flows – a debt instrument whose principal and interest are secured against future remittances passing through a given financial institution – research shows that the rating available and price achieved can beat those for the relevant sovereign borrower. They may therefore reach investors not available to the sovereign. Diaspora bonds, meanwhile – securities issued by governments specifically to tap the wealth of their nationals abroad – provide an interesting investment vehicle that again can potentially capture new funds. Their success will depend on the investment attractiveness of the country to its own migrants and this usually depends in turn on variables such as economic stability and control of corruption. Brazil, Colombia, El Salvador, Mexico, Panama and Peru appear best positioned to explore the viability of such instruments

As regards sentiment, remittances may influence the view of the capital markets through their impact on the work of the credit rating agencies. They have above all an indirect effect on ratings through the volatility of external flows. Research supports the view that the rating agencies do take remittance flows into account when rating sovereign borrowers. A favourable trend of remittances can improve ratings but the reverse also applies. Moreover, the impact of remittances remains small compared to other factors that affect ratings. That said, "shadow ratings" – ratings calculated for countries not rated by the main agencies – confirm the significant effect that remittances would have on ratings for small, low and middle income Central American and Caribbean countries where the relative size of these flows is high.

22 Volatility of Inward External Flows With and Without Workers' Remittances

Percentage change on volatility excluding remittances (average 1993-2007)



Note: The height of each bar represents the percentage change in annual variation of external resource inflows over the period 1993-2007 if workers' remittances are eliminated; a higher bar means that remittances reduce volatility of external flows to a greater extent.

Source: Avendaño *et al.* (2009).

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FIVE CONCRETE ACTIONS TO MAXIMISE THE POTENTIAL OF MIGRATION FOR LATIN AMERICAN DEVELOPMENT

By its nature, international migration is a shared policy responsibility of both the sending and receiving countries. Five concrete actions provide the pillars for reform to improve the lives of many migrants and their families, while helping societies in both Latin American and OECD countries maximise the gains from migration and minimise its risks:

1. **Create legal and flexible labour market access on a par with labour demand.** Employers in many sectors aggressively seek immigrant workers to fill gaps in their labour market, and even so cannot always find enough workers. The mismatch of labour supply and demand, and the large earnings differentials with countries of destination, mean that many Latin American and Caribbean migrants will seek out these job opportunities, whether or not legal channels are available. The incentives for irregular migration – and the associated human cost – could be reduced by expanding legal channels.
2. **Extend social protection to more Latin American migrants.** The lack of employment-related benefits and in particular pension portability are major obstacles to migrant mobility and return migration. Making pension rights fully portable – as they are already for some Latin American migrants – would increase the social wage earned by these migrants and reduce their vulnerability in old age. The necessary steps to achieve this are both clear and capable of being accomplished in the short term, notably ratifying the *Convenio Multilateral Iberoamericano de Seguridad Social* (adopted at the XVII Ibero-American Summit in November 2007), and the United States-Mexico social security agreement (signed in 2004).

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3. **Leverage the benefits of remittances.** Although ratings agencies take remittances into account when calculating the sovereign risk of emerging economies, they do not monitor many countries with high levels of remittances relative to GDP, particularly in Central America and the Caribbean. A public-private partnership could boost country coverage and supply useful information on as-yet unrated economies, to the benefit of their cost of public debt. Governments in the region should review if they are doing all they can to incentivise migrants to channel remittances into community investments, following the example set by initiatives such as *Tres por uno* in Mexico.

4. **Lower the costs of remittances.** The cost of remittance transfers to Latin America has fallen dramatically in the last decade, in part because of competition among service providers, in part because of government initiatives to reduce costs. Mobile payments are an emerging example in the region of an alternative and cheap transmission system. However, a clearer regulatory framework is needed if these services are to achieve all that they can.

5. **Engage diasporas**. The worldwide communities of Latin Americans and Caribbeans and their children born abroad constitute emerging transnational political forces that can be engaged both by countries of origin and by countries of destination. Governments should harness these networks to pursue policy objectives jointly in the domains of labour markets, social protection, integration, development co-operation and international migration.

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PART ONE

Macroeconomic Overview

LATIN AMERICA AND THE CRISIS

"When the United States sneezes, Latin America catches a cold" is a familiar refrain. But what if the US economy has flu? If history is a guide the answer is unsettling. From July 1981 to November 1982 the United States experienced one of its two longest post-war recessions (the other started in November 1973 and also lasted 16 months). Recession quickly spread throughout Latin America. But – deep as those initial recessions were – the region's real drama was just unfolding. While developed economies recovered in time and returned to their pre-crisis economic paths, Latin America fell into a debt crisis that led to a sharp reduction in potential growth. This drag on growth persisted for more than a decade – in some countries for a quarter of a century – and left lasting scars on Latin America's income and development.

The crisis of the 1980s did profound and long-term damage to the region. Most countries, however, face this crisis from a stronger position

The long-term consequences of the 1980s crisis were devastating. Until 1981, real per capita income in Latin America and the Caribbean and the OECD economies was growing in tandem, at an average 3.6% per year. But after 1981, growth rates in the two regions diverged and the OECD countries pulled ahead. Average real per capita income in the OECD economies rose from 2.5 times the Latin American and Caribbean equivalent to 3.6 times. As Figure 0.1 shows, if Latin America had kept growing at OECD rates, real GDP per capita today would be almost 70% higher than in 1981, rather than less than 20% higher as has actually happened[1]. Unsurprisingly, the poorest part of the population has been hit the hardest. As discussed later, the proportion of the population beneath the poverty line fluctuates with the business cycle, decreasing during booms and increasing in recessions. However, low growth rates after the 1980s crisis prevented any long-term reduction in the region's 40% poverty rate.

Today there is measured optimism that history will not repeat itself. In the last quarter of 2008 developed economies followed the United States into a new recession, labelled by many as the most severe since the Depression. But according to both market and analysts' forecasts, this time Latin America is expected to suffer only a cyclical downturn, without compromise to its recent significant progress in long-term development.

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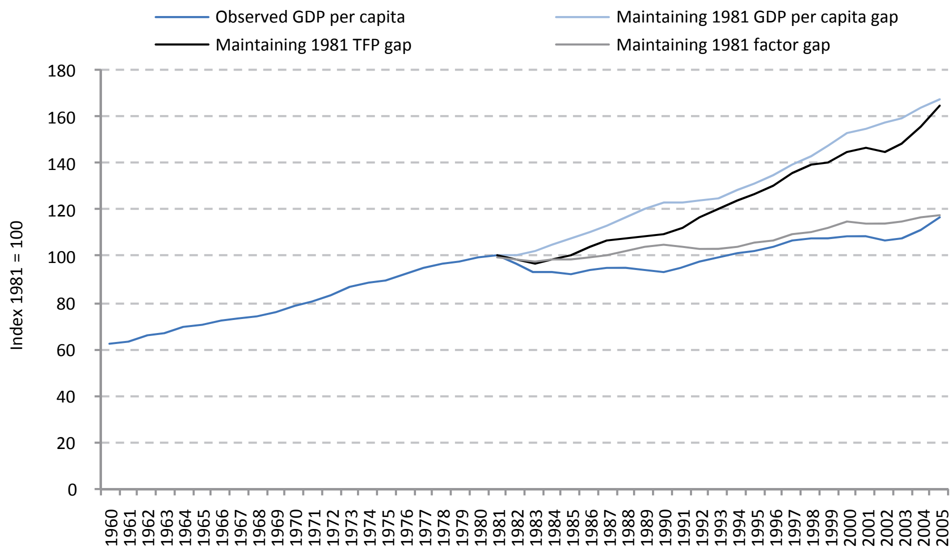
Figure 0.1. Evolution of Real GDP Per Capita and Counterfactuals for Latin America



Source: OECD Development Centre calculations based on Blyde *et al.* (2009).

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Regional GDP per head is expected to fall 3.6% in 2009, recovering 1.6% in 2010. This compares with a decline in OECD countries of 4.1% in 2009

As shown in Figure 0.2, forecasts point to a sharp 3.6% contraction in GDP per capita during 2009 followed by a modest rebound of 1.6% in 2010 (based on *Consensus Forecasts,* June 2009)[2]. Even though these numbers at once put paid to over-optimistic talk of Latin America's "decoupling", they are encouraging about the longer term. Not only is growth expected to resume as soon as 2010, but also several countries in the region are expected to fare better than the OECD average. Peru, Panama and Uruguay, for example, are expected to show positive GDP growth in 2009 (2.2%, 0.9% and 0.2%, respectively), while for most countries in the region the expected contraction is only 1 to 2%, compared to an average 4.1% decline in OECD countries[3]. These figures give some support to the view of many economists that Latin America faces the current crisis with a newly gained resilience.

To understand and assess this resilience one needs first to understand the mechanisms by which cyclical downturns hinder long-term growth. Recessions are costly in the short term but – in principle at least – they can also present opportunities for the kind of deep restructuring and needed-but-unpopular policies that would be politically impossible in better times. They can bring a cleansing effect to the economy with benefits in the long term. However, there is ample practical evidence that recessions hamper rather than boost long-term growth. Following financial crises economies usually do not reach their previous potential-output trajectory (Cerra and Saxena, 2008). Furthermore, crises have been associated with a permanent decline in the trend of GDP per capita, mainly due to a collapse in total-factor productivity (TFP) (Blyde *et al.*, 2009). These large and persistent declines in TFP reflect the significant deteriorations in policies and institutions during crises[4]. High levels of income inequality combined with uneven access to insurance against the effects of the cycle are fertile ground for inefficient and unsustainable policy responses[5]. This combination of problems was undoubtedly present during the aftermath of the 1980s crisis, a time when Latin American countries were left with unsustainable debt burdens.

Better practices and greater room for the use of fiscal and monetary policies are among the key factors behind today's optimism, even though the world crisis is in many ways deeper than that of the 1980s (GDP across the OECD countries fell

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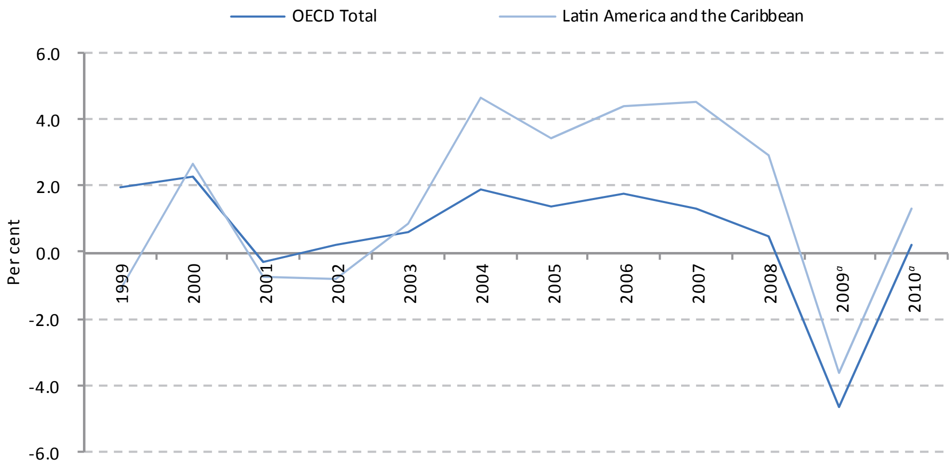
0.8% in 1982; far less than the 4.1% expected for 2009). Several governments and central banks have built both the credibility and the financial resources that can help them combat the worst of the downturn, without compromising the path for development successfully outlined – and in some cases consolidated – during the last decade. This highlights that a key risk for the region is the duration of the crisis in the OECD economies. If this is protracted, the policy response in Latin America may progressively deteriorate as room for manoeuvre diminishes and the pressure for unsustainable policies resurfaces.

Figure 0.2. Real GDP Per Capita
(Percentage change on previous year)



Notes: *a)* forecast as of June 2009.

Source: OECD Development Centre calculations based on OECD (2009), *Consensus Forecasts* (2009), and the IMF WEO database July 2009.

StatLink http://dx.doi.org/10.1787/714755574184

This greater resilience is the result of recent fiscal and monetary policies, and a number of structural changes in the region's economies

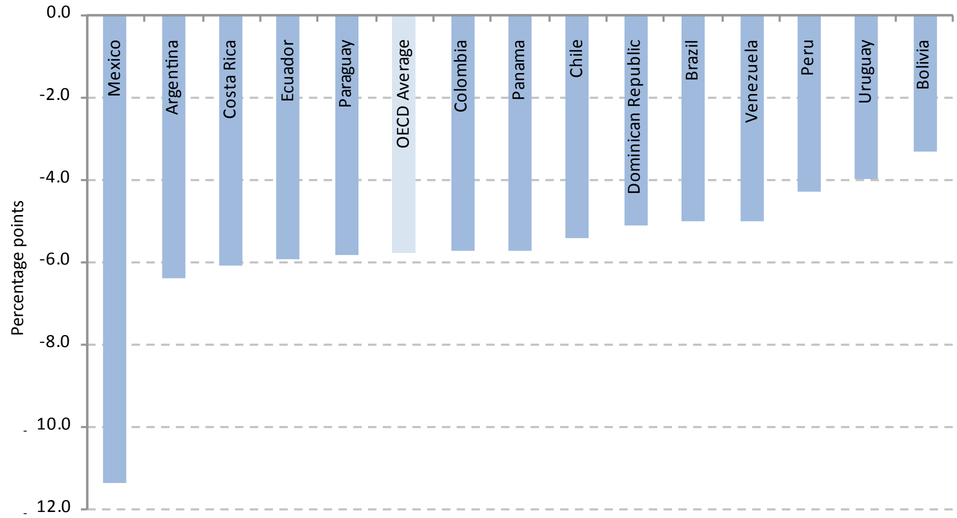
But it is not just improved fiscal and monetary policies that are helping several Latin America countries to withstand the current turmoil. A number of structural changes are also important, and go some way to explaining the varying degrees of exposure and resilience found in different countries of the region. The market reflects this heterogeneity and its forecasts differ significantly from one country to another.

To isolate the effect of the crisis, Figure 0.3 shows the change between GDP forecasts for 2009 made shortly before the collapse of Lehman Brothers in mid September 2008 and those as of June 2009. While Mexico has lost more than 11 expected percentage points of growth in 2009, the fall in expectations for countries such as Chile and Peru are less than the OECD average of 5.8 percentage points.

What factors explain such differing responses to a single global crisis? The answer relies on the strength of the two linkages through which Latin America's economies interact with the rest of the world:

- **The current-account link,** through which goods and services are exchanged (export and import flows) and through which other current transfers, such as income and remittance flows, take place.
- **The financial link,** through which savings are converted into cross-border lending and investment.

Figure 0.3. Short-term Output Cost of the Crisis
(Percentage of GDP)



Note: Percentage-point change between real GDP growth forecasts for 2009 as of June 2009 and June 2008.

Source: OECD Development Centre calculations based on OECD (2008*b,* 2009) and *Consensus Forecast* (2009).

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A deep and protracted crisis in developed economies affects both of these. Such crises reduce both demand for Latin American exports and the disposable income of remittance-sending migrants. Additionally, economic agents in developed economies react to crises by diverting investment towards traditionally more secure domestic assets. As a result, a crisis alters the normal run of flows in both the current account and financial channels and hence spreads through all economies in the region in a process referred to as "contagion".

How strongly the crisis is felt through each of these two linkages will depend on two elements: an economy's degree of exposure to the flows, and its resilience to shocks transmitted through each channel. Since the 1990s most of the world – Latin America included – has moved towards globalisation. Countries have progressively opened their frontiers to commercial and financial markets, distancing themselves from the more protectionist policies that predominated for most of the 20th century. This higher exposure and interdependency do not necessarily mean more vulnerability. As financial and commercial flows have grown larger countries have simultaneously gained resilience against potential adverse shocks: economies have increasingly diversified their exports, hedged their financial portfolios, built up foreign liquidity provisions, protected their revenues from terms-of-trade risk and stabilised their macroeconomy so as to have some room for sustainable fiscal and monetary stimulus. As will be shown later in this chapter, developing this resilience provides better protection for an economy than simply reducing exposure to financial and commercial flows.

To assess Latin America's current economic condition and its outlook, this chapter therefore first examines the scale and characteristics of the current global crisis and compares it with previous crises the region has faced, particularly the disastrous 1980s. It constructs and analyses a sequence of indicators of how exposed given economies are to international shocks and also their built-in resilience to them. It then examines the scope for and potential effectiveness of counter-cyclical fiscal and monetary policies. The conclusion is a discussion of expectations for Latin America's long-term development and the risks to these.

THE CURRENT CRISIS: HOW IT DEVELOPED

Global Liquidity Crisis: August 2007 to August 2008

The global crisis has developed in two stages. The first was the contraction of liquidity starting in August 2007

Global financial markets felt the first gust of cold air in mid-August 2007, when a widespread liquidity shortage forced the European Central Bank (ECB), the Federal Reserve (Fed) and other major central banks to inject USD 326 billion rapidly into the world financial market. This concerted monetary effort was aimed at restoring a sudden fall in interbank lending. Behind this collapse of the overnight market – part of the lifeblood of the financial system – were banks hoarding liquidity, unwilling to lend to each other. This reaction, though sudden when it came, was the outcome of a gradually accumulating fear among the banks that they had wrongly assessed their own and their peers' balance-sheet exposure to the US subprime mortgage market.

The fear was justified. Following the bursting of the subprime bubble a year earlier casualties had been mounting and increasingly included not only the expected, such as bankrupted mortgage lender New Century Financial[6]. Large divisions of major financial institutions were seeking extraordinary injections of capital or facing crisis. Balance-sheet mismatches appeared to be sprouting in all corners, with firms sliding into trouble or announcing huge write-downs in a growing number of countries: joining the Bear Stearns hedge funds were HSBC Holdings in the United Kingdom, insurer AXA in France and bank IKB Deutsche in Germany. The loss of confidence that followed can clearly be traced through the "TED spread". This is defined as the difference between the inter-bank interest rate and that implicit in the price of short-dated US government debt and therefore provides a measure of the perceived credit risk of lending to commercial banks. The evolution of the TED spread is shown in Figure 0.4. By September 2007 it had risen to levels not seen since the "savings and loans" crisis in 1987.

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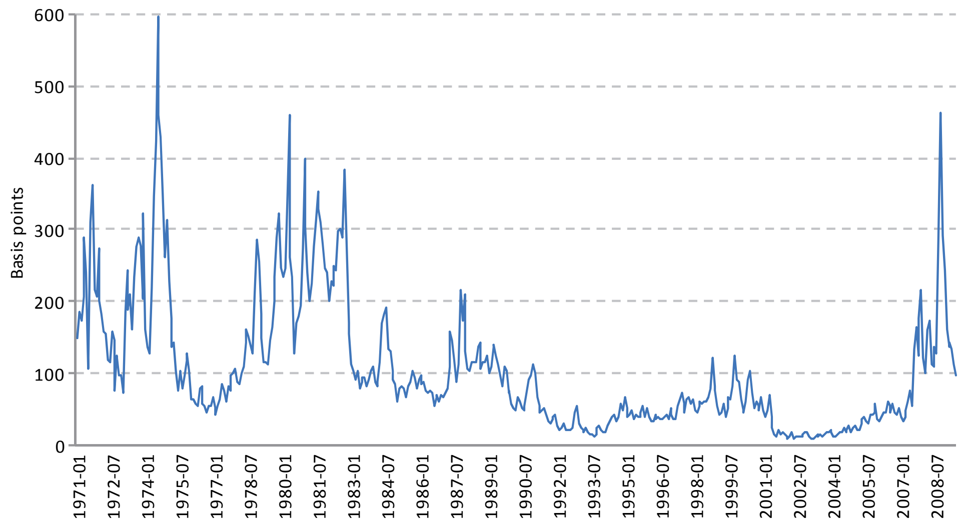
Figure 0.4. TED Spreads
(Basis points)



Note: Spread, in percentage points, between the daily 3-month Euro-Dollar deposit rate and 3-month Treasury bill secondary market rate (discount basis); monthly averages.

Source: OECD Development Centre calculations based on Federal Reserve Board, *Selected Interest Rates* database.

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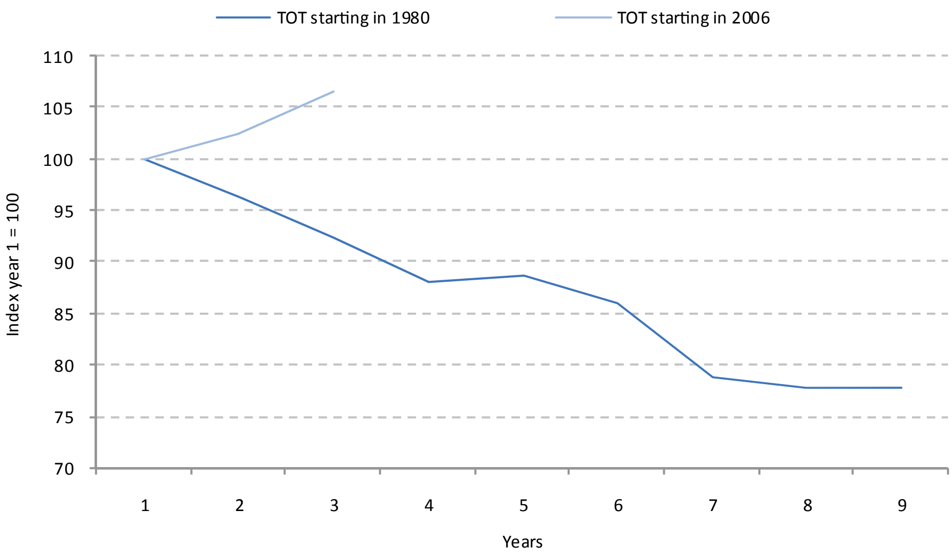
Over the next 12 months, and despite significant efforts from all major economies, those early liquidity shortages progressively developed into a full-fledged credit crisis. By August 2008 the Fed had reduced interest rates to only 1.5% from 5.25% a year earlier. It had also deployed a battery of non-traditional tools to provide further liquidity to the financial system. The ECB, the Bank of England and the Bank of Japan followed, albeit at a slower pace: rates in Europe went from 5% to 4.25%, in the United Kingdom from 5.75% to 5% and in Japan rates remained at a low 0.75%. On the fiscal front, several stimulus packages were put in place. Despite these fiscal and monetary policies, global credit continued to dry up and TED spreads did not abate.

Yields on Latin American securities rose, but less than might have been expected. The markets appeared to recognise the region's improved risk profile

As the financial crisis spread among developed countries, the old script initially ran as expected: uncertainty rose; investors started rebalancing their portfolios to shield them from risk; "flight to quality" proceeded at an almost stampede-like pace and risk premiums soared. But rebuffing history, Latin America withstood the unfolding of these events admirably well. During previous episodes of financial turmoil, such as the debt crisis in 1982, the East Asian crisis of 1997-98 or the Russian crisis in 1998, "flight to quality" meant the risk premiums on Latin American sovereign bonds soared in tandem with those of high-yield "junk" bonds in developed economies. But this time, global financial markets differentiated and decoupled the risks embedded in Latin American investments from those in other assets traditionally viewed as risky. As a result spreads for Latin American government bonds rose more slowly. Three reasons explain the modest impact of the liquidity crisis on Latin America's financial outcomes:

Figure 0.5. Evolution of Terms of Trade in Latin America: 1980 versus 2006



Note: Index 1980 and 2006 equals 100, respectively.

Source: OECD Development Centre calculations based on ECLAC Economic Indicators and Statistics database (*BADECON*).

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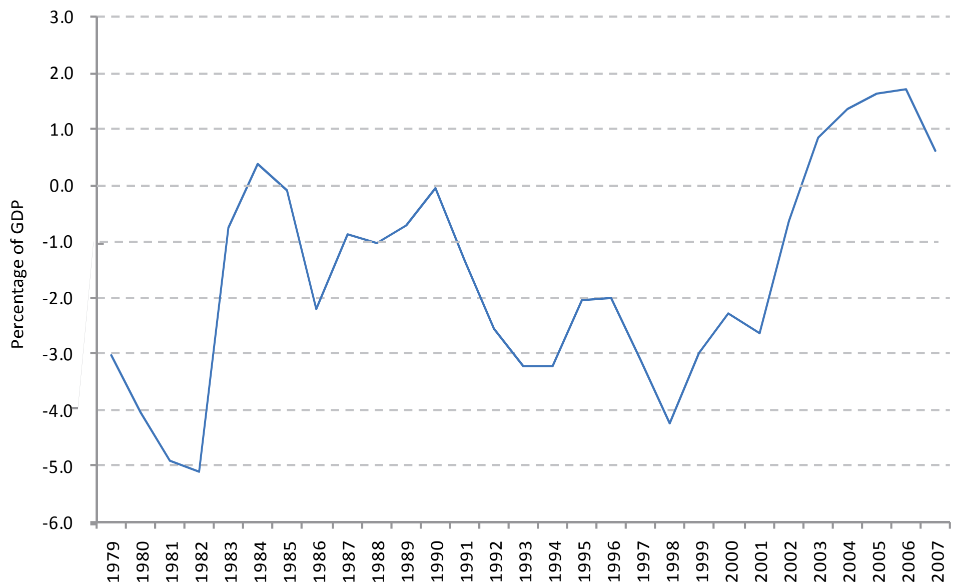
- **The current account linkage remained solid.** As shown in Figure 0.5, Latin America's terms of trade remained firm, thanks to high commodity prices sustained by China's continued growth and expectations of its future demand. In turn, strong exports provided the collateral needed to calm increasingly worried international investors. Remittances remained stable since labour-market pressures in the OECD economies were still contained up to the second quarter of 2008. (At this point the average OECD unemployment rate was 5.8%, and in two key sources of remittances it stood at 5.4% in the United States and 10.5% in Spain.)
- **Economies were more resilient to financial shocks.** Lower sovereign-debt ratios with longer maturities and a greater proportion of debt denominated in domestic currency reduced the risk of and effect of self-fulfilling capital flights. Moreover, central banks had been gaining credibility freed from (potentially dangerous) mandates to defend the exchange rate.

Terms of trade held up, the denomination and tenor of sovereign debt was more sustainable, and most nations had become exporters of capital

- **Most countries in the region faced the crisis as net exporters of capital.** Figure 0.6 shows that, unlike in the crisis of the 1980s, this time most countries in the region had positive current account balances (though remained net debtors of total stocks).

Unfortunately, this first year was not to be the end of the crisis. Instead September 2008 saw it enter a new phase both deeper and likely to be more protracted.

Figure 0.6. Latin America's Current Account Balance



Note: Data set is the aggregate of Argentina, Brazil, Chile, Colombia, Costa Rica, the Dominican Republic, Mexico, Peru and Venezuela.

Source: OECD Development Centre calculations based on IMF IFS and World Bank WDI databases.

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Credit-Freeze and World Recession: September 2008 Onwards

The collapse of Lehman Brothers in September 2008 triggered a new and much deeper phase of the crisis

On 15 September 2008 US investment bank Lehman Brothers filed for bankruptcy triggering a full-fledged banking crisis. Economic agents in industrialised countries (businesses, consumers and governments) revised downwards their expectations and prepared themselves to face the worst global recession since the Depression. Now Latin America was hit by large negative shocks through both its financial and trade linkages: on one hand, a shock in global credit markets much larger than a year earlier, on the other, a collapse in world income and global trade.

The financial shock was immediately apparent in the banking sector, lifting TED spreads to levels not seen since 1973 – a time when the world was dealing with the collapse of Bretton Woods, the oil crisis and the 1972-73 stock market crash. More than just credit markets were affected and stocks around the globe also plummeted. At the same time the value of major currencies became increasingly uncertain. Volatility in the euro-dollar exchange rate reached levels not seen since the 1980s, as shown in the lefthand panel of Figure 0.7. Investors ran for shelter. The rise in the relative price of gold – a traditional safe haven during uncertain times – provides eloquent evidence of such behaviour; its evolution can be seen in the righthand panel of Figure 0.7.

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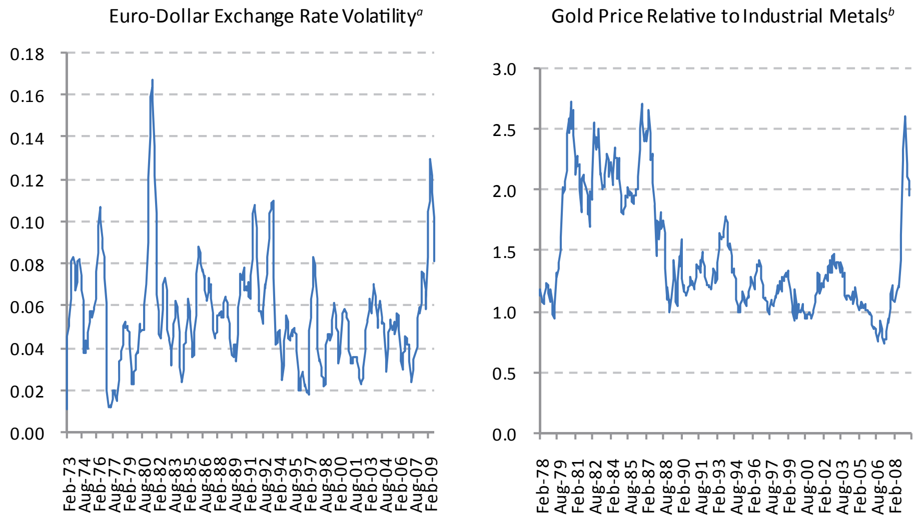
Figure 0.7. Measures of Global Risk Aversion and Volatility



Note: *a)* 12-month rolling standard deviation; *b)* Ratio between the spot US dollar prices.

Source: OECD Development Centre calculations based on Datastream database.

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Volatility reached record level, and both world trade and commodity prices collapsed

What is worse, the financial shock this time was now accompanied by a sizeable trade shock. World trade collapsed in the final quarter of 2008 and first quarter of 2009, as credit for trade finance dried up and global demand retrenched. The OECD forecasts a 16% decline in world trade in 2009 (projections as of June 2009).

The lefthand panel of Figure 0.8 shows that world demand in 2009 is expected to shrink the most since the Depression, dragging down prices for Latin American exports and commodities in general (illustrated in the righthand panel). Remittances have also fallen sharply, and will remain under pressure as a result of rising unemployment rates in the OECD countries. The OECD forecasts high unemployment in two key remittance-sending countries: the United States with 10.1% unemployment expected for 2010 and Spain with an expected 19.6%.

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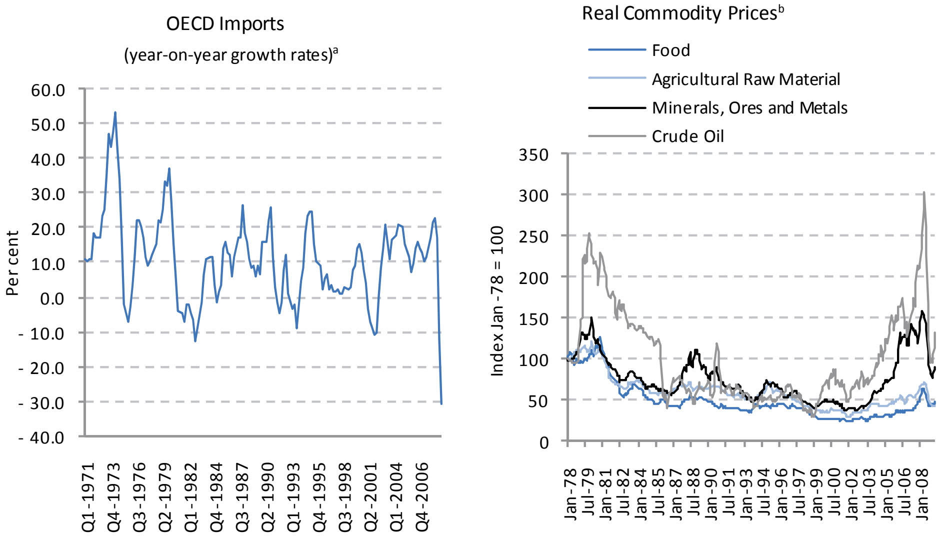
Figure 0.8. External Demand and Commodity Prices



Notes: a) Imports are denominated in current US dollars; *b)* US dollar prices deflated by US CPI (excluding food) seasonally adjusted.

Source: OECD Key Short-term Indicators, 2009; OECD Development Centre calculations based on UNCTAD Commodity Price Statistics Database and BLS database.

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EXPOSURE AND RESILIENCE IN LATIN AMERICA AND THE CARIBBEAN

The external environment is at least as bad as in 1980s. The ability of the region to withstand this challenge is tested using measures of exposure and resilience

The combination of trade and financial shocks described above is alarming. Many global indicators are in territory last seen in the early 1980s – at the start of the Latin American debt crisis and lost decade. Given the many structural changes undergone by Latin American economies since the late 1980s and early 1990s is history is bound to repeat itself? Have these changes improved or worsened the ability of the region's economies to confront today's crisis? On one hand, financial and trade globalisation have meant that countries are increasingly exposed to global turmoil. On the other, Latin America has also developed its resilience.

To assess and compare how global shocks impact different Latin American economies, we have constructed indices for trade and financial links. These distinguish between exposure and resilience as follows:

- **Exposure:** size of external linkage, measured both by its size relative to the economy and by its importance to growth.
- **Resilience:** attributes that may resist or dissipate external shocks channelled through each linkage, such as diversification of exports or international liquidity provisions. Another important source of resilience, common to both the trade and financial linkages, is the availability of counter-cyclical policy tools.

Current Account Linkages and Diversification

For several Latin American economies exports have become an increasingly important driver of growth. However, global crises reduce world purchasing power thus weakening demand for a significant number of Latin American industries. How exposed to a fall in world commerce are countries in Latin America and the Caribbean? Nine countries are analysed: the seven largest regional economies (Argentina, Brazil, Chile, Colombia, Mexico, Peru and Venezuela) and two representatives of Central America and the Caribbean (Costa Rica and the Dominican Republic).

Exposure on the current account is measured as a combination of trade openness, reliance on export growth and remittances

In each country, two distinct measures represent the level of exposure to global trade shocks. The first is the degree of trade openness: larger volumes of trade amplify the macroeconomic impact of shocks to exports or to the terms of trade. To measure trade openness a ratio well established in the literature is used: trade volume (exports plus imports) over GDP. In order to focus on the productive structure of a country, PPP values further corrected by terms of trade (from the Penn World Tables 6.2) are used. For each country openness in 1981 and 2007 is considered, these being the years preceding the 1982 and 2008 crises. Openness thus defined is then scaled from 0 to 1, with higher values representing a higher degree of exposure. Costa Rica is assigned the value of 1 in 2007, when trade volume reached 98% of GDP. A value of 0 is given to Argentina and Brazil in 1981, when their trade volumes constituted only 12% of their respective GDPs.

A second dimension, dynamic in nature, refers to the role exports play in the development strategy of each country. The development strategy chosen determines the importance of commerce in long-term growth. To measure this dimension the contribution of exports to GDP growth during the decade previous to each crisis is considered. Flows are valued in dollar rather than PPP terms so as to capture the importance of external demand in the total income generated in each economy. Countries are then scaled as in the case of trade openness. Chile is assigned a value of 1 in 2007 (when export growth had contributed 67% of total GDP growth over the previous decade) and the lower bound of 0 corresponds to Argentina in 1982 (where exports contributed only 6% of total growth)[7].

Migration also generates new current account linkages that significantly affect both sending and receiving countries. Remittances provide one such linkage, with net positive inflows running parallel to trade in the current account of most Latin American countries. This particular source of foreign exchange has steadily increased, notably in Mexico, where remittance inflows surpassed oil international revenues in 2007 and the Dominican Republic, where remittances now represent a striking 10% of GDP[8]. Large inflows of remittances expose Latin American economies to OECD labour-market cycles, since wages are migrants' main source of earnings. Box 0.1 reviews historical evidence showing that remittances may prove less volatile than other financial flows.

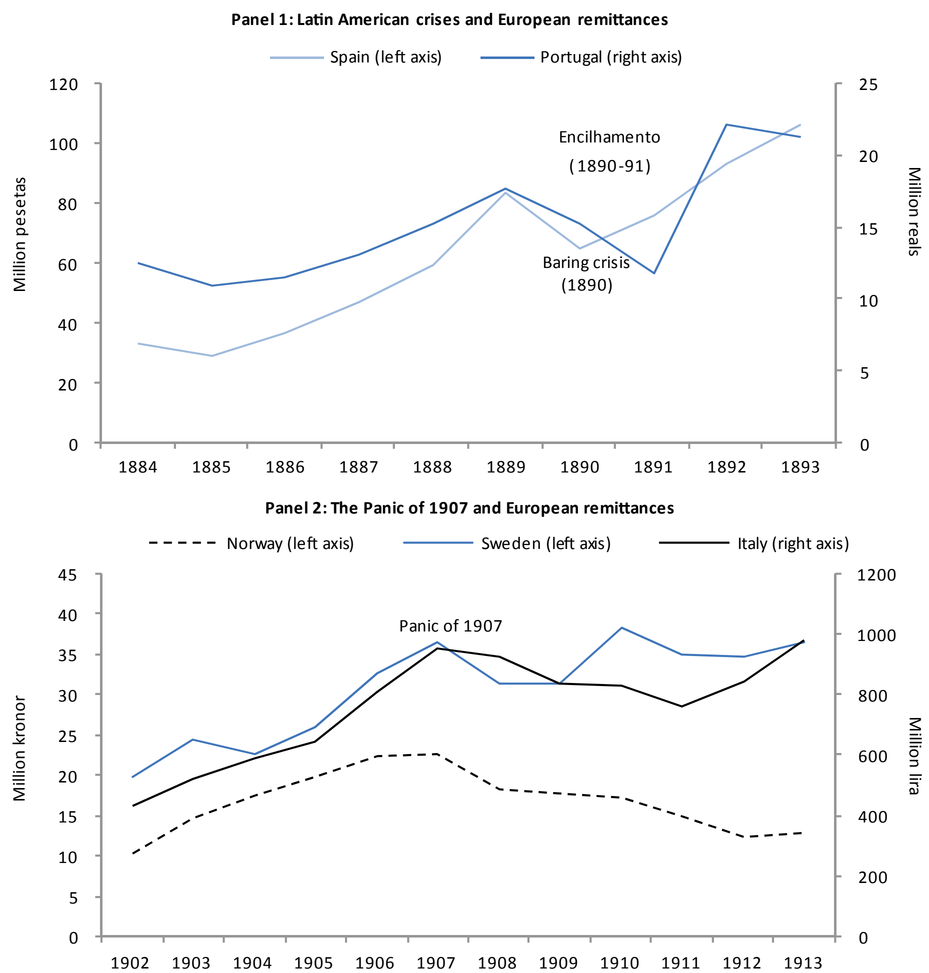
These flows are measured in a similar way as before, with the remittance-to-GDP ratios of the nine selected Latin American countries in the year previous to each of the two major crises under consideration scaled between 0 and 1. The following bounds were imposed: remittances below 0.3% of GDP were ranked 0, while remittances above 5% of GDP were ranked 1. There is considerable heterogeneity among countries: remittances in Chile and Brazil scale to close to 0 in both periods, while remittances in Dominican Republic grew from 3% to almost 10% of GDP, so hitting a score of 1.

Box 0.1. Remittances in Times of Trouble: Lessons from the Gold Standard

Economic dependence on emigrants' transfers is not unique to today's developing countries. A century ago, it was many of the European nations that had to contend with the ups and downs of remittance flows. Attracted by the rapid development of the New World, millions of Europeans moved to the distant shores of the Americas. The money they sent home irrigated European economies and spurred consumption, savings and investment. As today, these flows were sensitive to the business cycle in the countries of destination.

The clear impact of financial crises in countries of destination on remittances to Europe is illustrated by Figure 0.9. In the wake of the Baring crisis in Argentina transfers to Spain fell by 22% in 1890, while the Brazilian *Encilhamento* of 1890-91 saw remittances to Portugal decline by 14% in 1890 and 23% in 1891 (panel 1). In the same way, the Panic of 1907 in the United States was accompanied by a sharp decrease in remittances to Europe between 1907 and 1909: a 12% fall to Italy, 15% to Sweden, and 21% to Norway (panel 2). However, downward variations tended to be brief and generally did not affect the long-term trend of remittance inflows.

Figure 0.9. Financial Crises and Remittances Before World War I



Source: Esteves and Khoudour-Castéras (2010).

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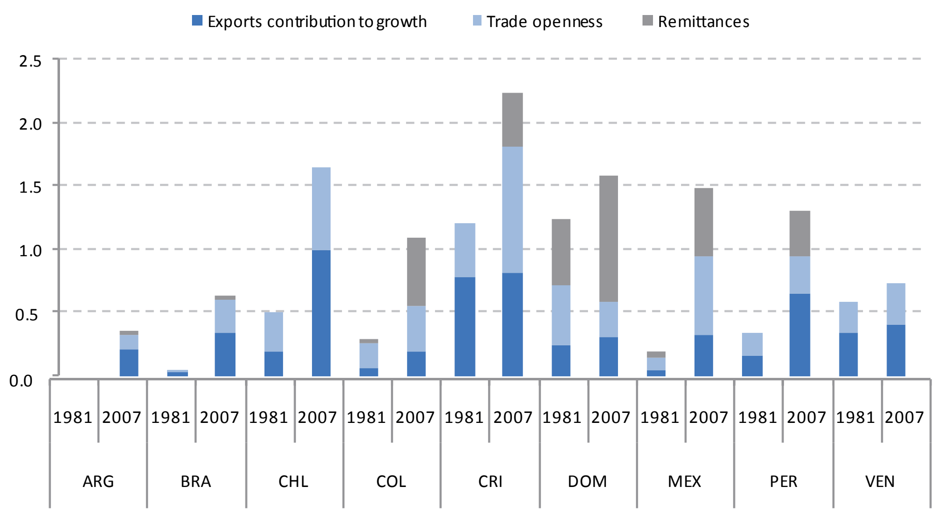
In this period before World War I, as today, remittances were nonetheless much less volatile than other balance-of-payments items from the country of origin perspective. During periods of financial instability or economic slowdown in the home country, foreign capital tended to flee, whereas migrants living abroad were inclined to send more money to their families, leading to a counter-cyclical pattern of remittances. According to Esteves and Khoudour-Castéras (2010), remittances helped preserve financial stability in peripheral European economies, notably those with fixed exchange rates. Based on a sample of economies characterised by substantial emigration (Austria-Hungary, Italy, Portugal, Spain and Sweden) over the period 1880-1913, they show that remittances substantially reduced the probability of financial disturbances, namely sudden stops and current account reversals[9]. The adjustment role of remittances was particularly significant for nations on the gold standard and which, accordingly, could not rely on exchange rate fluctuations.

These results are in line with recent findings from Bugamelli and Paternò (2006), who conclude that, for a dataset of 110 developing countries between 1976 and 2003, high levels of remittances (above 3% of GDP) reduce the risk of current account reversals. Remittances facilitate international risk sharing for countries with limited access to international capital markets, or which are faced with pro-cyclical capital movements.

Opening up to international markets may initially make countries vulnerable to financial volatility. These countries may still derive substantial benefits from financial openness if sufficient buffer mechanisms, among them remittances, help offset the costs associated with international financial shocks.

The "Current Account Exposure Index" (CAEI) is derived by adding up all three scaled results described above: two associated with trade and one with remittance flows. The evolution of the CAEI thus captures the globalisation process undertaken by the region since the 1990s. As shown in Figure 0.10, the CAEI significantly increased in all countries. Costa Rica appears today as the most exposed economy in the region, followed closely by Chile, Mexico and Peru. The Dominican Republic is also among the most exposed, mainly owing to its dependence on large inflows of remittances.

Figure 0.10. Current Account Exposure Index



Note: Each indicator is scaled between 0 and 1, with higher values indicating a larger exposure. See text for details on the construction.
Source: OECD Development Centre calculations based on the IMF IFS database, Penn World Tables 6.2, and the World Bank WDI database.

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The CAEI captures relative exposure, but it does not necessarily indicate which countries are more or less vulnerable to global shocks. A country may be more open and thus exposed to global economic cycles but may also have developed important resiliencies. A first barrier to shocks transmitted through the current account is trade diversification. Since the 1980s the Latin American export basket has indeed diversified. This has reduced terms-of-trade risk since this greater diversity means that the impact of a price drop in any given export item is proportionately less.

Current account resilience combines diversification of exports in terms of both product and markets, and geographical dispersion of remittances

To capture product diversification, we construct a Herfindahl-Hirschman index of concentration. This index reaches a maximum level of 1 if exports are all concentrated in one sector; and a minimum of 1/N if exports are equally distributed among the N different available sectors of the economy. Examining dollar value exports in each of the 90 sectors reported by UNCTAD TRAINS database (2 digit SITC v1 classification), Latin American economies have significantly diversified since the 1980s. Latin American exports were highly concentrated in 1981, with a concentration index of 0.16 compared to the 0.07 index for total world commerce. But by 2007, just before the current crisis, diversification of Latin American exports had matched the HH concentration index of world commerce, which remains around 0.07.

This diversification of exports is not a phenomenon shared by all countries in the region. While Chile significantly reduced its export dependence on copper (lowering its concentration index from 0.4 in the 1970s to 0.13 in the decade prior to the 2008 crisis), Venezuela's exports have remained highly dependent on oil (with a concentration index close to 0.85 during most of the 1970s and 0.70 in the decade before the 2008 crisis).

But product diversification is only part of the story. World markets are still not fully integrated for many of the goods and services exported from Latin America and a significant proportion of trade is carried out under bilateral agreements. Thus, a country will hedge risk by diversifying not only the content of its exports, but also their geographical destination[10]. Looking at six key destinations (the United States, EU, Japan, China, other Latin American countries and Middle Eastern countries)[11] we replicate the Herfindahl-Hirschman (HH) index for each country using total exports to each of these regions. On the one hand, the growing importance of China for countries including Argentina, Brazil, Chile and Peru increases diversification; on the other the United States has solidified its position as the main destination for exports from other Latin American countries including Colombia, Costa Rica, Mexico and Venezuela. At the aggregate level, Latin America has not diversified its export destinations.

The Current Account Resilience Index is illustrated in Figure 0.11. This captures the level of diversification in both export production and geographical destination as follows: for each of these two dimensions, we define a diversity index equal to 1 minus the corresponding HH concentration index. We then rescale each to be equal to 0 for small values (less than 0.5) and to 1 for the most diversified scenario observed. On products, the most diversified basket is Brazil's current export bundle, while the most diverse set of destinations is for current Chilean exports.

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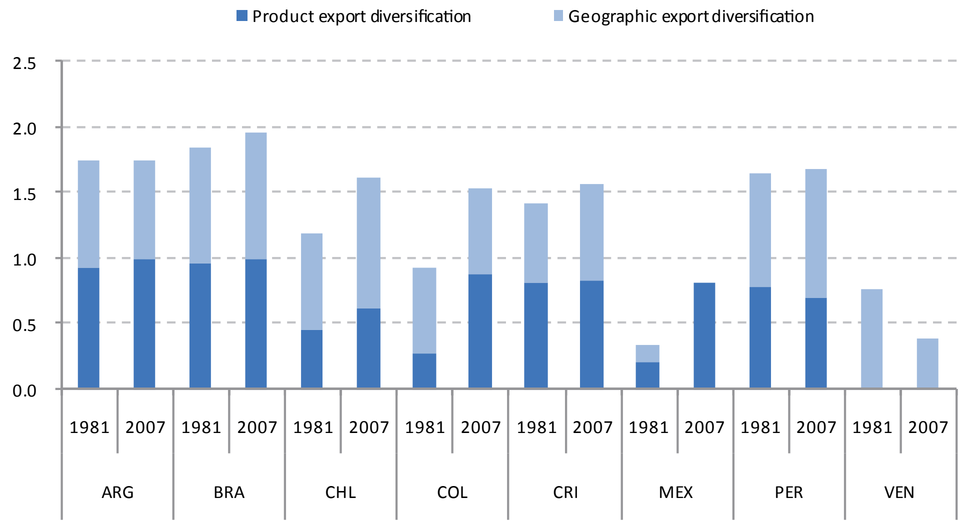
Figure 0.11. Current Account Resilience Index



Note: Each indicator is indexed between 0 and 1, with higher values indicating a larger resilience. See text for details on the construction.

Source: OECD Development Centre calculations based on UNCTAD TRAINS database.

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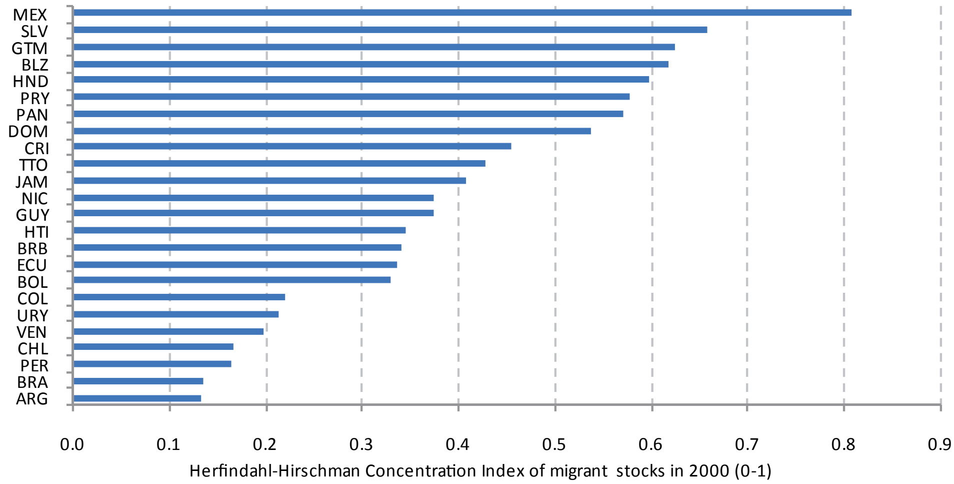
All countries in the sample show a more diversified export basket than in the 1980s. The improvement may be small in some cases, but for others, such as Colombia and Mexico, the change is large and significant. Geographical diversification, on the other hand, shows no such clear trend. Brazil, Chile, Costa Rica and Peru are the only economies to have increased diversification and, in major part, this is thanks to the emergence of China as a major global trading partner. Mexican exports are the least geographically diversified with close to 80% of the total sent through the northern border to the United States.

All countries in the sample have diversified export products. Geographical mix is less clear cut, and the position may be flattered by the rise of China as a trading partner

Brazil scores the highest for total diversification, with high diversification in both products and destinations. It is closely followed by Argentina, Chile, Colombia, Costa Rica and Peru. Despite having the most diversified export basket, Mexico ranks low given the geographical concentration of its exports. Venezuela ranks at the bottom because of its dependence on one particular export: oil.

A country may enjoy diversity not only of its export flows, but also in its inward remittances. Remittance flows are more resilient if migrants' earnings originate in a broad set of different industries or if migrants are spread over a range of host countries. Unfortunately, countries with large exposure to remittances prove in practice to be the ones least diversified. As illustrated in Figure 0.12, migrants from Mexico, the Dominican Republic and Costa Rica are highly concentrated in the United States which may be contrasted with the much broader distribution of migrants from Chile, Argentina and Brazil. Peru is the only country with large exposure to remittances which also benefits from significant resilience.

Figure 0.12. **Concentration of Migrants by Geographic Destination**



Note: The Herfindahl-Hirschman concentration index is computed using bilateral stocks of migrants for each country in the region with respect to countries in the rest of the world. The index is bound between 0 and 1, with higher values representing a higher level of geographical concentration of migrants.

Source: OECD Development Centre calculations based on Ratha and Shaw (2007).

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Financial Linkages and Resilience

Financial exposure is measured by combining the current account deficit and external debt, both relative to GDP, with an indicator of financial openness

When reading Latin American history, one rapidly observes that financial unrest is at the origin of most crises in the region. This historical vulnerability to financial turbulence has been rooted in Latin America's need for external financing, reflected – until recently at least – by positive net capital inflows (the flip side of the current account deficit historically observed in Latin America). But the region finds itself in a very different situation today, with several countries registering current account surpluses at the onset of today's crisis. Over the course of the past decade, external national balance sheets in many Latin American countries have improved enormously, creating the potential for significant macroeconomic stability.

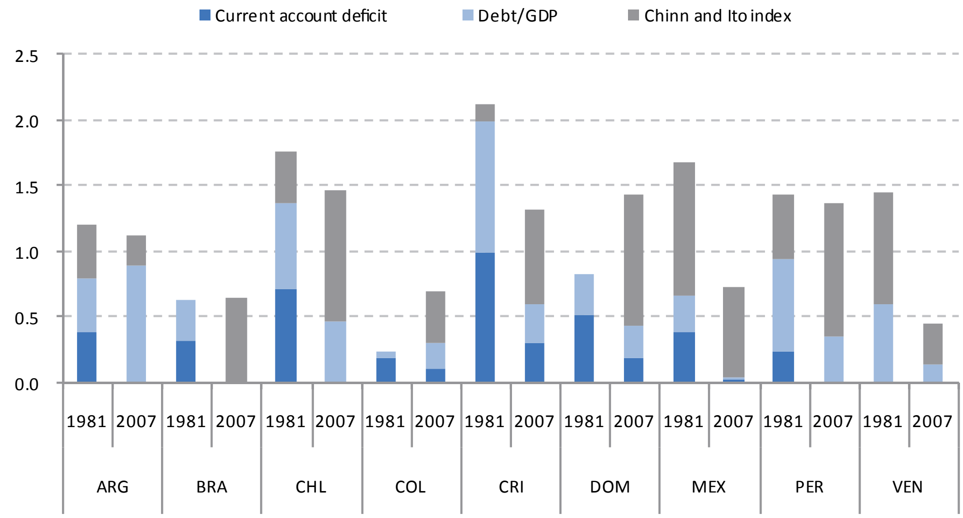
But a net current account surplus does not preclude the *need* for external financing. First, Latin America remains a net debtor. Second, there may be short-term but constant liquidity needs (for example for trade finance) which net out in any yearly or quarterly accounting. Third, a loan to be paid in ten years is very different from a loan that needs to be rolled over every six months. And lastly a country is not a set of uniform entities that behave identically. There are at least three important and very different sectors in any national economy: households, industries and government. A country that is a net lender to the rest of the world does not necessarily have all its sectors enjoying financial self-sufficiency. Thus, exposure to financial shocks should not be based only on net inflows. Just as important are gross capital inflows and debt maturities.

To examine this, we use an index of financial exposure based on three distinct variables. First are current account deficits relative to GDP, used as a proxy for ongoing financing needs. These are measured as the average of the three years prior to each of the 1982 and 2008 world crises. Second, we look at external debt relative to GDP, as a proxy of debt burden. Third, we compute the financial openness indicator developed by Chinn and Ito (2008), using information from the IMF's *Annual Report on Exchange Arrangements and Exchange Restrictions.*

This indicator seeks to capture the legal framework, looking at the existence of multiple exchange rates, restrictions on current account transactions, restrictions on the capital account, and exchange rate controls such as the requirement for exporters to give up some part of their foreign exchange[12].

As before, all three dimensions are scaled between 0 and 1 and then summed to create the financial exposure index shown in Figure 0.13. Countries that have significantly opened their financial markets, such as Chile and Peru, are not necessarily more exposed to financial shocks than in 1980 since they no longer run significant deficits and carry lower debt burdens.

Figure 0.13. Financial Exposure Index



Notes: Each indicator is ranked between 0 and 1, with higher values indicating a larger exposure. See text for details on the construction.

Source: OECD Development Centre calculations based on the IMF IFS and the World Bank WDI and GDF databases, and Chinn and Ito (2008).

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Analysts have argued that the presence of foreign banks in the domestic financial system is another potential channel for contagion. In general, FDI in the banking sector has been found to contribute to more efficient and better-functioning financial markets in the region (Micco *et al.*, 2004). However, if local affiliates of international banks are required to respond to a global strategy, a liquidity shock at headquarters or elsewhere in the corporate network (for example in eastern and central Europe for European banks) might result in a contraction of credit in Latin America. Given the importance of global banks in several financial systems of the region this transmission channel could potentially be important.

The potential exposure from the presence in domestic financial systems of foreign banks is mitigated by the stronger balance sheets in the region

As the IMF pointed out in its May 2009 *Regional Economic Outlook,* systemic problems in Latin America's financial sector are mitigated by four factors. First, lending from global banks in the region is mainly undertaken by local affiliates and in domestic currency, rather than cross-border lending in foreign currency; second, affiliates do not rely heavily on borrowing from headquarters to fund loans in the local market; third, the share of foreign-currency short-term interbank lending is low; and, finally, those global banks in Latin America are not themselves significantly exposed to eastern and central European banks.

What was true for trade linkage is also true for financial linkage; the impact of the crisis does not depend on exposure alone, it also depends on each country's resilience. On this front, Latin America looks better placed than in the past. In contrast to the OECD countries, the banking sector in Latin America and the Caribbean was not materially exposed to those financial markets in the United States that triggered the crisis. The absence of large rescue packages for financial companies in the region confirms this premise. While the IMF estimates the support to banks in the advanced economies of the G20 amounts to around 50.4% of aggregate GDP for 2009, the corresponding figures for Argentina and Brazil are 0.9% and 1.5% respectively[13]. Recent research (see for example Reinhart and Rogoff, 2009) indicates that bank crises are especially costly in terms of the fiscal effort to restructure the financial sector. In this sense, if the region can withstand the current global downturn without major accidents in the financial sector it might also be able to rebound.

Financial resilience combines measures of liquidity, roll-over risk and the sustainability of external debt

In order to analyse the region's resilience to financial shocks, an index that includes liquidity, roll-over risk and measures of the sustainability of the external account is constructed. The liquidity measure used is the ratio of reserves relative to short-term external debt[14]. This is an external liquidity indicator often associated with the "Greenspan-Guidotti" rule that reserves should cover at least a year of external obligations[15]. Given that not all reserves might be available to meet short-term external obligations, a threshold of two times the short-term debt is assigned the maximum value of 1[16].

Roll-over risk is captured by looking at the maturity structure of external debt. High levels of short-term debt expose a country to sudden changes in financial market conditions, undermining debt sustainability[17]. The ratio of short-term external debt relative to total external debt is used. The value of this sub-index is set to 1 if the country holds no short-term debt and to 0 if the share of short-term debt reaches 52.9%, which is the highest value across countries and periods (attained by Venezuela in 1981).

The third resilience indicator measures the sustainability of external debt obligations. To quantify the debt burden, debt-to-GDP ratios are adjusted by the real exchange rate and for the business cycle[18]. To measure the balance of payments required to keep this debt burden constant, one needs GDP growth rates and interest rates. For the first requirement, the average GDP growth rates in the previous ten years are used. For the second requirement we take average interest rate paid on external obligations over the same period. Finally, the sustainable balance is compared with the observed balance over the latest ten years. If the observed current account balance is greater than the required balance, the external position is sustainable and the third resilience sub-index takes the value of 1. Lower values imply less sustainable positions, until a threshold of a required adjustment of 10 percentage points of GDP. Values below this threshold are assigned an index value of 0.

The resulting "External Financial Resilience Index" is the sum of all three indicators. As seen in Figure 0.14, all countries have significantly improved their resilience since the early 1980s[19]. Mexico is the most resilient country according to the index, followed closely by Chile, Colombia, Peru, Venezuela and Brazil. Examination of the external debt sustainability sub-index shows that, while in the early 1980s only Venezuela had a sustainable external position, nowadays Argentina, Chile and Venezuela have clearly sustainable positions, and Brazil, Colombia, Mexico, Peru and the Dominican Republic would require only a moderate adjustment to reach a sustainable position. Only Costa Rica would require a somewhat larger adjustment. Although Costa Rica's current account deficit has been associated with large and stable FDI inflows, a high share of short-term debt and comparatively low levels of reserves make Costa Rica more vulnerable than other countries in the region, according to this indicator. Therefore, the country's recent stand-by agreement with the IMF seems a reasonable preventive step.

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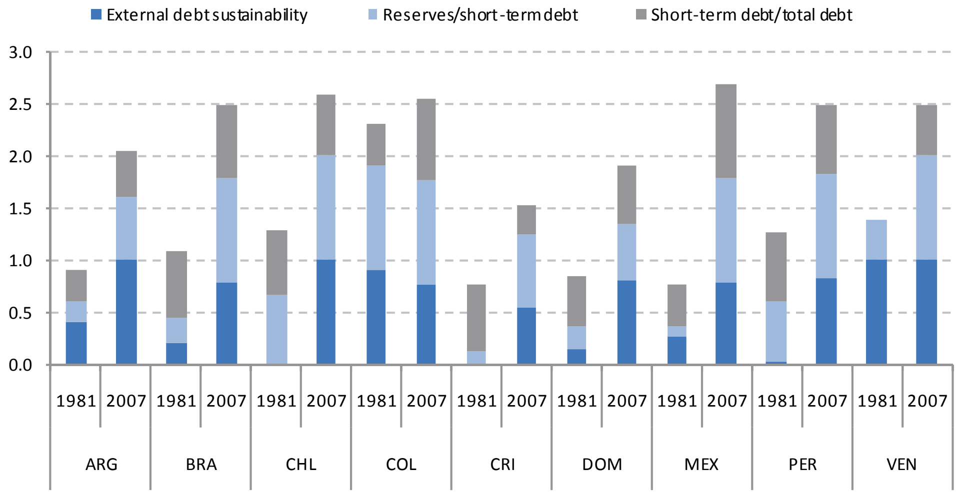
Figure 0.14. External Financial Resilience Index



Note: Each indicator is scaled between 0 and 1, with higher values indicating a larger resilience. See text for details on the construction.

Source: OECD Development Centre calculations based on the IMF IFS and the World Bank GDF databases.

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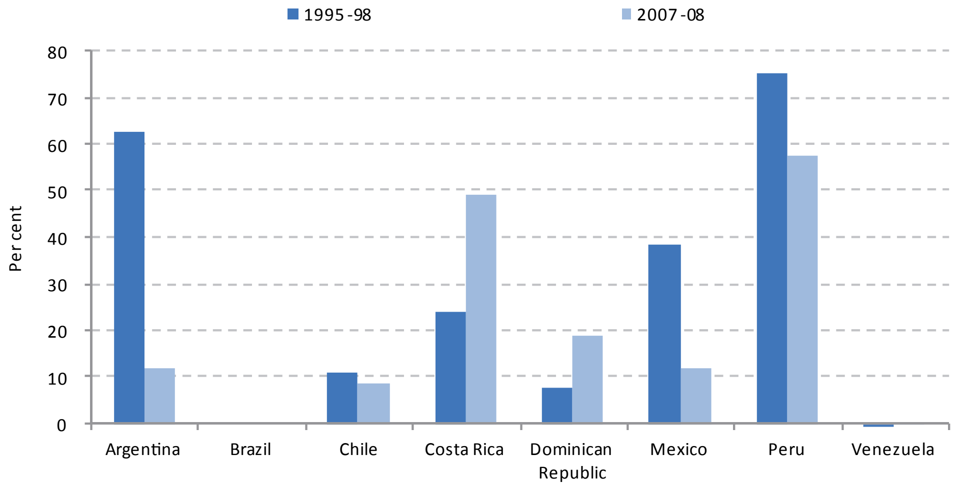
While all these indicators focus on the resilience of external finance, financial shocks can propagate and do damage to the real economy through the domestic structure of the financial system. Thus, other indicators of domestic financial soundness are needed to complement the foregoing analysis. Of particular importance is the domestic banking sector, given its relevance as the primary source of financing in all Latin American economies. Fortunately, as shown below, most of these indicators point to a significantly more resilient structure than in the past.

Resilience of domestic financial systems appears improved: with some exceptions, dollarisation is falling and provisions are higher than in OECD countries

First, financial dollarisation and currency mismatches in the banking sector are not as bad as in the past, when many economies of the region were highly susceptible to sudden interruptions in capital flows. These forced real depreciations which, in turn, triggered profound banking crises. Figure 0.15 compares financial dollarisation across countries in the region since the mid-1990s. Brazil, Venezuela and also Chile were basically not dollarised during the mid-1990s and continue to have a banking system substantially free of dollarised deposits and credits. Next are Argentina, Mexico and Peru which have significantly reduced their degree of dollarisation (although the Peruvian financial system still sees almost 60% of credit denominated in foreign currency). In the final group are Costa Rica and the Dominican Republic which have increased the level of financial dollarisation. Although it is not easy to determine the optimal level of foreign currency loans, an increase of the magnitude observed in both countries – a doubling of their share – seems risky.

Figure 0.15. Share of Foreign Currency Denominated Credit in Total Credit (Percentages, period averages)



Note: For Brazil and Venezuela, the indicator is based on deposits.

Source: Inter-American Development Bank Latin Macro Watch database.

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Countries in the region have been able to raise finance in local currency, so reducing their exchange rate risk

The riskiness of a country's national balance sheet depends also on the composition of sovereign debt. As documented in last year's *Latin American Economic Outlook* (OECD, 2008*a*), several countries in the region have been actively developing their domestic bond markets and have issued debt in local currency (overcoming the so-called "original sin" of not being able to finance themselves long-term in local currency), thereby reducing their vulnerability to fluctuations in the exchange rate.

A range of indicators of liquidity and solvency show that the financial system of the region overall is in relatively good shape. A good example is the ratio of provisions to nonperforming loans, which has increased since 2003 and generally stands higher than in the OECD countries. While for the average OECD country, provisions represent 92% of nonperforming loans as of 2008, in Latin America this indicator is well above 100%[20]. Chile, Brazil, Costa Rica, Venezuela and Mexico rank with the highest ratio of provisions to nonperforming loans. A similar message comes from the risk-adjusted ratio of capital to assets. All nine countries are well above the 8% threshold recommended by the Basel committee.

Of course, this improved resilience is only a background and Latin America's capacity to weather a world crisis will ultimately be determined by the size and sustainability of its policy response. Active fiscal and monetary policy can boost demand in the short term, but left unchecked may plant the seeds of long-term stagnation. The region's ability to balance effective fiscal and monetary stimuli with the achievement of long-term goals must therefore be next in our assessment.

POLICY RESILIENCE AND ROOM FOR MANOEUVRE

For most of Latin America, the crisis of the 1980s produced fiscal and monetary policies that led ultimately to unsustainable debt burdens, inflationary cycles, and a generalised loss of institutional credibility. In a crisis, the size of stimulus packages matters for short-term performance, but must be constrained by long-term considerations of the sustainability of such policies. Is the sustainability of Latin America's current policy programme affected by the crisis? If not, how much room do countries have for effective counter-cyclical policy stimuli? To answer these questions we construct a "Fiscal Resilience Index" (FRI) and a "Monetary Resilience Index" (MRI). As before, countries are compared in a series of dimensions that affect their capability to conduct active and sustainable policy in the current economic environment. To gain a historical perspective of the region's relative strengths, the current situation is again compared to the early 1980s.

Fiscal Policy Resilience

The Fiscal Resilience Index measures a county's ability to fund counter-cyclical policy. It combines measures of solvency, funding cost and budget balance

On the fiscal sustainability front, a foremost concern is whether governments can fund a counter-cyclical fiscal policy without jeopardising the country's external balance sheet. The ratio of external debt to exports, a standard solvency indicator, is thus the first measure included in the FRI. A country with a low ratio has a strong external balance, which allows for additional leverage from domestic agents – the government in particular. A second indicator measures governments' market credibility regarding debt repayment. That this varies considerably among governments is evidenced by their different financing costs. The relevant JP Morgan EMBI Global spread – that is the difference in yield between a benchmark sovereign bond of the country and a comparable US Treasury bond – is thus also included in the FRI[21]. The third measure included is government's budget balance as a proportion of GDP. This captures the sustainability of the policies pursued. All three indicators are averaged over the four years preceding each of the two crises analysed. These pre-crisis indicators are a weak upper bound for fiscal sustainability because fiscal revenues may deteriorate significantly during a global downturn; apparent strength on this indicator may be fleeting.

As before, all three measures are scaled between 0 and 1, with higher values representing a higher degree of fiscal resiliency. The FRI is the sum of these sub-indices. The debt-to-exports sub-index is benchmarked between 0 and the maximum value attained in the region over the two periods considered[22]. For the financing cost sub-index, EMBI spreads above 500 basis points are assigned a value of 0. For lower spreads, the indicator lies between 0 and its maximum of 1, which would indicate zero spread (that is, financing costs equal to those of the US Treasury)[23]. Finally, the government's budget balance sub-index is distributed between 0 and 1 using the largest and smallest values of the sample[24].

All countries, other than Venezuela, appear better placed now than in the 1980s

Figure 0.16 reveals several interesting features. First, on this measure all countries other than Venezuela entered the current crisis better positioned than in the early 1980s. The best placed was Chile, which had been able to accumulate significant fiscal resources during the boom in copper prices over the preceding four years. These had translated into lower levels of debt, high fiscal surpluses and the reserves in the country's stabilisation funds that are now being used to finance a fiscal stimulus of around 3% of GDP. Financial markets have acknowledged Chile's continuing resilience by upgrading its sovereign debt rating[25] at a time when several OECD countries have been downgraded[26]. Additional signs of Chile's high level of fiscal-policy credibility are the decline in spreads and appreciation of the peso following the announcement of its fiscal stimulus package. Peru and Mexico follow Chile closely in the index, and this group all enjoy significant market credibility. Brazil and Colombia are next and are also in a significantly better position than in the 1980s from a fiscal resiliency viewpoint. Further down the list are the Dominican Republic and, notably, Argentina. For these countries the room for manoeuvre is much more limited according to the FRI, a result primarily of their high financing costs and the risk of these leading to a vicious credibility/sustainability cycle.

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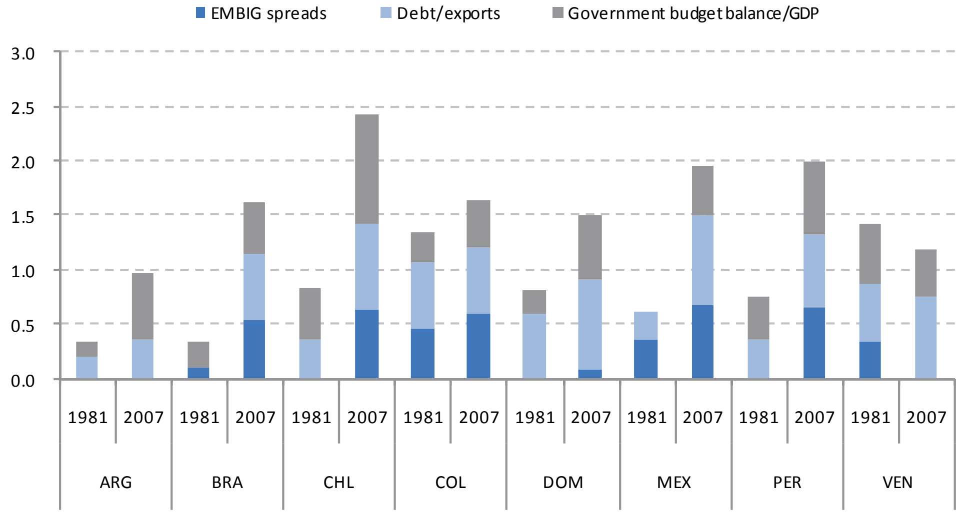
Figure 0.16. Fiscal Resilience Index



Note: Each indicator is ranked between 0 and 1, with higher values indicating a larger resilience. See text for details on the construction.

Source: OECD Development Centre calculations based on the World Bank GDF and WDI databases, ECLAC Economic Indicators and Statistics database (*BADECON*), the IMF IFS database, Institutional Investor and Datastream.

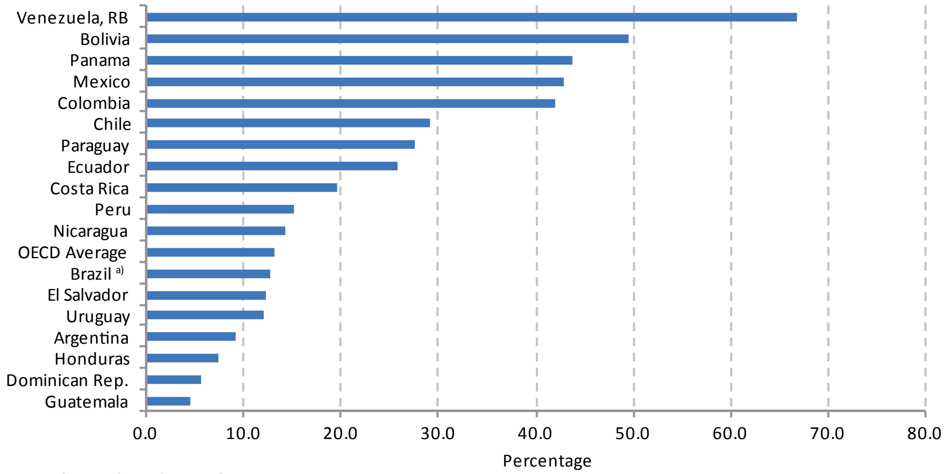
StatLink http://dx.doi.org/10.1787/715235006554

Public finances in the region remain heavily exposed to commodity prices. Structural rules, such as those adopted in Chile, are successful in mitigating this risk

When analysing the resilience of public finances, an important consideration is the degree to which fiscal revenues are linked to commodity prices. As shown in Figure 0.17, on average non-tax revenues – mainly related to commodities in the region – represented around 24.6% of total revenues in 2006, almost twice the OECD average of 13.3%[27]. Of course, there is significant variation between countries in the region. Venezuela and Bolivia are fiscally the most dependent on commodities, a result of their oil and natural gas, respectively. Although commodity prices currently remain relatively high by historical standards, dependence on what has proved to be a volatile source of income continues to be a vulnerability for several economies in the region. The most exposed are those that – in contrast to Chile – have not based their public expenditure programmes around structural rules that take into account the medium-term equilibrium price of the commodities in question.

How has fiscal policy responded in the current crisis? Most industrialised and emerging economies have put in place fiscal packages in the Keynesian mould (personal income tax cuts, reductions in indirect taxes, increased infrastructure spending, and higher transfers to local governments, families and firms), in an attempt to counteract the fall in domestic demand. As noted above, several Latin American economies are facing this crisis with unprecedented fiscal capacity, allowing them to pursue counter-cyclical fiscal policies in a sustainable way. Governments have used this capacity to implement fiscal stimulus packages without undermining the support of the financial markets. The only regret is that their individual actions could have had greater effectiveness had they been better co-ordinated in size and nature.

Figure 0.17. Non-Tax Revenues as a Share of Total Revenues (2006)



Note: *a)* Brazilian data refer to 2005.

Source: OECD (2008*a*).

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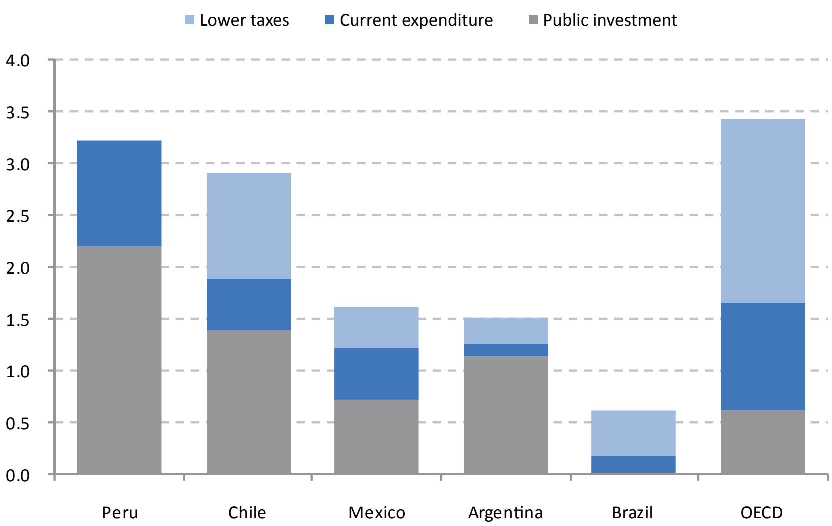
Stimulus packages in the region are smaller than in the typical OECD country, and more heavily weighted to public investment

Governments in the region have announced fiscal stimulus packages ranging in size from around 3% of GDP in Chile and Peru, through 1.5% in Argentina and Mexico to 0.6% in Brazil (see Figure 0.18). In all cases other than Brazil, public investment has been the vehicle of choice. It constitutes 2 percentage points of GDP in Peru, more than 1 percentage point in Chile and Argentina, and more than half a point in Mexico. Chile and Brazil also reduced direct taxation, to the benefit of households (and firms in the case of Chile). A third vehicle, favoured by Peru and Mexico, has been current expenditures, such as monetary transfers to lower-income groups. To put all these figures in context, OECD economies plan to spend an average of 3.4 percentage points of GDP from 2008 to 2010, with tax reductions accounting for 50% of this, current expenditure 30% and infrastructure investment 20%.

Figure 0.18. Fiscal Stimulus in Selected Latin American Countries
(Percentage, GDP points)



Source: OECD (2009), IMF (2009*b*) and national Ministries of Finance (Peru and Chile).

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Access to funding limits the size of fiscal packages. This funding can be internal (coming from stabilisation funds created in good times) or foreign (loans from private markets and multilaterals). In turn, access to funding is largely determined by "fiscal resilience". The three top performers in our fiscal resilience index – Chile, Peru and Mexico – have announced the biggest fiscal stimulus.

Fiscal stimulus packages may boost short-term domestic demand, but their quantitative impact on GDP is extremely difficult to assess. Nevertheless, there is near consensus among economists on some key qualitative assertions. First, the short-run multiplier obtained from increasing fiscal spending is larger than the multiplier obtained from lowering taxes. The reason is that taxpayers may not spend the proceeds from lower taxes, especially during a deep crisis where precautionary savings and deleveraging prevail. The second is that higher infrastructure investment may have the added benefit of promoting long-term growth, but that slow implementation (due to the usual lags in the process, or to bad governance) may defeat the purpose of the stimulus. The third is that – given this uncertainty – the best policy is to diversify the mechanisms used to stimulate the economy. And last but not least, credibility and a clear exit strategy are fundamental for the stimulus to have the intended impact, and, more importantly, to not compromise long-term development. On these measures, the fiscal responses of Chile, Mexico and Peru seem best structured[28].

Monetary Policy Resilience

A country's room to use monetary policy is measured by its Monetary Resilience Index, which is constructed in the same vein as the FRI.

Monetary policy resilience reflects a combination of central bank credibility, the availability of reserves and practical exchange rate freedom

The first sub-index, and a crucial factor, is the credibility of the central bank in keeping inflation at low and predictable levels. This depends on both formal and informal institutional arrangements (such as legal *and* financial central bank independence) which avoid fiscal dominance – and the monetisation of fiscal deficits – and set appropriate objectives and incentives for central bankers. We have measured the credibility of a central bank by its ability to keep inflation at single-digit levels, so that measured credibility is low if inflation over a four-year period exceeds 10% per annum[29].

A second aspect is the availability of reserves, since these represent a measure of the resources available to shield the financial sector from liquidity problems. This sub-index is measured as the ratio of reserves to GDP relative to the overall maximum across countries and the two periods considered.

Finally, a sub-index of exchange-rate flexibility captures policy constraints arising from legal or practical needs to manage the exchange rate (see Calvo and Reinhart, 2002). For example, a country with no formal commitment with respect to the exchange rate but a highly dollarised financial system may find in practice that large exchange rate fluctuations would generate unacceptable transfers between debtors and creditors in the economy. Such a country – unable to let a flexible exchange rate act as a shock absorber for the external account – could not set its monetary policy by reference only to the domestic equilibrium. Our exchange rate flexibility sub-index is defined as the ratio of the variance of the rate of change in the nominal exchange rate against the US dollar and the sum of the variances of the change in international reserves and the domestic nominal interest rate (Calvo and Reinhart, 2002). These variance ratios are then rescaled by the observed overall maximum (here Chile in 2008).

The resulting compound MRI is presented in Figure 0.19 on the next page.

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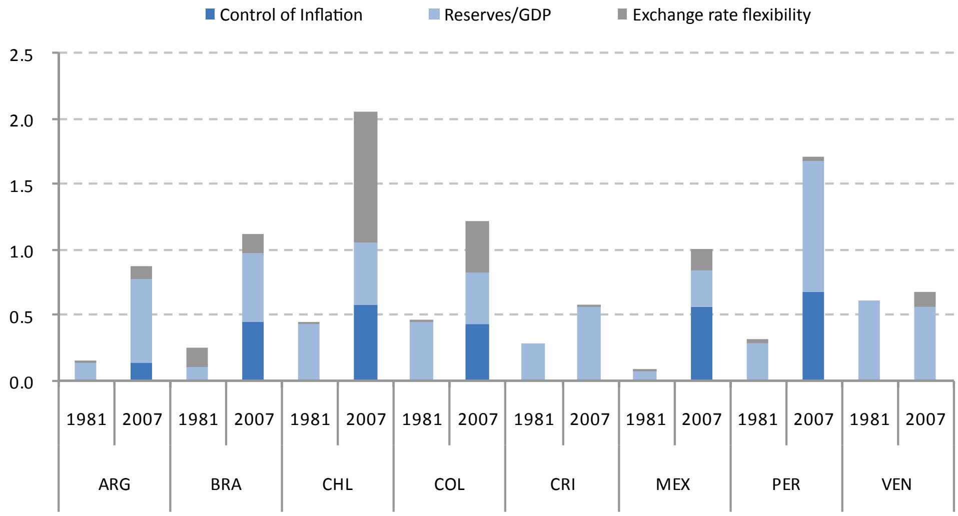
Figure 0.19. Monetary Resilience Index



Notes: Each indicator is ranked between 0 and 1, with higher values indicating a larger resilience. See text for details on the construction.

Source: OECD Development Centre calculations based on the World Bank GDF and WDI databases, ECLAC Economic Indicators and Statistics database (*BADECON*), the IMF IFS database, Institutional Investor and Datastream database.

StatLink http://dx.doi.org/10.1787/715317323337

As shown in the figure, all countries in the region for which data are available show more resilience in 2007 than in 1981. As for fiscal policy there is significant variation across countries. Chile and to a lesser extent Peru are clearly the most resilient countries from a monetary policy perspective. Both have been able to tame inflation and have greatly strengthened their reserves. However, Chile has been able to allow for greater exchange-rate flexibility. Peru, with less progress on this heading, partially compensates by holding more reserves. These differences reflect primarily the different degree of "dollarisation" of the two economies: loans denominated in foreign currency account for 56% of total bank credit in Peru, but only 9% in Chile.

Monetary policy headroom seems to be closely associated with the adoption of inflation-targeting regimes

It is interesting to note that the countries which appear to have most room for monetary-policy manoeuvre are precisely those that have adopted an inflation-targeting regime (Brazil, Chile, Colombia, Mexico and Peru). While the current crisis is possibly the first serious test of this monetary regime, it seems that inflation-targeting countries in the region are overall in a better position to conduct monetary policy in a credible and sustainable way. It is also interesting to observe the strong rank correlation between the MRI and the FRI of 0.93. Thus, resilience on the monetary front seems to go hand-in-hand with fiscal resilience.

Inflation-targeting countries in the region have been loosening monetary policy since early 2009 by reducing policy interest rates, as inflationary pressures have mitigated. Chile has been the most aggressive, reducing its policy rate from 8.25% in December 2008 to 1.92% by April 2009, while Brazil has reduced its SELIC policy rate to 8.75% as of July 2009 – a level not seen since the 1960s. Countries still have considerable theoretical scope for further cuts before they hit the limit of zero nominal interest rates, though are likely to be constrained in practice by the need to maintain anti-inflationary credibility before this level is reached.

What Does It Mean? – Exposure, Resilience and Outcomes

The premise of the analysis in this chapter is that the final effect of the present crisis for a given country will depend both on its exposure to shocks and its resilience to them, including its ability to implement effective and sustainable policies to mitigate their effects.

In order to assess the relative importance of these two factors we now look at how each of exposure and resilience influence the cyclical costs of the crisis on the one hand, and its effect on long-term potential growth on the other. For the former the reduction in the consensus growth forecasts for 2009-10 since the bankruptcy of Lehman Brothers (as defined at the start of this chapter) is used. To measure the effect on potential growth, the IMF's growth forecasts for 2011-14 (drawn from the *World Economic Outlook*, July 2009) are used. The two exposure indices (current-account and financial-exposure) calculated above are added to produce a single "Total Exposure Index" (TEI). In the same way, the range of resilience indices (real, financial, fiscal policy and monetary policy) are aggregated into a Total Resilience Index (TRI).

Greater exposure does not imply greater suffering; if anything the reverse is true...

Figure 0.20 demonstrates that exposure measured by the TEI is positively correlated with long-term growth potential – the medium- and long-term benefits of globalisation – while there is no significant correlation between exposure and cyclical costs. If anything, more exposed countries in the region are expected to suffer less in the short-term than countries that are more isolated. (The notable exception is Mexico with its particularly deep interconnections with a battered US economy.) This suggests there is a powerful argument against trying to mitigate the effects of the current crisis by using financial and trade controls. There is no evidence of a trade-off, for the countries analysed here, between short-term gains and the long-term costs of these policies.

...but greater resilience is indeed associated with better expected performance

Figure 0.20 also shows that countries resilient on the TRI measure are indeed expected to withstand the crisis better. Policies that have created fiscal and monetary policy capacity, as well as structural reforms developed better to absorb external shocks, are paying off in the current circumstances. Moreover – as economic theory would predict – this resilience is also positively correlated with medium- to long-term growth.

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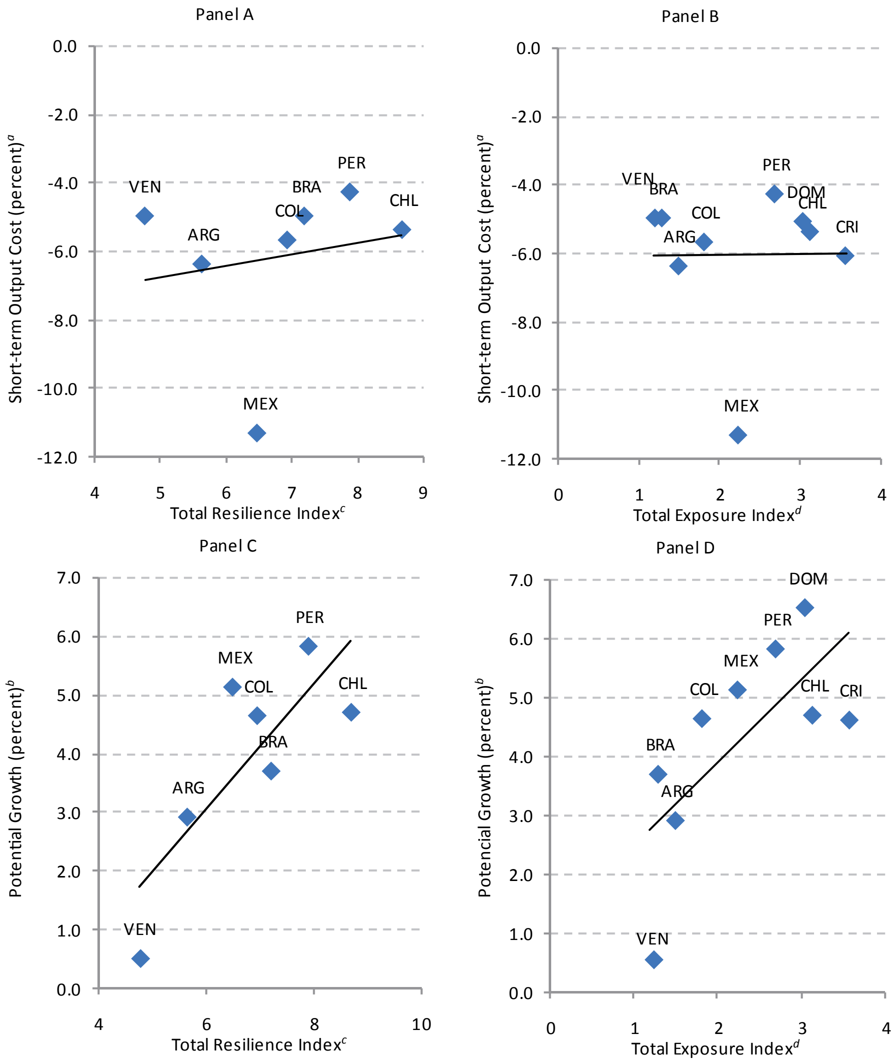
Figure 0.20. Correlations between Exposure, Resilience and Outcomes



Notes:

a) Percentage-point change between real GDP growth forecasts as of June 2008 and June 2009.

b) Potential growth is estimated as the average projected real GDP growth rate by the IMF WEO database, April 2009, for 2011-14.

c) The index is the sum of the Trade Resilience, External Financial Resilience, Fiscal Resilience and Monetary Resilience Indices.

d) The index results from the sum of the Current Account and Financial Exposure Indices.

Source: OECD Development Centre calculations based on OECD (*2008b+,* 2009), Consensus Forecasts (2009) IMF WEO and World Bank WDI database.

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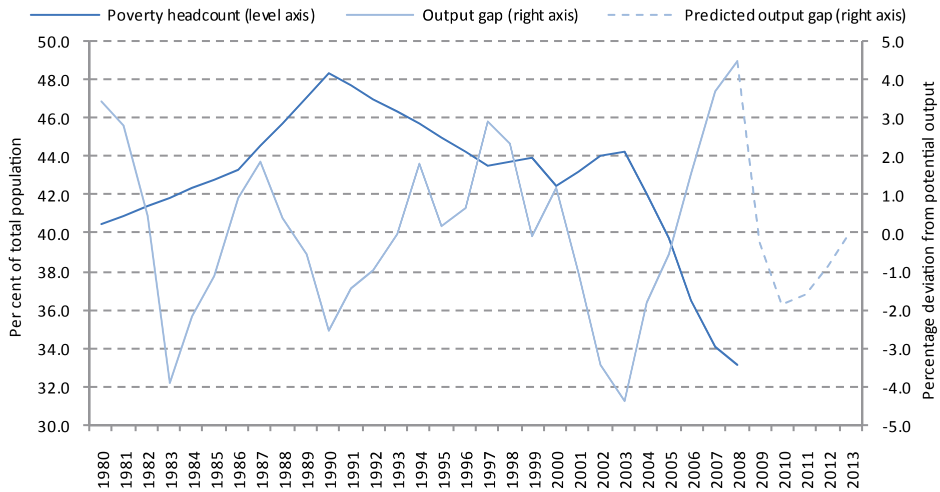
DEVELOPMENT IMPACT OF THE CRISIS

The five years 2004-08 brought Latin America the highest rates of growth in per capita income for at least 50 years. This impressive performance – particularly when set against the region's rather lacklustre track-record – brought with it the unprecedented reduction in poverty rates shown in Figure 0.21, and a significant decline in inequality in most countries[30]. While all countries in the region still face high levels of inequality, low social mobility, social exclusion and poverty, there has been significant progress.

Figure 0.21. Poverty and the Business Cycle in Latin America



Source: OECD Development Centre calculations based on ECLAC Social Indicators and Statistics database *(BADEINSO)* and the IMF WEO (April 2009) database.

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A strategy to mitigate the poverty effect of the crisis must first ask how much of the recent reduction was cyclical

The dramatic change in the economic outlook raises two important questions for policy makers in the region. First, how much of the recent achievement in poverty reduction was merely due to the somewhat exceptional boom (and so will revert in the near future) and how much is attributable to structural changes in the economy and successful public policies. Second, how to identify the likely impact of the crisis and so design sustainable policies to mitigate its effects in the short term, particularly for the most vulnerable citizens, and protect long-term investments, such as in health and human capital. The remainder of this chapter considers both.

Assessing the Impact on Poverty

One of the main risks of the current crisis is an increase in poverty. The actual and forecast falls in growth and the corresponding increase in slack capacity will lead towards higher levels of unemployment. Given the lack of a comprehensive system of social safety nets and the meagre assets held by most families, poverty rates could easily revert from their extraordinary decline of 2003-08 and rise quickly in several countries in the region. In many cases this would compound the effects of the increase of 2008 in the relative price of foodstuffs (which pushed up poverty rates despite the then rapid GDP growth), especially in Central America and the Caribbean.

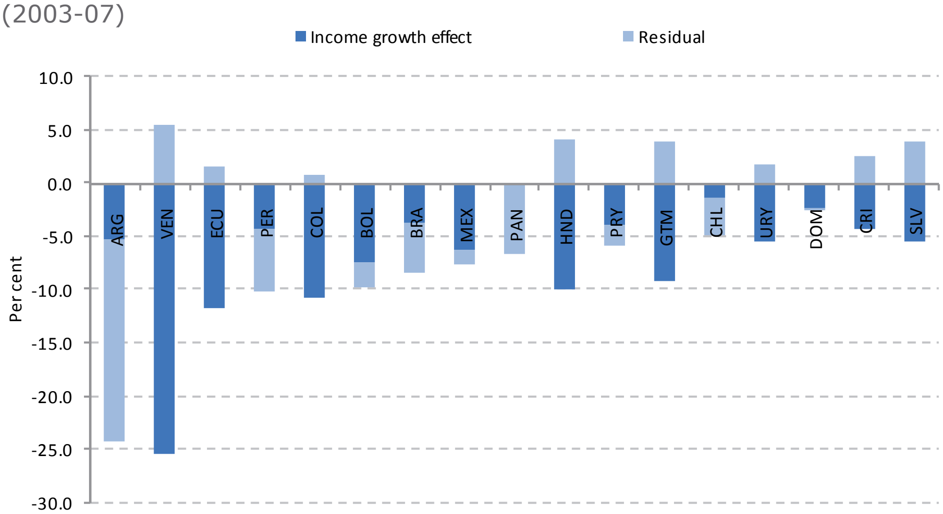
Poverty rates are negatively correlated with the business cycle and the current crisis could translate into an increase in poverty of 7 percentage points

There is a significantly negative correlation between the business cycle and poverty rates in the region (see Figure 0.21), suggesting that potentially part of the impressive decline in poverty rates in the last five years might be a cyclical phenomenon[31]. Combining the poverty-growth elasticity of 3 with the latest

IMF forecasts (showing a decline of 3.6% in real GDP per capita in the region in 2009 and only a 1.3% increase in 2010), poverty could increase by almost 7 percentage points[32]. This estimate would translate into almost 39 million people in the region newly falling below national poverty lines, reversing almost entirely the progress made during the 2003-07 period. Now, this is clearly a back-of-the-envelope estimate. In particular, caution is needed because growth-elasticity in Latin America is historically lower, and the average elasticity hides large disparities across countries (Ravallion, 2001). This effect may be linked to the region's high income inequalities and their effect on the growth-elasticity of poverty (Bourguignon, 2003).

To explore this linkage further, Figure 0.22 presents the counterfactual reduction in poverty headcount ratio that would have been observed in each country had no changes in the distribution of income taken place, under the assumption that the elasticity of poverty reduction depends on the initial level of income inequality (Ravallion, 2005). The figure also analyses the reduction in poverty headcount into this income-growth effect and the residual. Overall, the average decline in poverty of around 8.2 percentage points in the region during 2003-07 is explained as to 85% by growth in income per capita. This would imply that potentially a large part of the decline in poverty observed in the region is at risk of being reversed in coming years if the global crisis reduces per capita income growth significantly. However, there is considerable heterogeneity across countries: in Argentina, for example, despite strong income per capita growth, only 20% of the decline in poverty is explained by that growth, while in other countries including Colombia, Ecuador, Uruguay and Venezuela, income growth explains 100% or more of the decline in poverty rates.

Figure 0.22. Analysis of Reduction in Poverty Headcount Ratio
(2003-07)



Source: OECD Development Centre calculations based on SEDLAC database, ECLAC Social Indicators and Statistics database (BADEINSO) and World Bank WDI database.

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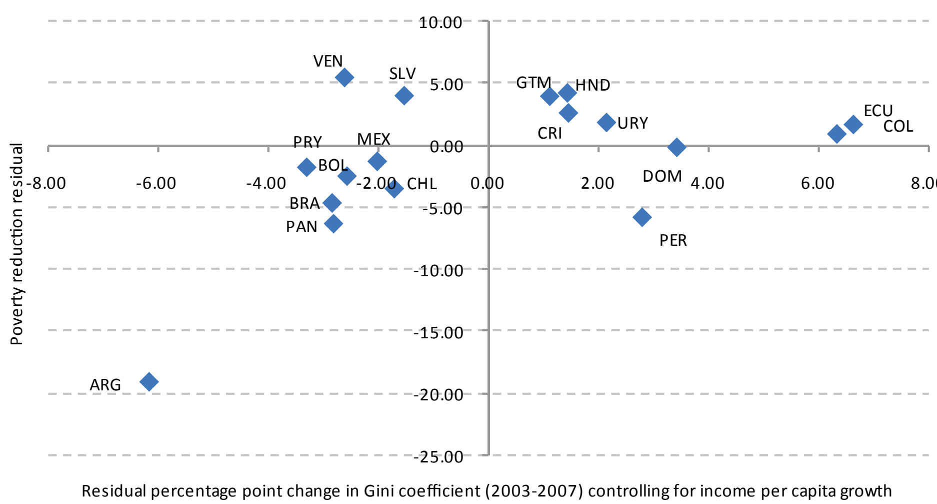
What explains these differences across countries in the region? A possible answer is provided by Figure 0.23 which plots the residual – that is the part of the change in poverty that is not explained by income per capita growth – against the change in income distribution during the period, measured by the Gini coefficient controlled for income per capita growth. There is a positive and significant correlation (the simple correlation coefficient is 0.5) between these variables, such that countries with large declines in poverty unexplained by income growth also have a large decline in income inequality[33]. Strongly in Argentina and to some extent in Panama, Brazil, Paraguay, Bolivia, Chile and Mexico poverty reduction has been associated with changes in the distribution of income.

Should the underlying policies that supported this redistribution be sustainable in a less favourable international environment, it could be argued that these changes would be relatively immune to changes in income growth, given the relative lack of sensitivity of income distribution to economic growth found in the (global) literature. Significant policy reforms, such as the recent pension reform in Chile (see Box 0.2 on page 57) are well founded and should not be reversed by any cycle. However, crises in the region have in practice generally been also accompanied by an increase in income inequality (Lustig, 2000). In particular, she finds that in 15 out of 20 crises in the region the Gini coefficient increases in the aftermath of the crisis, rising on average by 2 percentage points. Thus, if the impact of the current crisis is similar in magnitude, it would on average reverse the entire fall in income inequality[34].

Policies to reduce income inequality have been effective in reducing poverty, but may come under strain in the crisis

Furthermore, the sustainability of the policies in several countries (particularly Argentina and Venezuela) that have allowed for the relatively large transfers behind reduced income inequality seems precarious[35]. The governments in these countries have as a result enjoyed popular support despite controversial economic policies. However, as noted earlier in this chapter, lower revenues (largely as a result of lower commodity prices) mean reduced capacity to use fiscal and monetary policies in a counter-cyclical way and will make it difficult to sustain the transfers and implicit as well as explicit subsidies that underpin these policies[36].

Figure 0.23. Poverty Reduction Not Explained by Income Growth and Changes In Inequality



Source: OECD Development Centre calculations based on SEDLAC database, ECLAC Social Indicators and Statistics database *(BADEINSO)* and World Bank WDI database.

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DEVELOPMENT PRIORITIES IN THE CRISIS

As already noted, lower growth, lower commodity prices and reduced access to international capital markets will have a significant effect on the resources available to governments in the region. While many governments face the global crisis with a more solid fiscal position than during previous episodes of economic distress, they still will be confronted with important dilemmas regarding which programmes to maintain, prioritise or reduce.

Historically public expenditure in the region has tended to be pro-cyclical

Overall, social expenditures have shown historically a similar cyclical pattern as other fiscal aggregates[37]. Spending tends to rise above trend during economic expansions and contract pro-cyclically during recessions (see Table 0.1). Thus, not only are social expenditures and safety nets in most countries of the region low compared to most OECD countries, but they are also pro-cyclical. Combined with very limited household access to financial services and insurance instruments, by historical standards there is little evidence for being optimistic.

Table 0.1. Cyclical Correlations between Social Expenditures and GDP

Country	Education	Health	Social security	Housing	Total social spending
Argentina	0.81	0.86	0.89	0.79	0.87
Bolivia	-0.12	0.04	0.35	0.08	0.19
Brazil	0.50	0.61	0.29	-0.30	0.56
Chile	-0.08	0.39	-0.11	0.23	-0.04
Colombia	0.40	0.64	0.72	0.07	0.74
Costa Rica	-0.11	-0.06	0.33	-0.15	0.08
Dominican Republic	0.79	0.68	0.12	0.04	0.70
Ecuador	0.54	0.35	0.54	0.39	0.59
El Salvador	0.01	0.30	0.17	0.06	0.14
Guatemala	0.20	0.24	-0.04	0.35	0.35
Honduras	-0.27	-0.33	0.44	-0.31	-0.31
Jamaica	-0.36	0.13	0.27	0.37	-0.04
Mexico	0.36	0.58	-0.16	0.21	0.64
Nicaragua	0.11	0.05	n/a	-0.17	-0.01
Panama	0.76	0.32	-0.16	0.26	0.50
Paraguay	0.43	0.35	0.24	0.04	0.38
Peru	0.54	0.77	0.24	0.69	0.58
Trinidad and Tobago	0.29	0.19	0.29	-0.20	0.27
Uruguay	0.62	0.66	0.81	0.66	0.84
Venezuela	0.38	0.39	0.30	0.45	0.51
Average	**0.29**	**0.36**	**0.29**	**0.18**	**0.38**
Median	**0.37**	**0.35**	**0.29**	**0.14**	**0.44**

Note: All amounts are HP-filtered constant price series in logarithms.

Source: OECD Development Centre calculations based on ECLAC Social Indicators and Statistics database (*BADEINSO*).

StatLink http://dx.doi.org/10.1787/717261157332

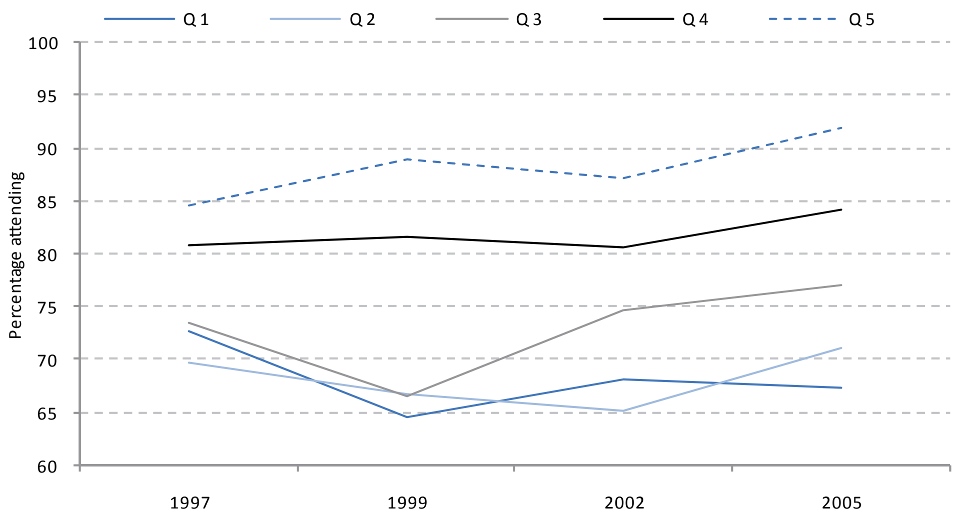
From a long-term development perspective it is important to avoid disrupting those investments that promote social mobility and allow citizens to move out of poverty, such as nutrition, health and education. Public support in these areas is very important, because vulnerable households do not have the means to self-insure against the consequences of the crisis at adequate levels. Crises in the region have historically had a negative impact on educational and health outcomes, inducing possibly permanent losses in the human capital of the poor (Lustig, 2000).

The effects of macroeconomic shocks on the poor can be severe and can have very long-term consequences

For example, in Brazil unemployment shocks at the household level increase the probability of child labour, missed education and school failure – as much as a 50% increase in probability for 16-year-old girls, for example (Duryea *et al.*, 2007). The results suggest that some households are not able to absorb short-term economic shocks, and this has negative consequences for children. However, this pattern was not seen in Argentina during the crisis of 2001-02 (López Boo, 2008). The probable reason for the difference lies in the nature and size of the underlying shock. In an episode of the scale of the Argentinian crisis, lower wages and higher unemployment create the same incentives for poor families to rely on child labour as a survival strategy. But at the same time, macroeconomic shocks reduce employment opportunities for children, and the final outcome depends on the relative strength of these pull and push factors. Furthermore, informal social insurance and risk-sharing arrangements often used to overcome individual shocks become ineffective against the general shocks of a more widespread crisis. Similar pro-cyclicality is seen in child health outcomes in Latin America, though the evidence in education is less conclusive (Ferreira and Schady, 2008).

A further example of the vulnerability of poor households to macroeconomic shocks is presented in Figure 0.24. In 1999 Ecuador suffered a severe economic and financial crisis, with GDP falling by 6.3%. The effect of this crisis on school attendance for children in secondary education varied significantly across income quintiles. As the figure shows, for the richest two quintiles there was actually a slight increase in school attendance, while the poorest three quintiles all suffered a significant decline – more than 8 percentage points in the case of the poorest. Furthermore, while for the middle-income quintile the effect of the crisis was short-lived, for the poorest sectors of society school attendance was still significantly below pre-crisis levels six years later. The secondary effects of these immediate impacts threaten to be even more lasting, tending as they do to widen income inequality with all what that implies for social mobility and inclusion.

Figure 0.24. School Attendance in Ecuador for 13-19 Year-Old Cohorts by Income Quintiles



Source: ECLAC Social Indicators and Statistics database *(BADEINSO)*.

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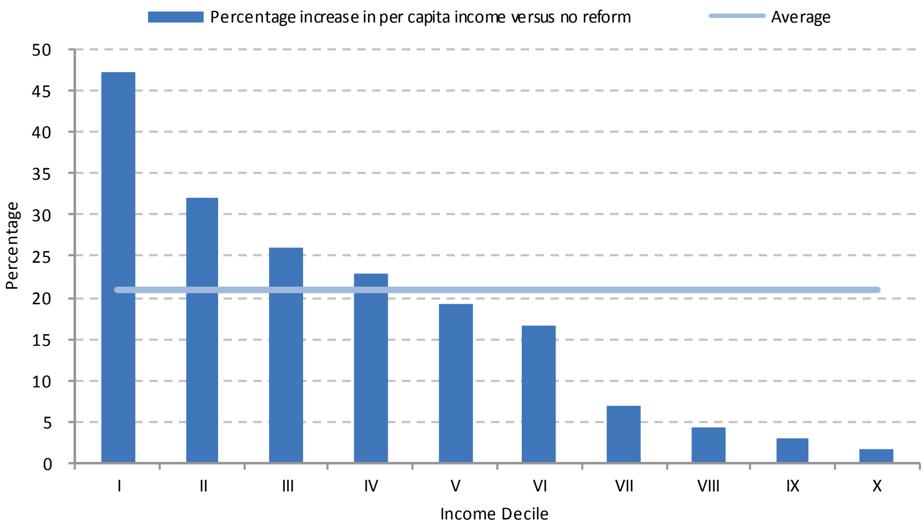
Box 0.2. The Enhanced Solidarity Pension System in Chile: A Response for the Crisis – and Beyond

Extending social safety nets, for example through greater coverage or the introduction of a minimum pension scheme, can provide an effective tool to mitigate the economic effects of the current crisis for some of the most vulnerable segments of society. Any such proposals must, of course, be financially sound and sustainable in the long term. The Chilean experience offers an interesting case study in the region.

Figure 0.25. Impact of the New Pension Solidarity Pillar in Chile



Source: Huepe (2008).

StatLink http://dx.doi.org/10.1787/715463266854

One of the milestones of Bachelet`s presidency is pension reform. More than 25 years after the last reform, with accumulated savings in mandatory pension funds reaching 60% of GDP, and just as the first scheme members under the existing rules began to approach retirement age, a lively debate on the future shape of pension provision in Chile got underway. In 2006 the new Chilean government appointed an advisory council (*Consejo Asesor Presidencial para la Reforma Previsional*) to propose changes, while preserving the central components of the existing system. The council was plural in composition (members were mostly specialists from academia), and their consultation drew in union leaders, industry representatives, and national and international academics. Based on this transparent process (see Rofman *et al.*, 2009, for an analysis of its strengths and a comparison with the Argentinian reform), the council produced a comprehensive report, which became the basis for legal reforms enacted in early 2008 (*ley 20.255*).

The report concluded that the system was sound but required upgrades. The most pressing problems to be addressed were broadening coverage of minimum pensions, increasing gender equality, improving competition to reduce costs, and creating a better framework for investment. Strengthening the minimum pensions` pillar was considered the priority. Berstein *et al.* (2005) had projected that 55% of scheme members would accrue pension rights below the minimum, and among them, only one-tenth would qualify for the contributory minimum pension. This was mostly as a result of the interaction between labour informality which, though low by regional standards, was still significant at around 30% of the workforce, and the relatively strict eligibility criteria (20 years of contributions were required for the contributory minimum pension), together with the scheme's voluntary status for independent workers.

The government chose to pursue a very ambitious reform, establishing a new redistributive pillar, the *Sistema de Pensiones Solidarias* (SPS). The SPS will cover both old-age (over 65 years) and disability pensions for those with incomes in the lowest 60% of the population (rising from 40% in 2008). The minimum benefit, known as the *Pensión Básica Solidaria* (PBS), is set by law and provides CLP 75 000 a month in 2009 (around EUR 100) to those with no contributions to the pension system. For those with some contributions, the *Aporte Previsional Solidario* (APS) provides a complementary benefit which tapers according to the size of the self-financed pension, reaching zero from a limit known as the *Pensión Máxima con Aporte Solidario*, set at CLP 255 000 (around EUR 340) per month in 2012[38].

The effects of the reform will be wide-reaching. According to official estimates (Arenas *et al*., 2008), the system will benefit nearly one million Chileans almost immediately (2009-10), and 1.6 million by 2020. This is three times the beneficiaries of the previous solidarity pillar, which combined a non-contributory benefit (*Pasis*), with Minimum Pension Guarantee for those who contributed for at least 20 years.

The new system will also have significant redistributive impacts. Preliminary estimates by Huepe (2008) show that the impact of the reform on per capita income is significantly positive for low-income deciles, while the income of the upper four deciles is not particularly affected (see Figure 0.25). The effect is to reduce inequality among older Chileans significantly (the Gini coefficient of per capita income for those in the over-65 age group falling from 0.49 to 0.44) and poverty on a national basis by 2 percentage points.

Obviously, these benefits do not come without cost. Arenas *et al.* (2008), from the Chilean Budget Office, estimate that related expenditure will rise to 1.2% of GDP in 2025 (from 0.5% in 2009), and ultimately mean a permanent increase of 1 percentage point in government expenditure as a proportion of GDP. Melguizo *et al.* (2009) project a higher net short-term cost, but lower over the long term (relevant expenditure reaching between 0.8% and 0.9% of GDP in 2010, and peaking at 1% in 2016). Though significant, these fiscal costs seem manageable; particularly given the accompanying reduction in the unfunded liabilities in the economy that would otherwise arise from the ageing profile of the country (see Zviniene and Packard, 2004). These savings are apparent even in the short and medium term. According to the same projections, in absence of the structural reform, the unfunded pension liability in 2010 would have been 150% of Chilean GDP against 25% post-reform.

Overall, the reform greatly improves the social protection network in Chile, achieving full coverage for poor middle-income workers. The fiscal cost is not negligible, but from a social and a financial sustainability perspective, the Chilean reform is a sensible step forward. It is affordable thanks to good fiscal and labour-market institutions and rules. And the reform demonstrates that responses to the crisis can be effective in the short term and still be compatible with long-term sustainable goals.

POLICY OPTIONS IN THE FACE OF THE CRISIS

Latin America faces a different type of shock from that faced by the OECD countries. It will require its own solutions

When considering fiscal and monetary policy options it is important to bear in mind that the nature of the current shock faced by Latin America is qualitatively different from that experienced by most OECD countries. The shock originated in the OECD economies as a financial crisis that has undermined banks' balance sheets and their lending capacity, and gone on to produce a collapse of domestic aggregate demand in most countries. In contrast, countries in Latin America

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suffer the crisis as a mainly exogenous external shock affecting external demand and commodity prices, and potentially external financing. This difference is important because while in OECD countries policies can directly address the sources of economic weakness, the application of those same policies in Latin America would presuppose a potentially major shift towards domestic demand. This rebalancing would require productive factors to migrate across sectors, and could trigger a sizeable current account deficit (via imports of capital and intermediate goods) which could be problematic for some countries in the region. Therefore, although countries in the region may have the capacity to use fiscal and monetary policy to stimulate aggregate demand, the effectiveness of these policies may be questioned.

Despite this, for those that have the fiscal and/or monetary capacity, the use of *sustainable* counter-cyclical policies can be an effective tool in mitigating some of the potentially more harmful long-term effects of a recession. This is particularly the case where programmes can be directed towards the most vulnerable households. In principle, this also allows for a larger multiplier effect since cash would flow towards households that will tend to spend it[39]. The caveat is the importance of designing such programmes so that their temporary nature is embedded, in order to avoid the creation of higher permanent entitlements not matched by a corresponding permanent increase in financial resources. While it may be tempting to see the current situation as an opportunity for structural reforms such as building social safety nets and associated automatic fiscal stabilisers, the need for quick action should not obscure the complex development issues, such as informality and the tax system, that underlie such reforms.

The region has greater capacity than ever before to pursue counter-cyclical policies in a sustainable and co-ordinated way. Policies should target the poor, who are at greatest risk of long-term harm from the downturn

Infrastructure investment presents another opportunity, and can be mobilised relatively rapidly by executing projects already planned and evaluated or updating existing infrastructure. Such investments directly create employment, and also strengthen public infrastructure in ways which may allow enterprises to increase their efficiency and competitiveness, so – almost literally –"laying the foundations" for the next expansion once the world economy recovers. In the absence of large social-safety nets, maintaining employment levels in the most productive way can be an effective tool to fight cyclical poverty.

Some countries in the region find themselves much more constrained in the conduct of aggregate fiscal expansions or counter-cyclical monetary policies than their inflation-targeting neighbours. For them, it will be important to prioritise policies that protect human capital, the destruction of which would jeopardise both the social advances of recent years and do long-term damage to the growth and development outlook. This implies governments redirecting expenditure towards the health, nutrition and education of their most vulnerable citizens, especially children. Particularly in those countries that suffer institutional limitations there is an important role for bilateral donors and international financial organisations in providing not only funding but also know-how in the design of sustainable and effective programmes.

NOTES

1. This graph shows the evolution of real GDP per capita of the typical Latin American country, defined as the simple average for the region, in the aftermath of the crisis under alternative counterfactual evolutions of total factor productivity (TFP) and productive factors. The Latin American and Caribbean countries examined are Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, the Dominican Republic, Ecuador, El Salvador, Honduras, Jamaica, Mexico, Nicaragua, Panama, Paraguay, Peru, Uruguay and Venezuela. TFP series are Hodrick-Prescott filtered trends used to isolate cyclical fluctuations from the long-term analysis. See Blyde *et al.* (2009) for more details on the data and sources.
2. The IMF WEO update of 8 July 2009 shows a similar picture for the region with a contraction in GDP of 2.6% in 2009 and a rebound of 2.3% in 2010. Given population growth of around 1.2% per annum in the region, these forecasts are very similar to those reported above.
3. The exception is Mexico with OECD projections (as of June 2009) pointing towards a sharp decline of 8% in 2009, and only a modest rebound of 2.8% in 2010.
4. This interpretation is in line with the emphasis on institutional factors as a major determinant of income per capita dispersion in the literature (see, for example, Acemoglu *et al*., 2001 and Hall and Jones, 1999).
5. See Berg *et al.* (2008).
6. The national Case-Shiller index, which measures constant-quality house prices in the United States, fell in the third quarter of 2006 after 15 years of uninterrupted increases.
7. Argentina's 2008 dollar GDP remains below its pre-2002 crisis level. For this reason, instead of 2008 we analyse the decade ending 2001.
8. Measurement of remittances is far less reliable than measurement of other current account flows. As will be discussed in Chapter 2, increased observed flows may be simply a consequence of the formalisation of previously informal flows.
9. Sudden stops are defined as "sharp contractions of international flows" (see for example Calvo *et al*., 2004). Current account reversals are "episodes in which the current account strengthens sharply, generally moving from deficit to surplus, in three or fewer years." (Adalet and Eichengreen, 2005).
10. Of course, it could be argued that diversification is of limited value in the presence of a synchronised aggregate shock that has the same impact across destinations. However, even the current crisis cannot be classified as such, given the different impacts it is having across the world.
11. Bundled together are Africa, Australia, rest of Asia and Russia.
12. The indicator used is the first principal component across countries and it is normalised to have mean 0 and standard deviation 1. Higher values represent fewer restrictions, that is greater financial openness.
13. The report does not include corresponding information for Mexico, the third G20 member from the region.
14. Short-term refers to debts that are due within a year. External debt includes private and public obligations.
15. See Jeanne and Rancière (2009) for a more detailed approach to the optimal level of reserves in emerging markets.
16. Therefore, the index is constructed as min (2, Reserves/ShortTermDebt)/2.
17. See Calvo (1988) and Blanchard and Missale (1994) for theoretical arguments on how short-term debt structures and other forms of risky debt composition are an incentive to reduce moral hazard problems. Broner *et al.* (2003) focus on the supply side of credit and the importance of fluctuations in investors' risk aversion in understanding emerging market debt maturity.

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18. Debt-to-GDP ratios (D/GDP) are adjusted by the exchange rate misalignment (ten-year rolling real exchange rates) and by the output gap (using Hodrick-Prescott filtered real GDP over forecast-extended series from the IMF April 2009 WEO database).
19. A similar conclusion is reached if we compare the current situation to the mid-1990s.
20. On average, the ratio of provisions to nonperforming loans is 161% as of 2008. Among OECD countries the decline in this indicator has been particularly large in the United States, reflecting the magnitude of the financial crisis in this country.
21. Given that EMBI spreads are not available prior to 1993 in order to compare with the 1980s, we extrapolated the spreads based on a panel regression for 33 countries that includes fixed country effects and time effects of the spreads on the *Institutional Investor* rating that have been used extensively in the literature to capture default risk (see for example Reinhart *et al*., 2003). The simple correlation coefficient between spreads (in logs) and the IIR index is 0.85 and significant at conventional levels.
22. This maximum is Brazil in 1982 with an external debt of 306.6% of exports. The index is then computed as 1- (DebtToExports/306.6).
23. In particular, the financing-costs capacity is computed as max (0*,* 1- Spread/500).
24. Thus, we compute the indicator as (GovBudgetBalance - MinBal)/(MaxBal – MinBal), where MaxBal and MinBal are respectively the highest and lowest observed values.
25. Moody's upgraded Chile's foreign-currency sovereign debt from A2 to A1 in March 2009.
26. Sovereign debt ratings for Spain, Greece, Ireland and Portugal were revised downwards in early 2009.
27. In fact, given that in many countries in the region taxation on corporate profits or income related to the extraction and production of commodities is an important source of revenues, the figures presented here represent a lower bound of the fiscal importance of commodities.
28. These criteria follow Spilimbergo *et al.* (2008), who extended the standard "3Ts approach" (that is, fiscal stimulus should be "timely, temporary and targeted") to "timely, large, lasting, diversified, contingent, collective and sustainable".
29. Similarly to the FRI indicators, we measure ControlOfInflation as max (0, 1 - InflationPerAnnum /10).
30. The business cycle is estimated using the Hodrick-Prescott filter on the aggregate real GDP series from the IMF WEO database (April 2009). In order reduce the influence of the endpoint, we use the forecast extended series until 2014, provided by the IMF, to compute the cycle, as recommended by Maravall and Kaiser (1999). Poverty data are headcount poverty using national poverty lines. For 2008, the poverty headcount rates are projections by ECLAC.
31. Thus, poverty increases during recessions and decreases during more benign times. This is reflected by a correlation coefficient between poverty in the region and the output gap (measured as the deviation from logarithmic HP-filtered real GDP) of -0.63, while using real GDP growth rate it amounts to -0.54.
32. This is the estimated effect reported by Ravallion and Chen (1997).
33. Even if Argentina and Venezuela are excluded the correlation is 0.53 and remains statistically significant.
34. See also Baldacci *et al.* (2002) for mixed cross-country evidence on the impact of financial crises on inequality and microeconomic evidence for the Mexican Tequila crisis.
35. It should also be noted that there is controversy over the way Gini coefficients are computed in Venezuela based on income reported in household surveys, given recent increases in the proportion of missing observations and how households reporting zero income are treated. According to Freije (2009), correcting for these problems would leave income distribution in Venezuela basically unchanged over 2000-05.
36. Implicit subsidies include price controls on energy and transport in the case of Argentina.
37. See the *Latin American Economic Outlook 2009* for a comparative analysis of pro-cyclicality of fiscal policy in Latin America and the OECD.

38. For comparison, the average contributory minimum pension guarantee in December 2008 was some CLP 115 000 per month (slightly over EUR 150), and the non-contributory one around CLP 55 000 (EUR 75). The average monthly wage in Chile is some CLP 350 000 (EUR 470) and the minimum wage CLP 159 000 (EUR 210).

39. This potentially contrasts with several OECD countries where low-income households have access to asset markets and are indebted.

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PART TWO

Migration and Remittances in Latin America

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CHAPTER ONE

Flows of People, Money and Ideas

LATIN AMERICAN MIGRANTS IN THE EYE OF AN ECONOMIC STORM

The task that this year's *Latin American Economic Outlook* has set itself is to make clear the opportunities and risks presented by international migration – in both directions – to the societies of Latin America and the Caribbean. Doing so will identify what is at stake when setting policy for the governance of mobility of people. It will back this up with a review of policy tools and what has been learned from their use. It takes on this topic at a time when migrants increasingly find themselves at the centre of heated global policy debates. The long boom in the world economy has created ideal conditions for migration with labour shortages on the one hand and the promise of a share in new wealth on the other encouraging many to move. Sometimes these flows have been highly visible, sometimes less so. But they now amount to many millions since the world economy last paused.

This much – mass movement of people – has been going on almost since recorded history began. What is new is that at the same time ever cheaper international travel and communications have changed the face of emigration both for the migrant and those left behind. The results are twofold. In countries of destination there are whole new communities of migrants, frequently sharing the cultures of both their home and host countries. And in countries of origin there is much greater awareness of these communities abroad and the day-to-day challenges and opportunities they have found in their new lands.

Migration, even mass migration, is not a new phenomenon but technology is giving it new aspects. Its visibility and scale ensure its political profile

In June 2008 the European Parliament adopted the "Return Directive", an instrument creating tough procedures for the deportation of unauthorised migrants in the European Union to their country of origin[1]. While a major stepping stone toward the development of a Europe-wide migration policy, it was easy to read into the directive's focus on the expulsion of undocumented workers concern about the economic crisis and European leaders' wish to be seen to be addressing rising domestic unemployment levels. This apparent political desire to be seen to be doing something about immigration as a response to the economic crisis was not limited to Europe. In the United States a series of large-scale and high-profile workplace raids were presented as symbols of a renewed zeal with which the authorities would seek to enforce laws against unauthorised migrants[2]. Other OECD countries, including Japan and Australia, likewise sought to moderate immigration flows, or give the impression of a hardened stance toward immigration. At least one such action was directly relevant to Latin America: the attempts by the Japanese authorities to encourage unemployed *Dekaseguis* (Brazilians of Japanese descent who have returned to Japan) to move back to Brazil. Non-OECD countries, too, have acted to restrict inflows or encourage return migration. Notable among these were the Persian Gulf countries, which have been the destination of sizeable labour migration flows from Africa, Asia and the Middle East.

Much of this political action has been in connection with irregular migration – but not all. The United States Congress, for example, prohibited firms receiving funds from the Troubled Asset Relief Program (TARP) from using them to pay the salaries of – entirely regular – H1B visa recipients.

Latin America has never been a bystander to the long-term international mobility of people, and one should not fall into the trap of thinking of it just as an area of emigration. Our improving knowledge of pre-Colombian civilisations increasingly supports the view that mass movements were very much part of the region's story long before a single European foot trod its soil. And thereafter one might argue that Latin America received "illegal immigrants" on a massive scale for centuries beginning with the Spanish in 1492[3]. It is certainly the case – as some Latin American political leaders have recently felt it necessary to point out – that the region received huge waves of European immigrants, chiefly from Spain, Portugal and Italy, during what economic historians Hatton and Williamson (1998) have called the "age of mass migration"[4]. During the century beginning in 1870, for example, Argentina was hugely a net recipient of migrants. Early in the 20th century net immigration inflows exceeded 150 000 people per year, and in many years surpassed 200 000. In the 1914 census, 30% of Argentina's population was foreign-born (Maurizio, 2008). Latin America has moved from being a massive region of destination for migrants to being an important region of origin, while Europe has done the converse.

The gains from migration reform potentially outweigh those from cross-border movement of capital or goods. This is little recognised in political debate on the issue

The anti-migrant actions noted above, and others like them, did not pass unnoticed in Latin America and have frequently provoked strong political reactions, in rhetoric at least. This reaction well illustrates the importance of international migration to economies and politics of the region. It has also served to remind the world migration has an origin as well as a destination – and to point out the asymmetries in the global frameworks for the cross-border movement of people compared with those for goods and capital. This last point is well made. From a purely economic point of view, cross-border movements of goods, capital, and people have very similar characteristics. Putting barriers in the way of a South American worker in Europe is, according to some observers, no different from forbidding European foreign direct investment in South America. Economists have long asserted that the gains to the global economy from easier movement of people would be greater than those from total liberalisation of trade in goods. Yet substantially greater progress has been made in eliminating barriers to trade in goods (and capital) than in promoting international people flows. What explains this discrepancy? The answer is of course the very different politics and political visibility of migration. The present crisis is demonstrably enough to open the debate. May it also provide the momentum for a rational examination of the facts.

WHY DO PEOPLE MIGRATE?

More than 20 million people from Latin America and the Caribbean are international migrants; equivalent to 4 to 5% of the region's population (Chapter 2 will provide further details about who they are and where they go). Worldwide, approximately 3% of the global population, over 190 million people, are migrants (United Nations, 2009).

Why do so many people leave their countries of origin? The classic Harris-Todaro model – developed to explain the phenomenon of rural-to-urban migration within a developing economy – considered the case of the individual migrant, who will move from one labour market to another if he or she expects to earn a higher wage in the new location (Harris and Todaro, 1970; Todaro 1969). This "expected wage" takes into account the probability of finding a job in the destination economy. This may be less than 100% where there is unemployment, but still leave an expectation sufficient to induce the individual to move (and absorb any costs of that move).

This basic economic motive is confirmed by a statistical study by Ortega and Peri (2009) of bilateral migration flows to 14 OECD countries. Not surprisingly, the larger the income differential between two countries (other things being equal), the larger the flow of migrants from the poorer to the richer country: Ortega and Peri estimate that an increase of USD 1 000 in this income difference would raise migration flows by 10%. But economic opportunities alone do not tell the whole story. Policies matter too: in particular, tighter rules of entry also have a large and well-measured negative impact on immigration, or at least on regular migration. The study also found that a substantial amount of the variation in migration levels – some 30 to 40% – was explained by factors exogenous to the country of destination; this underscores the importance of push factors.

Up to 5% of Latin America's population live outside their country of birth. Choice of destination is affected by cultural factors and rules of entry

Docquier *et al.* (2009) also examined the forces behind migration concentration in OECD countries, analysing the results across educational levels. In line with existing literature they found that cultural ties (particularly for former colonies that share a common language with each other and the former colonial power), immigration policies and income prospects significantly affected migration decisions, but also that skills matter. Skilled workers are more responsive to distance and income differences, while unskilled workers are more sensitive to cultural links, welfare programmes and linguistic proximity.

In summary migrants move to take advantage of earning opportunities, can be thwarted by hardening of the immigration regime in their selected destination, and many of the country-to-country differences one observes in migration flows have to do with factors in migrants' home countries. Box 1.1 presents the perception of a group of young Latin American students on these issues.

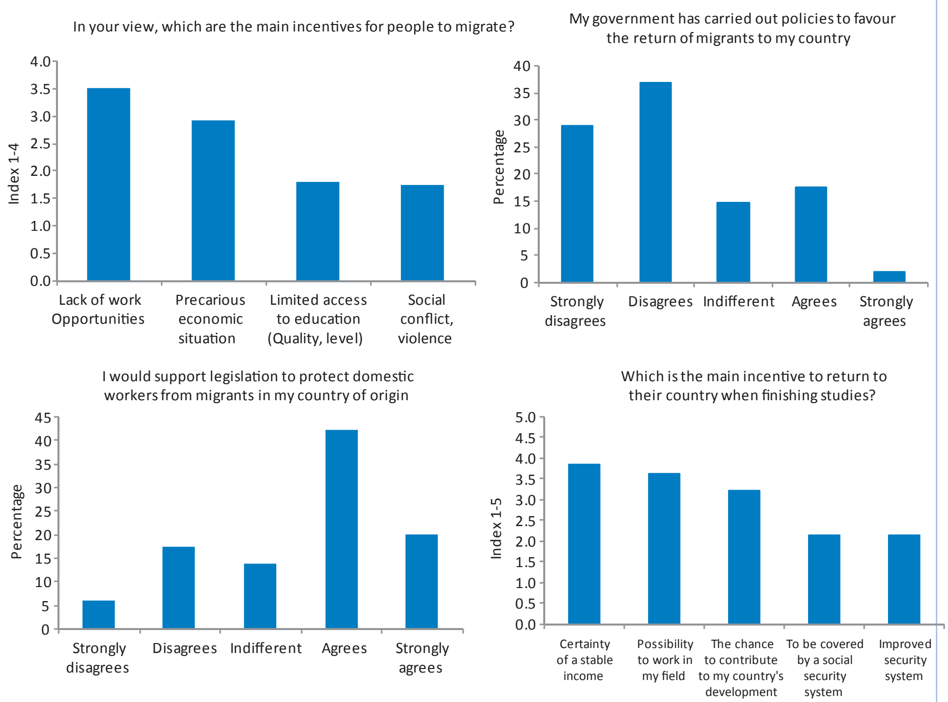
Box 1.1. Vanguardia Latina: Migration from the Perspective of Latin American Youth

Young people are particularly tempted by the possibility of emigration, especially if they are well educated. How do just such a group of young Latin Americans feel about migration? Under what circumstances would they decide to migrate? Are they happy about the migration policies in their countries and in the main countries of destination? How do they perceive those policies? And, if they did go, what would bring them back to their countries of origin?

The basis of our survey was the group of students attending the 2009 meeting of *Vanguardia Latina* – a meeting point for students from Latin and North America to discuss socio-economic issues. As a joint project between the OECD Development Centre, the IDB Youth Programme and the NGO *Espacio de Vinculación*, the survey sought to draw out their point of view on various issues affecting the region. As in previous gatherings, migration proved a central topic of interest, and a broad range of its different dimensions were discussed: the reality of Latin American migrants in the United States, their relationship with the Obama administration, the role of Latin American communities in the media, among others.

The survey revealed a consensus about why many Latin Americans chose to migrate: 64% identified lack of work opportunities as the main factor, followed by the poor economic situation (26%). It is interesting that around 57% of the students believed that their work situation would be substantially better if they were abroad, whereas 23% disagreed with this statement.

Figure 1.1. The Perceptions of Young People in Latin America



Note: For those measures reported as index values, participants were asked to rank the variables in order of importance with 1 being the least important and 4 (or 5) the most important. The index is the average of these responses.
Technical Note: Sample size: 150 students. Type of Survey: Written questionnaire (online). Geographical distribution: Argentina 8, Bolivia 3, Chile 3, Colombia 16, Cuba 1, Dominican Republic 1, Ecuador 2, El Salvador 4, Honduras 4, Mexico 90, Panama 1, Paraguay 3, Peru 8, Uruguay 1, Venezuela 3, other 2. Gender distribution: females 80, males 70. Educational background: undergraduate 123, postgraduate 12, other 15. Age range: Under 20 8, 20-25 107, 26-30 32, 31-35 3. Socio-economic status range: Private school 49, Public-private school 1, Public school 84, other 16.

Source: Survey by OECD Development Centre, IDB Youth and *Espacio de Vinculación* (EVAC).

StatLink http://dx.doi.org/10.1787/715481323824

Financial constraints were seen as the most important barrier to migration (34%), followed by lack of agreements between the sending and receiving countries (29%) and inappropriate integration policies in the receiving country (26%).

Young people in the survey furthermore disapproved of the current migration policies in their countries. Fully two-thirds of them felt that Latin American governments were failing to provide policies to encourage return migration to their countries. Moreover, about half of respondents disagreed with the proposition that immigrants living in their own countries– most of them from other Latin American countries – were well integrated into the host society.

Despite being critical of migration policies abroad, students do not believe that immigrant workers in their own country should be given the same opportunities available to the native born: 62% agree or strongly agree that there is a need for special legislation to protect domestic workers in their own countries of origin.

As for possible emigration destinations, Latin America is not the most attractive destination for potential young migrants: about 55% would definitely not migrate to a Latin American country and only 19% would consider it (26% expressed themselves indifferent).

Again, work opportunities figure in the hypothetical decision to return. Were they to migrate, most students (nearly 70%) would be reluctant to accept a lower quality job in the host country. However, a very similar proportion, around 68%, would be unwilling to accept a similar job in their country of origin, suggesting that for this group at least quality of job opportunities dominates their thinking and trumps issues such as family ties.

Inequality in economic opportunities surely motivates some emigration decisions, and on this issue the surveyed young people are not optimistic. The majority of students reported they are not confident that the region's future will be less unequal, indeed – a shocking – two-thirds of them (66%) consider that in the future their countries will become more unequal.

The survey has provided an interesting window on some of the key issues that young students in Latin America will have in their minds when considering migration. But in many ways it has only scratched the surface of a question that surely deserves better understanding: what are the trade-offs for the rising generation when considering migration?

In assessing the implications of migration today it is important to realise that the term covers a much wider range of activities than just a near-permanent move to the host country – though this is still the image that dominates popular debate on the subject. Migration today takes many forms, including the international movement of students and seasonal migration patterns in agriculture (some stretching back centuries, others of more recent origin) as well as definitive long-term relocation (which may itself be followed by re-migration back home on retirement). Many observers point to increasing periodicity or circularity in migration movements in recent decades. Whether or not circularity in this form is increasing, the social meaning of migration is changing in line with reductions in transport and communication costs. Increasingly migrants and non-migrants alike live in what many social scientists refer to as "transnational spaces". There is no formal definition of this term, but an example (provided by anthropologist Patricia Landolt, 2006) illuminates its meaning: the semi-literate Salvadorian grandmother who has never left her home region but can speak knowledgeably about shops and parks in Los Angeles, who has no fixed-line telephone in her home but speaks daily to her children in the United States on the mobile telephone they have given her, and has strong and informed views on the migration debate in Californian politics.

The "transnational spaces" occupied by many migrants today reflect the complex patterns of migration and return that they experience

Table 1.1 summarises how migration specialists' views on international mobility have evolved over the decades by pulling together the dominant schools of thought on this issue.

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Table 1.1. Changing Schools of Thought on Motives for Migration

School of Thought	Determining Factors of Emigration	Determining Factors of Return and Circular Migration
Neoclassical	Push-Pull: benefits of migrating exceed the costs	Benefits of return exceed the costs
New Economics of Labour Migration (NELM)	Household strategy, relative deprivation	Target-saving, part of household strategy, preference
Structuralist	Personal, social and contextual reasons for migration	Economic and Institutional situation in both sending and receiving countries, but also expectations of the migrant
Transnational/Meso	Movement and livelihood within and between transnational space, migration as a livelihood strategy, social networks	Circular mobility to maintain transnational links, workspace covering more than one country, life-cycle considerations *(e.g.* completion of education, retirement)

Source: Loosely adapted from Ammassari and Black (2001) and De Vreyer *et al.* (2007)

As thinking about migration has developed it has increasingly stressed the importance of non-economic factors

The neoclassical school of thought, based on a simple cost-benefit analysis, is perhaps the simplest and most driven by stark economic logic. The New Economics of Labour Migration (NELM) approach widened the unit of analysis from the individual decision to that of a larger social unit such as the household. Subsequent approaches have given greater prominence to non-economic concerns. Structuralist approaches, for instance, stress the importance of the migrant's expectations and the institutional and social contexts in both the countries of origin and destination. Research, however, increasingly reflects the view that the mobility of individuals is a consequence of transnational workspaces, including a role for family and social networks. Munshi (2003), for example, found that among Mexican migrants in the United States the probability a migrant is employed, and the level of his or her wage, rises with the size of the migrant's network, that is the number of people from his or her community of origin in Mexico who are also in the United States (Munshi is careful to account for possible endogeneity – the possibility that good economic conditions in an area simultaneously raise a migrant's probability of employment at a good wage and attract more of his or her neighbours to the area.)[5].

Two celebrated 20th-century poems provide contrasting visions of the journey through life, visions that align with older and newer perspectives on international migration. Spanish poet Antonio Machado's *Caminante no hay camino* describes a one-way path striking out through space and time. Canadian-American poet Mark Strand, in contrast, describes a different kind of movement in *Keeping Things Whole,* one that can serve to knit together social networks.

It is by walking that you make the trail
and looking back
you see only a path
you will never tread again[6]

We all have reasons
for moving.
I move
to keep things whole[7].

A recurring theme in current trends in Latin American international migration is the emerging importance – both quantitative and qualitative – of migrants who come and go to "keep things whole".

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THREE FLOWS: PEOPLE, MONEY, IDEAS

We introduced migration as one of a trio of international flows: of people, of goods and of capital. On closer examination the migration phenomenon itself resolves into three component parts. In the new transnational setting, international migration is best seen as a complex of bidirectional flows: of people, of their money, and of ideas.

People flows are at the heart of the migration phenomenon: migration is after all by definition the movement of people, whether they be workers, their family members (working or not), refugees, asylum seekers or students. In turn, these people flows have consequences for the societies they leave behind and the societies to which they migrate: consequences for labour markets and for social services, but also for the fabric of society and family networks. It is the job of Chapter 2 to look behind these concepts to the wealth of varied migration experiences that underlie them. And uncovering the links between these people flows and the economic development of Latin America is the subject of Chapter 3, which addresses the question through the lens of labour markets and social protection.

People flows are the most visible component of migration. They affect labour markets both at home and abroad

The second flow is the flow of money from migrants to their families and others back home. As Chapter 2 will show in detail, remittances to Latin America have exploded in recent years, rising from some USD 20 billion in 2000 to over USD 60 billion in 2008[8]. These figures, moreover, only reflect flows through official channels – the total resources involved are certainly even larger. Remittances now outstrip official development assistance and foreign direct investment for many developing countries. In addition to fuelling consumption and investment, remittances may serve migrants' households as a form of insurance, providing resources during tough times at home. At the macro level remittances are less volatile from year to year than export earnings or investment-related flows, even taking into consideration the crisis-related slowdown in remittances to Latin America and other parts of the developing world. This raises the interesting question of whether remittances could buffer Latin American economies from economic tumult, just as they do for households within those economies. Chapter 2 provides descriptive information on the characteristics of these flows Chapter 4 explores the links between remittances and financial development in Latin America and the Caribbean at the household level, while Chapter 5 considers their impact on the financial markets and how this too affects development.

Flows of money impact the finances of countries as well as families

Accompanying migrants and their remittances are ideas – the third flow. This is certainly the hardest to quantify (though the flows of people and money are hard enough) but may be qualitatively the most important. One need only think of how in the age of mass migration, southern European migrants to South America brought with them modes and ideologies of union organising that would indelibly mark not only the labour history, but the future political development of their host countries.

Ideas are the hardest flow to measure, but may have the most lasting effects

Transnational networks linking migrants, their families and communities, and wider diaspora groups, can be fertile ground for creative and innovative activities. A positive evaluation of the Seasonal Agricultural Worker Programme between Canada and Mexico (discussed in Chapter 6), for example, notes that returning farm workers were more likely to adopt new crop varieties on their farms. So too, migration corridors allow new information and practices associated with health and education to flow to migrants' home regions. Entrepreneurial ideas flow in both directions: "ethnic entrepreneurship", serving emigrant communities with goods and services from back home, or opening new markets in countries of origin for products from countries of destination, is a good example. Ideas can

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flow with money, too: growing remittance flows provide a feasible market for the introduction of new financial services, like mobile banking, that are discussed in Chapter 4. And last but not least is the effect of raising expectations, of demonstrating what is possible.

A ROAD MAP TO THIS YEAR'S *OUTLOOK*

The objective of this year's *Outlook* then is to analyse these three inter-related flows, and in so doing to provide food for thought for decision makers in Latin America and the Caribbean, and in the wider transnational spaces where so many international migrants live and work.

Chapter 2 provides the descriptive tools for the analysis that follows, posing the questions "how many migrants?" and "how much in remittances?" Both questions raise problems of definitions and data availability. The majority of the region's migrants are to be found in the United States, but important numbers are elsewhere in the OECD area (particularly in Spain, Canada and the United Kingdom) and this chapter also underscores the qualitative and quantitative importance of intra-Latin American flows (Argentina, Venezuela and Costa Rica are important countries of destination, some increasingly so).

Following the descriptive analysis of these flows in Chapter 2, the following three chapters explore their development impact. Chapter 3 looks at people flows through the lens of employment and social protection. The rationale for choosing this perspective is twofold. First, international migration involves the movement of workers, so that labour markets are the logical first place to look for impacts[9]. Second, the primary source of economic well-being for most people everywhere – home or abroad – is their employment situation. Thus, any effect of international migration on labour markets and social protection is critical to understanding how migration makes people better or worse off. The chapter finds that international migration certainly benefits migrants themselves in the form of higher earnings, but that this comes at a cost of increased vulnerability. Immigration of Latin Americans in OECD countries has surprisingly small effects in the countries of destination on labour-market outcomes such as wages and unemployment, and on fiscal resources. The chapter highlights the case of Spain in recent years where these effects have been positive. Least well understood is the impact of emigration on labour markets and social protection in Latin American countries themselves, though there is scattered evidence that migration may raise wages for people back home and increase labour productivity by stimulating investments in education and human capital. The chapter notes that Latin American migrants, when they cross a border, often lose all or part of the social protection (pensions, health coverage) that international migrants in other parts of the world take for granted, and discusses policy proposals in this area.

Chapters 4 and 5 assess the impact of remittance flows on financial development – the sophistication and functioning of financial markets and institutions in a country. Differences in financial development, economists agree, can explain a lot of the cross-country variation in growth rates[10]. In a sense, these chapters' macroeconomic focus complements the microeconomic focus of the chapter that precedes them. Remittances, by swelling the flow of financial resources into a number of Latin American and Caribbean countries, can be expected to have important quantitative consequences for financial development. Their effects extend beyond these however. Remittances may have important qualitative consequences by extending the reach of the banking sector

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to families and regions formerly excluded from the formal financial sector (the "bankarisation" mechanism). They may also spur the development of new services such as mobile banking, which – given the right regulatory framework – have the potential greatly to extend access to finance.

Chapter 5 widens the stage and asks whether capital-market institutions give adequate weight to the contribution made by remittances to the macroeconomic health of remittance-receiving economies. Do rating agencies, for example, consider remittance inflows when setting ratings for sovereign debt? How would this change capital markets' perceptions of country risk for important remittance-receiving economies in Latin America and for the financial institutions in those economies?

Chapter 6, as a conclusion, draws together the most policy-relevant threads of the preceding chapters. What can decision makers, in the public and private sectors, in Latin America and the Caribbean and in OECD countries, do to maximise the gains from migration for all concerned?

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NOTES

1. European Parliament (2008); European Parliament and Council (2008).
2. In May 2008, nearly 400 people were arrested at a meatpacking plant in Postville, Iowa, the largest single workplace immigration raid in United States history. As a result 262 illegal immigrants – mostly villagers from rural Guatemala – were imprisoned for using false identity documents to secure their jobs. (Susan Saulny, "Hundreds Are Arrested in US Sweep of Meat Plant", *New York Times*, 13 May 2008.) A few months later, in August 2008, at least 350 workers were detained at a factory where electrical transformers were made in Laurel, Mississippi. (Adam Nossiter, "Hundreds of Workers Held in Immigration Raid", *New York Times*, 25 August 2008.)
3. Indeed some Latin American political leaders implicitly made just this argument.
4. Some Latin American political leaders have expressed their dismay at the Return Directive, noting that their countries had received millions of European immigrants, who are today fully integrated into Latin American societies.
5. Mckenzie and Rapaport (2007) analyse the effect of the size of a migrant network on the probability of a decision to migrate, again using data from Mexico, and the interaction between network size and schooling levels. They find that the probability of migration increases with education in communities with low migrant networks, but decreases with education in communities with high migrant networks.
6. From *Campos de Castilla*, 1912, anthologised in Machado (1988).
7. The poem was part of Strand's 1964 collection *Sleeping with One Eye Open;* it is anthologised in Strand (2007).
8. These are World Bank data, from www.worldbank.org/prospects/migrationandremittances.
9. Not all migration is labour migration, of course: refugees, asylum seekers and family members of economic migrants are an important part of the flows in the Latin American context, as in other parts of the world. As Chapter 5 will demonstrate, these "nondiscretionary" flows are critically important to policy making.
10. See, for example, the survey by Levine (1997).

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CHAPTER TWO

People and Money Flows: How Many and How Much?

Any discussion of international migration in Latin America must begin by answering two basic questions. First, how many Latin Americans are international migrants? And second, how much money do they send home in the form of remittances? Each of these raises new questions in turn. Where do migrants go, for example, and how have these patterns changed over time? What kinds of households receive remittances and how do they spend them? And, of course, it is not possible to begin to answer these without looking at questions of definition and measurement – even the definition of "migrant" is by no means straightforward. This chapter will address each of these points and provide the quantitative basis for the analysis in this *Outlook*.

LATIN AMERICANS ABROAD: HOW MANY?

Defining "migrants" is difficult. It is a broader concept than often understood. To this can be added the problem of counting irregular migrants

The place of immigrants in OECD countries is the subject of heated debate. And the international migrant at the centre of these debates frequently has a Latin American face: Mexicans and Central Americans in the United States; Ecuadorians and Colombians in Spain, for example. This perception is not entirely inaccurate, as we shall see. But first things first: if we are to count migrants, we must identify who they are. A broad definition would count all of the foreign-born within a country's borders at a given moment in time, except for those who are there as visitors or tourists. These foreign-born may retain their birth nationality or they may have adopted the nationality of their country of residence – indeed, they might hold both – but they will all be immigrants. Most migrants in most OECD countries enter through legal channels, but others may be in the country without proper documentation. These are all immigrants. Those of their children – and grandchildren and so on – born in the country of destination do not fall to be counted as immigrants, though frequently they are incorrectly labelled as such in public debate.

In practice, international agencies and organisations have sought to standardise definitions around "permanent-type migration" (UN, 1998; OECD, 2008*a*. See also Box 2.1). The OECD considers as "permanent-type" migrants persons joining the resident population with a residence permit that is either permanent or more-or-less indefinitely renewable. To this are added people who move across a border under free-mobility agreements, such as those in effect among European Union countries As such, this definition does not include several categories of international migrants that are of interest to policy makers, notably seasonal workers and international students.

Irregular and unauthorised migrants pose a special problem for international statistics: in principle they are included in censuses, but since they lack permits to live or work (or both) in their country of residence, they are left out of the OECD definition. The size of these irregular migrant populations is a matter addressed later in this chapter.

The harmonised statistics used to measure permanent-type migrants are produced on the basis of population censuses. This means that estimates of the permanent-type migrant population of a country, on an internationally comparable basis, are updated only every ten years in most cases. Using census data also means that unauthorised migrants are likely to be undercounted. This year's *Outlook* will use the term "stock" to refer to the migrant population in a country, to distinguish the concept from a "flow", which measures the gross or net change in the stock during a period of time. It is regrettable that the use of terms more perhaps suited to commerce has become so widespread, but precisely because the term is so widely used we have chosen not to confuse the issue by introducing some new term in its place.

The OECD's DIOC database is a source of harmonised statistics for the stock of migrants in OECD countries. This has been supplemented by national data from Latin American and Caribbean sources

The OECD's Database on Immigrants in OECD Countries (DIOC) is the basic source of information regarding the permanent-type immigrant stock used in this chapter (see Box 2.1 for more information on the DIOC data set); for migrant stocks in Latin American and Caribbean countries we have constructed an original database, on as comparable a basis as possible, based on national censuses (for more information refer to the Statistical Annex of the Country Notes in this publication). This means that the bulk of these numbers date from around 2000. They are nevertheless the most up-to-date internationally comparable data on international migration. Moreover, they provide excellent indications of the relative magnitude of flows from Latin America and the Caribbean both to OECD countries and within the region. This information on migrant stocks can be supplemented with data on annual flows from national authorities. These data are collated in the annual OECD *International Migration Outlook*, however they are not harmonised so cross-country comparisons must be made with caution. Such flow data will permit us to consider recent changes in the composition of migrant stocks, at least in OECD countries.

Latin American and Caribbean Migrants: A Global Perspective

Figure 2.1 illustrates the origin of migrants in OECD countries using information from DIOC. The figure distinguishes among the principal regions of the world and between migrants born in other OECD countries and those born in non-OECD countries. Europeans are the best represented among migrants in the OECD area, aided in part by the free mobility guaranteed among (most) European Union countries. The next regional group, in terms of size, is from Latin America and the Caribbean and represents 28% of total migrants in OECD countries. Migrants from the Asia-Pacific economies are a slightly smaller group. Africa and North America (here meaning the United States and Canada) account for relatively small shares of the migrants in OECD countries. Note that the stock of migrants in the OECD area is not proportional to the population of their regions of origin: were that the case, the ranking would be Asia-Pacific, Africa, Europe, Latin America and the Caribbean, North America.

Panel II of Figure 2.1 shows that migrants to the OECD area do not predominantly come from the poorest parts of the world. Indeed, 44% of OECD migrants were born in OECD countries, where average income levels are far higher than the world average. Even within the sizeable Latin American flows to the OECD intra-OECD flows predominate. Some 11% of the foreign-born in the OECD are Mexican-born and 1.8% are Puerto Rican (and therefore United States citizens).

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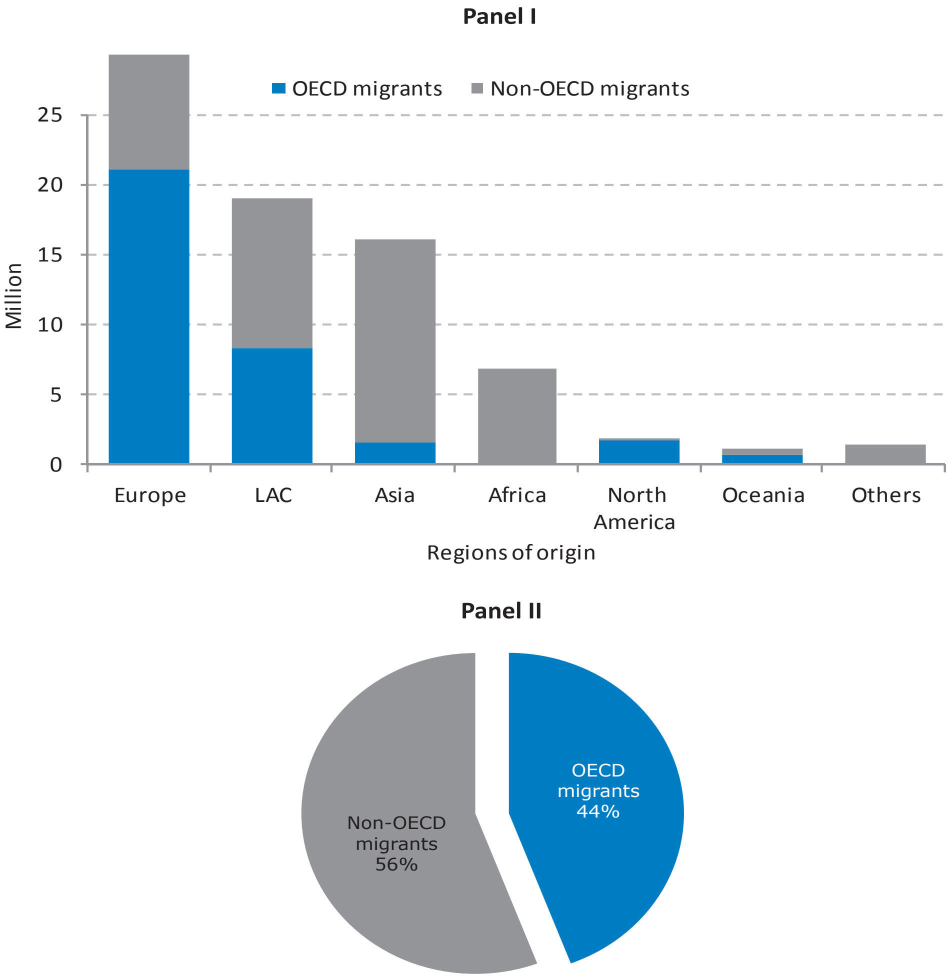
Figure 2.1. Origin of Migrants in OECD Countries by Region of Birth
(Number of migrants, circa 2000)



Source: OECD (2008*b*), Database on Immigrants in OECD Countries.

StatLink http://dx.doi.org/10.1787/715481444637

Figure 2.2 illustrates this more explicitly, plotting for each country its emigration rate to the OECD against its income per capital[1]. Despite huge differences in average income between the richest and poorest countries, migration to OECD countries is more likely to come from upper-middle or high-income countries (elsewhere in the OECD or in Latin America, wider Europe and North Africa), than from the low-income countries of sub-Saharan Africa or South Asia. Latin America's migration experience is emblematic of this pattern. Virtually all countries in the region are middle-income (with the exception of a handful of high-income Caribbean economies and Haiti which is low-income), and indeed the share of Latin Americans among migrants to the OECD is larger than their share in the world population[2].

Emigration is a middle-income phenomenon and this is reflected in the disproportionate global share of Latin American and Caribbean migrants

It is worth noting that the evidence in Figures 2.1 and 2.2 is consistent with the statistical analysis referred to in Chapter 1 of this *Outlook*, which finds that the larger the income differential between two countries, the more likely people are

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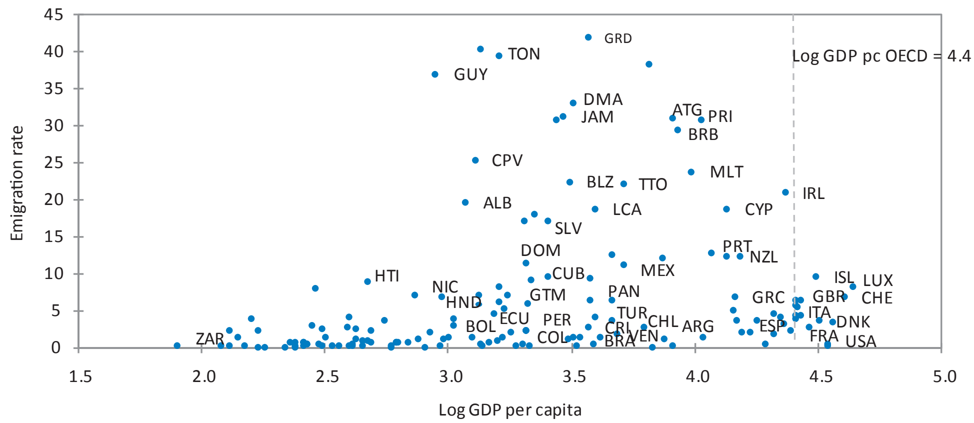
to migrate from the poorer to the richer of the pair – a finding that is intuitively quite reasonable. The difference is that those statistical studies control for other factors that might influence the potential migrant's decision, whereas Figures 2.1 and 2.2 present actual outcomes. An enterprising person from the Democratic Republic of the Congo, for example, would likely see major economic benefit from migrating to an OECD country, where average incomes are many times higher; but as Figure 2.2 shows, the actual rate of emigration from the Democratic Republic of the Congo to OECD countries is comparatively low. Our potential migrant might be dissuaded by the distance, the monetary cost of the move, the prospects for employment abroad given his or her skills and contacts, and the potential difficulties posed by the immigration regime in the country of destination. It is factors such as these that account for the difference[3].

Figure 2.2. Immigrants to OECD Countries Do Not Predominantly Come from the Poorest Countries (2007)



Note: Each data point represents and economy, plotting its (log) average income against the rate of emigration of its nationals to the OECD; for OECD countries, this is the rate.

Source: World Bank, *World Development Indicators* and OECD (2008*b*), Database on Immigrants in OECD Countries.

StatLink http://dx.doi.org/10.1787/715573587310

The Caribbean has the highest rates of emigration in the region and 10% of Caribbean nationals live abroad

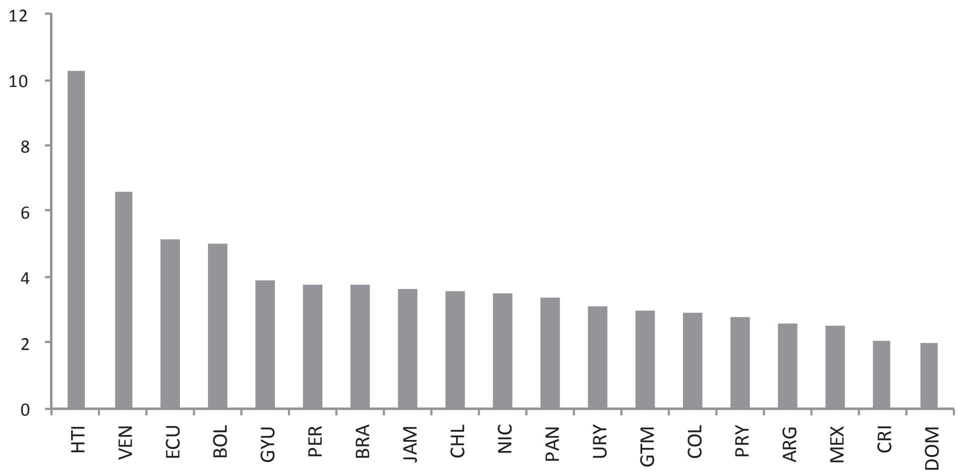
A visually striking element of Figure 2.2 is the high emigration propensity of people in the Caribbean, both in comparison with their Latin American neighbours and people from any other part of the world[4]. Most of the points in the higher reaches of the graph are Caribbean economies. Indeed, in 2000, 10% of Caribbean nationals lived outside the region, compared with 3% for Latin America and the Caribbean taken together. Migration from Cuba, Jamaica, the Dominican Republic and Haiti accounts for a substantial part – over 70% – of this extra-regional movement. Moreover, for the Caribbean, the emigrant stock (which, recall, excludes those born abroad) is growing as a share of total population, suggesting that emigration exceeds population growth. In part, the higher emigration rates in the Caribbean reflect the small size of these island nations: other things equal, one expects higher emigration rates from smaller jurisdictions, there being less scope for internal movement. However, even Cuba and the Dominican Republic, the most populous Caribbean countries, have higher emigration rates than Latin American countries with similar population sizes.

Just how large are the relevant income differentials for potential migrants? A recent study by Clemens *et al.* (2008) compares the earnings of immigrants in the United States with "observably equivalent" people from their home countries. Take their example of two 35-year-old men born and educated in Peru with nine years of schooling. Both work in the urban formal sector, one in the United States, one in Peru. The first can expect to earn USD 1 714 per month; the second USD 452 (using a purchasing-power-parity adjusted exchange rate to allow for differences in their cost of living). The Peruvian abroad is earning almost four times as much as his compatriot back home[5]. Clemens and his co-authors dub this the "place premium" – the wage increase you could get just by moving from one place to another.

The "place premium" is the wage multiplier a worker could enjoy by moving. It is typically four times in Latin America, with a range from two to ten times

The average value of the place premium (in each case for a hypothetical 35-year-old man with nine years of schooling) in the Latin American and Caribbean countries in their study is close to the Peruvian value, but ranges from over 10 for Haiti to 2 for the Dominican Republic; these estimates are illustrated in Figure 2.3.

Figure 2.3. The Place Premium
(Selected Latin American and Caribbean countries)



Note: The place premium is calculated as the ratio between the average wage of a urban male worker aged 35 years with 9 years of education resident in the US and an equivalent resident in each country of origin.

Source: Clemens *et al.* (2008).

StatLink http://dx.doi.org/10.1787/715611724551

Of course, these differences in earning power take no account of the other costs and benefits of the migration decision: perhaps opportunities to acquire new skills and experiences on the positive side, and the pain of separation from loved ones and familiar surroundings on the negative. Indeed, researchers at the University of Maryland asked Latin American migrant mothers in Baltimore if looking back they believed they had made the right decision in migrating. "To our surprise," the authors report, "most mothers said that the pain and disruption caused by family separation were so great that they doubted that they would have migrated at all given what they now know" (Gindling and Poggio, 2008). But the differences in earning power certainly illustrate, if only partially, the huge gains captured by migrants.

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Box 2.1. The OECD Database on Immigrants in OECD Countries (DIOC)

Efforts to count and characterise the immigrant population in OECD countries have suffered from differing national definitions of "immigrant". In settlement countries (Australia, Canada, New Zealand, United States), immigrants are considered to be persons who are foreign-born, that is, those who at some stage immigrated into the country of residence. In many other OECD countries, immigrants were – until recently at least – considered to be persons holding foreign nationality. Since persons born abroad can acquire the nationality of the country of residence, while persons born in a country do not necessarily acquire the citizenship of that country, this measure will count a different group of people. As immigrant populations have grown in many countries and naturalisations have become more common, estimates based on these different concepts have inevitably diverged.

In order to address this concern the OECD, in 2004, launched a data collection exercise in co-ordination with national statistical offices aimed at obtaining population-census or population-register data on the stocks of foreign-born and native-born populations in OECD countries. The core objectives of the project were to better measure and characterise foreign-born populations and especially to obtain, by aggregating across OECD receiving countries, data on emigrants by country of origin.

The first phase of data collection involved gathering data by detailed place of birth and education level. About 230 countries of origin were identified in this first database, which also made possible the estimation of "emigration rates" to OECD countries by level of education for approximately 100 countries of origin. This information provided a broad view of the movements of the highly educated for both OECD and less-developed countries.

The Database on Immigrants in OECD Countries (DIOC) goes a step further and provides from a comparative perspective comprehensive information on a broad range of demographic and labour-market characteristics of the immigrants living in OECD countries. The main sources of data for DIOC are population censuses and population registers, complemented by labour force surveys where appropriate. DIOC includes information on demographic characteristics (age and sex), duration of stay, labour market outcomes (labour market status, occupation, sector of activity), field of study, educational attainment and place of birth.

A Profile of Immigrant Populations in the 21st Century: Data from OECD Countries (OECD, 2008*b*) presents the main aggregated results of DIOC by country of residence and origin and profiles immigrant populations in OECD countries at the start of this century. It also aims to provide a first insight on how this new set of data might be used to address some of the burning questions which are posed to migration researchers and policy makers. These include, for instance, the gender dimension of the brain drain, the mismatch between the educational attainment and occupations of immigrants, international mobility in the health or domestic sectors, changes in recent migration of the highly skilled and its potential impact on origin countries.

Published results are available in OECD (2008*b*) and the data are available online at www.oecd.org/els/migration/dioc

Three-Quarters of Latin American Migrants are in the United States

As we have seen, Latin America is well represented among migrant flows to the OECD countries. How does international migration look when viewed from the Latin American perspective? Tables 2.A1 and 2.A2 in the appendix to this chapter provide detailed information about the stocks of Latin American and Caribbean

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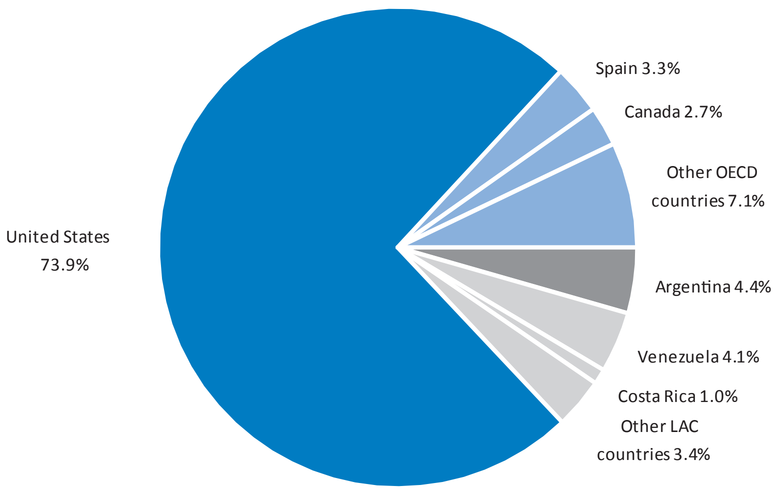
migrants within that region itself and in the OECD. Key information from these tables is summarised in Figure 2.4, which illustrates the distribution by country of destination of international migrants from Latin America and the Caribbean.

Figure 2.4. Latin American and Caribbean Migrants by Country of Destination
(Percentages, circa 2000)



Source: OECD Development Centre calculations based on OECD (2008*b*), Database on Immigrants in OECD Countries and the 2000 round of national censuses in Latin America (Processed with ECLAC Redatam+SP online).

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The bulk of international migrants from the region (86%) are in OECD countries. Fully 73.9% of total migrants are in the United States and as distant second and third place among OECD destinations are Spain (3.3%) and Canada (2.7%). Latin American immigration to Spain has accelerated since 2000, but the degree to which this will have changed the distribution in the figure is difficult to predict since flows to the United States have continued to be strong. For all Caribbean countries with the exception of Suriname at least 90% of emigrants are in the United States or Canada (with high numbers in the United Kingdom for some countries of origin). In addition to migration corridors linking Latin America and the Caribbean with North America and Europe, a historically significant Asian-Latin American corridor links Japan and Brazil. In the 2000-round censuses, some 71 000 Japanese-born people lived in Brazil, while 158 000 Brazilians lived in Japan.

OECD countries are the overwhelming destination for migrants from Latin America. Nearly three-quarters are in the United States alone...

While intra-regional migration only accounts for 14% of international migration from Latin American countries, at least two destination countries in the region, Argentina and Venezuela, have migrant stocks similar in size to those found in Spain and Canada. Costa Rica, too, is a substantial country of destination, particularly striking considering its relatively small total population (about 3.8 million).

...though Argentina and Venezuela are important countries of destination too

Figure 2.5 provides more information about the composition of migrant stocks in the six most important countries of destination: Argentina, Venezuela and Costa Rica in Latin America, and the United States, Spain and Canada in the OECD area. Migrant stocks in Venezuela and Costa Rica are overwhelmingly from a single country of origin (Colombia and Nicaragua, respectively). In all three Latin American countries, the share of immigrants accounted for by the

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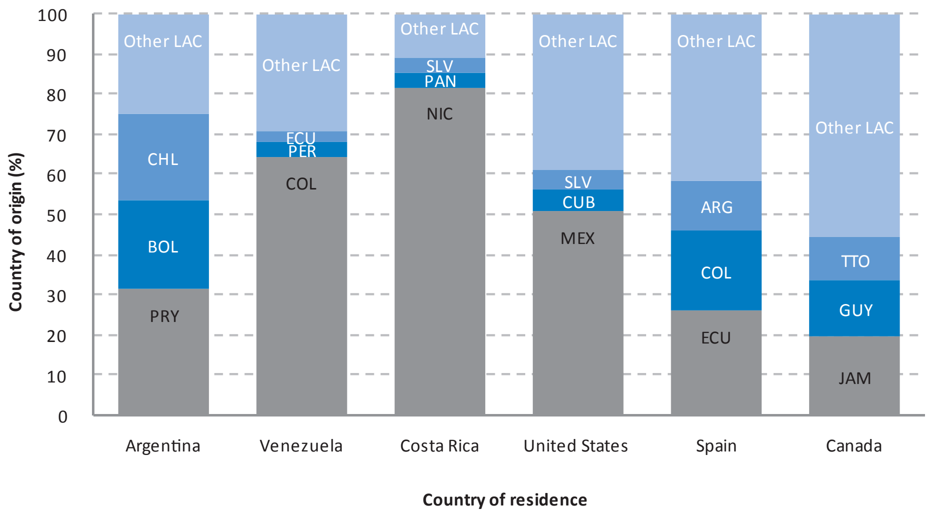
top three origin countries is over 75%. By contrast, countries of origin are less concentrated where the destination is in the OECD. In the United States only 50% of immigrants from Latin America are from the modal origin, Mexico (though this may understate the true share of the Mexican population as it certainly undercounts unauthorised migrants).

Figure 2.5. Stock of Latin American and Caribbean Migrants in Three Top Destination Countries in OECD and Latin America
(Percentages, circa 2000)



Source: OECD Development Centre calculations based on OECD (2008*b*), Database on Immigrants in OECD countries and the 2000 round of national censuses for Latin America (Processed with ECLAC Redatam+SP online).

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Intra-regional flows are smaller, but many significant corridors exist

Smaller, but nevertheless important, intra-Latin American migration corridors are identified by Durand and Massey (2008). Among these, they point out the following (with numbers from Tables A1 and A2 in the appendix in parentheses):

- Guatemalans and other Central Americans in Mexico, many of them in transit to the United States (40 000 Central Americans from all seven countries on the isthmus in Mexico, a number that probably undercounts transit migrants).
- the movement of refugees from the armed conflict in Colombia to Ecuador (45 000 Colombians in Ecuador, a number which may understate the magnitude of displaced people, especially since 2000. (Rojas and Ceballos (2006) report that some 45 000 refugees crossed the border from Colombia to Ecuador in 2001-03 alone, though relatively few were formally granted refugee status).
- movement in both directions between Paraguay and Brazil (23 000 Paraguayans in Brazil and 74 000 Brazilians in Paraguay).

Caribbean migration has likewise been characterised by significant intra-regional flows. A thriving tourism sector in Barbados and the Bahamas, and the oil sector in Trinidad and Tobago have attracted many migrants from elsewhere in the Caribbean (Martínez Pizarro, 2005).

Newer flows that may grow include: Honduras to El Salvador (9 000); Peru and Colombia to Ecuador (51 000); and Peru to Chile (36 000).

A separate category of cross-border movements, not always essentially migratory in nature, is associated with ethnic groups settled on both sides of a border, like the Yaqui straddling the United States-Mexico border, or the Yanomamo and other Amazon peoples crossing Brazil's borders with its neighbours. The line between migration and border-straddling ethnic groups is not always clear cut. In May 2009, for example, Panama and Costa Rica signed an agreement to facilitate the movement of members of the Ngöbe-Buglé ethnic group. Normally resident in Panama, 10 000 of members of the group annually cross to Costa Rica to harvest coffee beans[6].

Recent Flows to the United States and Spain Change the Picture – But Only Slightly

The quantitative discussion above has necessarily relied on census data, which provide a reasonably good overview of the composition of Latin American and Caribbean migrant stocks. And the DIOC database, which draws on these, harmonises definitions across countries to permit meaningful comparisons between, say, the number of Salvadorans reported in the United States, and the number of Salvadorans in Canada.

Information on stocks is drawn from national censuses and is therefore subject to time lag. These data can be supplemented by data on flows to paint a more current picture

But the downside of relying upon census data, of course, is their infrequency. The data reported in Table A1 date from the 2000 census round. The process of compiling and harmonising immigration data from the 2010 round of censuses has yet to begin and the kind of data presented here will not be available for many years hence. How distorted, then, is the picture these 2000 numbers provide regarding Latin Americans abroad? Certainly since 2000 some immigration flows have dramatically grown and, by the same token, some immigrant stocks large in 2000 may have experienced very little replenishment in the years since.

Information on annual immigration flows from individual OECD countries can partly fill the gaps. Indeed, information on recent flows to just the United States and Spain is nearly all we need. These are the two top countries of destination in the OECD for Latin American migrants. Moreover, the surge in South American emigration to Spain has been among the most remarked upon migration corridors in the world in the new millennium.

Table 2.1, accordingly, displays recent flows to the United States and Spain, as reported by the authorities in each country and published in the OECD's annual *International Migration Outlook*. These numbers are not in general comparable between countries, because of different definitions used (for example, a foreign student in one country might be counted as a migrant, but not in the other). Moreover, it is fair to caveat these numbers by pointing out that not all migrants remain in their destination country and, further, that circular migration may result in many being counted multiple times. Nevertheless, the comparison is illuminating. And for a given country it is meaningful to compare flows from one year to the next.

Table 2.1. **Recent Immigrant Inflows in the United States and Spain**

Country of destination	Country of origin	2000	2001	2002	2003	2004	2005	2006	2007	2008
United States	Mexico	173 490	205 560	218 820	115 580	175 410	161 440	173 750	148 640	189 989
	El Salvador	22 540	31 090	31 060	28 230	29 810	21 360	31 780	21 127	19 659
	Haiti	22 340	27 030	20 210	12 290	14 190	14 530	22 230	30 405	26 007
	Nicaragua	20 950	19 630	10 660	4 090	4 010	3 310	4 140	3 716	3 614
	Cuba	18 960	27 450	28 180	9 260	20 490	36 260	45 610	29 104	49 500
	Dominican Republic	17 460	21 200	22 520	26 160	30 510	27 500	38 070	28 024	31 879
	Jamaica	15 950	15 320	14 840	13 350	14 430	18 350	24 980	19 375	18 477
	Colombia	14 430	16 630	18 760	14 720	18 850	25 570	43 150	33 187	30 213
	Guatemala	9 940	13 500	16 180	14 390	18 920	16 820	24 150	17 908	16 182
	Peru	9 580	11 060	11 920	9 410	11 790	15 680	21 720	17 699	15 184
	Ecuador	7 650	9 660	10 560	7 070	8 630	11 610	17 490	12 248	11 663
	Brazil	6 940	9 450	9 440	6 330	10 560	16 660	17 910	14 295	12 195
	Trinidad and Tobago	6 630	6 620	5 740	4 140	5 380	6 570	8 850	6 829	5 937
	Others	30 950	37 140	38 100	27 970	35 280	50 210	58 720	46 886	45 233
Spain	Ecuador	91 140	82 640	88 970	72 580	11 940	11 590	14 290	24 647	29 353
	Colombia	46 060	71 220	34 230	10 890	16 610	20 540	27 860	35 690	33 873
	Argentina	6 670	15 980	35 410	24 760	23 240	23 660	23 040	21 216	15 413
	Peru	5 970	7 120	7 960	13 310	12 970	17 090	18 880	24 637	27 220
	Dominican Republic	5 540	5 380	5 460	6 560	8 170	10 510	12 290	16 036	15 100
	Cuba	5 370	5 160	5 070	3 900	4 690	5 210	6 940	7 865	7 947
	Brazil	4 120	4 300	4 670	7 350	13 020	20 770	28 250	31 838	21 777
	Others	13 240	18 440	28 910	44 850	64 370	79 630	101 490	79 647	33 668

Source: OECD Development Centre calculations based on US Department of Homeland Security, Yearbook of Immigration Statistics and INE Spain, Residential Variation Statistics.

StatLink http://dx.doi.org/10.1787/717261531428

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The countries which are the source of the largest inflows to the United States in 2008 are essentially the same countries that had the largest stocks there in 2000. The question is whether some stocks are growing more quickly than others, so that we might expect their ranking to be different in 2010. On the basis of this evidence, big changes are unlikely. Migration from Mexico continues to dwarf flows from other countries. Migrants from Colombia, the Dominican Republic and Haiti are entering at rates that might boost the relative importance of those immigrant populations in the United States relative to Cuban-born migrants, whose numbers are replenished relatively more slowly by migrant flows. Salvadoran inflows appear relatively less important than their stock numbers would suggest, and it may be that the relative importance of irregular migration from El Salvador – not counted here – is growing. The same may be true for Mexico.

Table 2.1 also presents information on recent flows into Spain. Here, too, the largest flows in 2008 came from the countries with the largest stocks in 2000, in this case Ecuador and Colombia. Flows from Brazil and Peru have, however, increased significantly. Ecuadorians arrived in very large numbers: 350 000 registrations between 2000 and 2004 (OECD, 2006). This may have been in response to the tightening of the immigration regime in the United States and their ability to enter Spain without a visa.

Latin American migrant populations in Spain have grown rapidly. It may now be the third most important destination after the United States and Argentina

The most important difference in the significance of the flows to Spain and the United States lies in the fact that Spanish stocks of Latin American origin started the period at much lower levels, both in absolute terms and relative to the total Spanish population. Thus the sum of the annual flows of Colombians between 2000 and 2008 is around 30% of the stock of Colombians in Spain in 2000. As a comparison the sum of the annual flows for Mexicans in the United States comes to less than 10% of the 2000 stock. This means that, while the composition of Latin American migrant populations in Spain may not be changing dramatically, their total size – as implied by these flow data – is growing more rapidly than in the United States. As a result, it is quite possible that Spain may have displaced Venezuela as the third most important destination for Latin American migrants, and indeed may displace Argentina from second place.

Undocumented, Undercounted: Irregular Latin American Migrants in OECD Countries

Readers may harbour another reservation about the use of census data: that they may not adequately account for irregular and unauthorised migrants. In principle, censuses do count irregular migrants, but in practice almost certainly underestimate the number of people in this situation. There is a surprisingly high level of uncertainty about how great the degree of underestimation is, and some studies suggest that the censuses may actually be capturing a large number of undocumented migrants (Macelli and Ong, 2002).

The scale of irregular migration can be hard to measure even if its political profile is always clear. Useful evidence can be drawn from amnesties

In many North American and European countries policy makers worry about the extent of irregular migration, particularly from developing countries. There is no more potent physical symbol of this concern that the fence along the United States-Mexico border, authorised by the US Congress in 2005, and which extended along more than 600 miles of the 2 000-mile border as of January 2009[7]. The fence, moreover, reflects the common but mistaken view that irregular migration is largely a matter of people sneaking across unguarded borders. In both North America and Europe, it is more common for migrants to fall into irregular status by overstaying a legal work or visitor visa. But regardless of how they become irregular migrants, these people face precarious situations that warrant analysis.

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The numbers of migrants discussed up to this point in this chapter probably do not adequately account for these irregular migrants. On the other hand getting reliable estimates of the irregular migrant populations in countries is difficult. One source of information is the experience of countries which have provided amnesties for the regularisation of irregular migrants. For example, Spain regularised the status of nearly 600 000 migrants in 2005, many of whom were Latin Americans. If all those regularised in 2005 had entered since the previous amnesty in 2001, this indicates that roughly 175 000 people entered Spain irregularly every year during the early part of the new millennium[8]. Another source of information is the record of arrests, detentions and other captures of illegal migrants once in the country. However, though this indicator may rise and fall with the overall size of the irregular population, it can also rise if more resources are allocated by governments to detaining irregular migrants[9].

The varied estimates of the sizes of the population of regular and irregular migrants provide an idea of the difficulty of knowing just how many migrants there are in a given country.

Table 2.2. Estimates of the Unauthorised Population in the United States
(Thousands of persons)

Country of origin	2008	2000
Mexico	7 030	4 680
El Salvador	570	430
Guatemala	430	290
Philippines	300	200
Honduras	300	160
Korea	240	180
China	220	190
Brazil	180	100
Ecuador	170	110
India	160	120

Source: Hoefer *et al.* (2009).

StatLink http://dx.doi.org/10.1787/717268245024

Estimates of unauthorised populations vary greatly, but even at the lower bounds are very substantial. Evidence from flows suggests that tightening legal entry encourages the use of irregular channels

In the United States, the Department of Homeland Security (DHS) provides annual estimates of the unauthorised population[10]. In statistics published in February 2009 (for January 2008), they estimated the total unauthorised population at 11.6 million, down from 11.8 million one year earlier. Latin Americans are well represented in this total, as Table 2.2 demonstrates. The DHS estimates that there are over 7 million unauthorised Mexican-born people in the United States. This number is almost as large as the 8.3 million Mexican-born included in DIOC of whom many, indeed probably most, reside legally in the United States. Note that according to Table 2.2, the DHS estimates the irregular Mexican population at 4.7 million in 2000, the year to which the DIOC figure refers. If all irregular Mexican migrants were counted by the census (which seems unlikely), then there were 8.3 million Mexicans in the United States in 2000, regular and irregular. If, however, the census counted *no* irregular migrants whatsoever, then the estimate of the total would be the sum of the two figures, or approximately 13 million. These figures provide reasonable upper and lower bounds on the true number of Mexicans in the United States in 2000.

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Table 2.1 shows a slight decline in the annual rate of inflow of Mexican-born migrants into the United States after 2001. Table 2.2, meanwhile, shows a growth of the stock of the irregular Mexican-born population in the United States of nearly 2.5 million between 2000 and 2008. To get a sense of the relative size of the authorised and unauthorised flows implied by these numbers, consider a back-of-the-envelope calculation. Assume that between 2000 and 2008, the unauthorised Mexican-born population increased by the same amount every year, and that no unauthorised migrants ever returned to Mexico[11]. Then the annual inflow is of the order of 294 000, almost twice the legal inflow. Similar relative magnitudes apply for El Salvador, Guatemala and Honduras – that is, unauthorised flows may have surpassed legal flows in an environment of tighter controls. The same cannot be said, however, for South American countries in the United States statistics: legal flows from these countries to the United States are probably larger than unauthorised flows. Taken together, these indicators strongly suggest that tightening of the immigration regime, as occurred in the United States after 2001, displaces some legal migrants toward illegal entry. This is consistent with a comprehensive research programme that studied undocumented workers in seven European countries, and concluded that the tightening of immigration controls in all seven countries was associated with an increased number of undocumented migrants (McKay *et al.*, 2009).

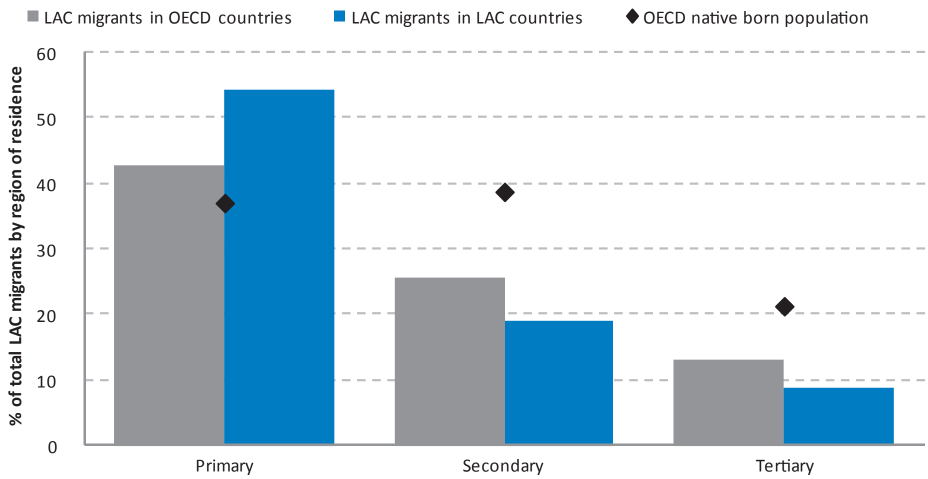
Skill Levels and Mobility: Two Different Worlds of Migration

DIOC data allow the analysis of migrant populations by educational attainment

The skill level of migrants is an important element in the debate surrounding migration from Latin American countries. Many OECD countries specifically compete to attract highly educated immigrants, facilitating their arrival with special programmes and visas. At the same time, citizens and policy makers in many countries of immigration wonder just how many poorly educated immigrants their economies can absorb. The DIOC data allow us to look at the average level of educational attainment of immigrants in OECD countries; this measure is frequently – though somewhat imprecisely – taken as a proxy for migrants' labour-market skills. In the graphs that follow, we distinguish among individuals with primary, secondary or tertiary education.

Figure 2.6 compares the distribution of education levels for Latin American migrants (in OECD countries and in Latin American countries) with that of the native-born population of OECD countries. OECD natives are more educated than Latin American migrants – more people have secondary and tertiary education, and fewer have only primary. On the other hand, different destination does not seem to reflect in education levels: in the aggregate, educational levels between migrants who go to OECD countries and those who go to other Latin American countries are very similar.

Figure 2.6. Level of Education of Latin American and Caribbean Migrants in OECD and Latin America
(Percentage of population aged 25 years or over, circa 2000)



Source: OECD Development Centre calculations based on OECD (2008*b*), Database on Immigrants in OECD Countries and the 2000 round of national censuses for Latin America (Processed with ECLAC Redatam+SP online)

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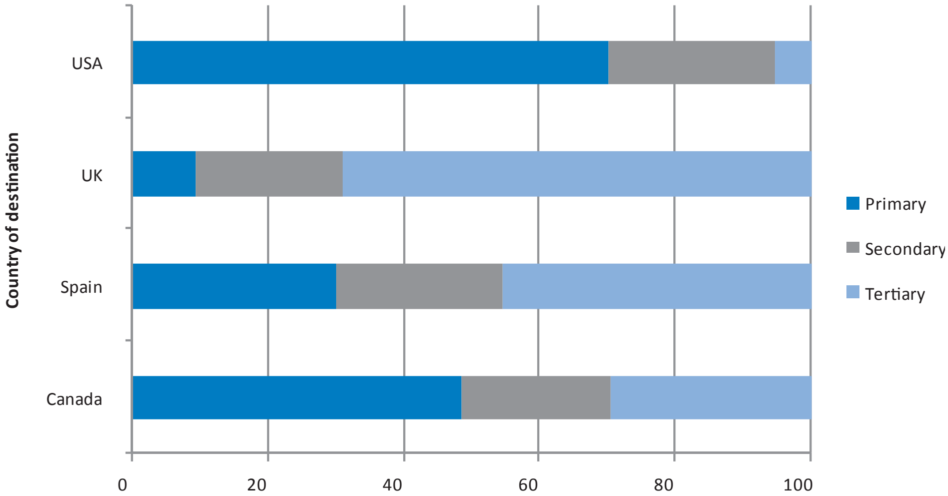
Differing migration corridors present very different educational profiles. Among migrants to the United States a quarter of South Americans have only primary education. For Mexican migrants the proportion is two-thirds

These aggregate statistics, however, mask a great deal of variation between different migration corridors. Thus, for example, Mexicans in the United States have relatively low levels of education, but Mexicans in other Latin American countries have relatively high levels. To provide some insights into the complicated relationship between educational attainment and destination, the different panels of Figure 2.7 illustrate the education distribution of migrants to the principal OECD countries of destination (the United States, Spain, Canada, the United Kingdom) together with Mexico, differentiating among four regions of origin: Mexico, Central America, South America and the Caribbean.

The panels demonstrate the heterogeneity of education levels and confirm the existence of low-skilled migration corridors from Latin America and the Caribbean to OECD countries. Among the most important is the largest of all the flows, that of Mexicans to the United States. Two-thirds of Mexican migrants in the United States have only a primary education, and less than 10% have tertiary education. The structure of this flow is mirrored in that of Central Americans in Mexico, Caribbean migrants in the United Kingdom and Spain, and, to a lesser degree, South Americans in Spain.

Figure 2.7a. Education Levels of Mexican Migrants
(Percentages, persons aged 15 years or over)



Source: OECD (2008*b*), Database on Immigrants in OECD Countries.

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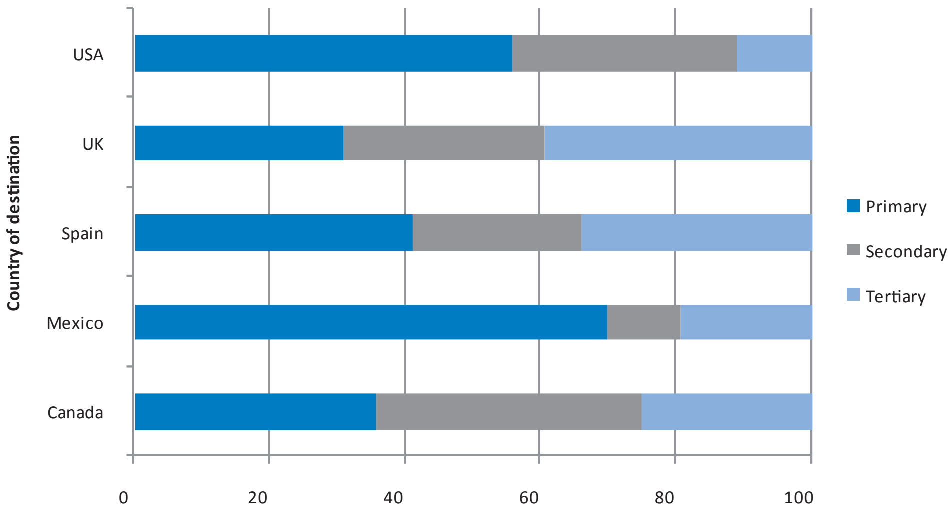
Figure 2.7b. Education Levels of Central American Migrants
(Percentages, persons aged 15 years or over)



Note: Central American migrants cover the following countries: Belize, Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua and Panama.

Source: OECD (2008*b*), Database on Immigrants in OECD Countries.

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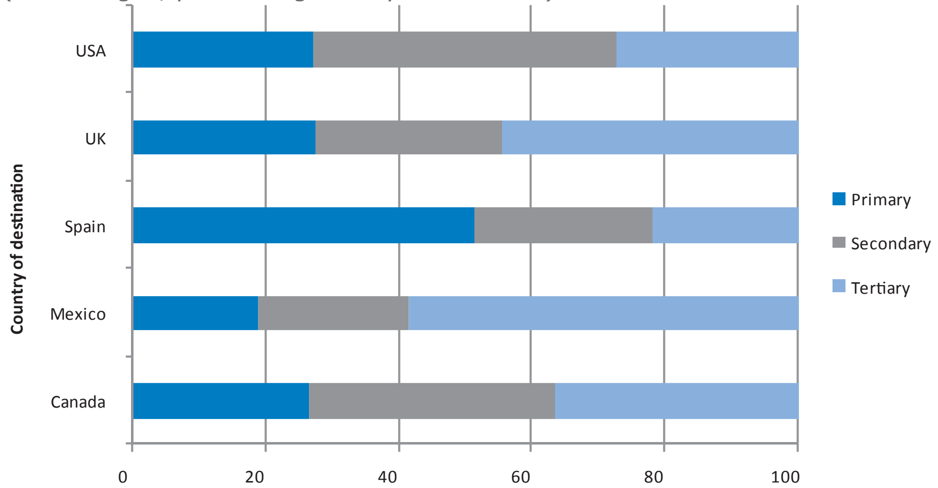
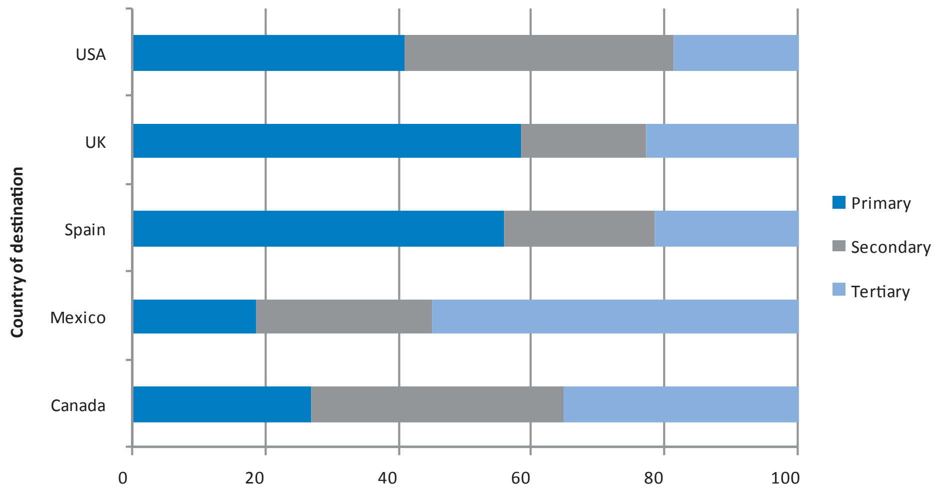
Figure 2.7c. Education Levels of South American Migrants
(Percentages, persons aged 15 years or over)



Note: South American migrants cover the following countries: Argentina, Bolivia, Brazil, Chile, Colombia, Ecuador, Guyana, Paraguay, Peru, Suriname, Uruguay and Venezuela.

Source: OECD (2008*b*), Database on Immigrants in OECD Countries.
StatLink http://dx.doi.org/10.1787/715737278381

Figure 2.7d. Education Levels of Caribbean Migrants
(Percentages, persons aged 15 years or over)



Note: Caribbean migrants cover the following countries: Anguilla, Antigua & Barbuda, Aruba, the Bahamas, Barbados, Bermuda, the British Virgin Islands, the Cayman Islands, Cuba, Dominica, the Dominican Republic, Grenada, Haiti, Jamaica, Montserrat, the Netherlands Antilles, Puerto Rico, St.Kitts and Nevis, St.Lucia, St.Vincent and the Grenadines, Trinidad and Tobago, Turks and Caicos and the US Virgin Islands.

Source: OECD (2008*b*), Database on Immigrants in OECD Countries.
StatLink http://dx.doi.org/10.1787/715753277101

Some migration corridors, meanwhile, are travelled by relatively higher-skilled migrants. This is notably the case of South American and Caribbean migrants to Mexico. For many skilled Latin Americans, Mexico is an attractive destination – indeed, during the era of military dictatorships in the Southern Cone Mexico was a common choice of political exiles, many of whom were relatively highly skilled. This also indicates that the "brain drain" is not exclusively a phenomemon affecting flows from developing to high-income countries, given Mexico's middle-income status. (The existence and impact of any brain drain from Latin America and the Caribbean is considered further in Chapter 3.)

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Migration and the Sexes

Globally nearly 50% of international migrants are female. One would not necessarily expect this apparent neutrality of migration to hold for all flows and at all times. Migration histories frequently seem to imply uneven sex ratios at different stages of the process. The classic example is of the male migrant who sets off on his own to work in agriculture or construction planning to send for his wife and children at a later date; or the lone female circular migrant working in people's homes. International statistics do indeed confirm imbalances in the gender composition of migrant stocks. While women are 52% of international migrants in developed countries, they make up only 46% of the total in developing countries, for example (UN, 2009).

Migrants to the United States are disproportionately male, while migrants to other OECD countries are disproportionately female

Among Latin American and Caribbean migrants in the OECD area, 49% are women[12]. But this aggregate average masks two very contrasting trends. First, migrants to the United States from Latin America and the Caribbean are disproportionately male. Thus, for example, only 44% of Mexican migrants in other OECD countries – the vast majority of whom go the United States – are women. Second, migrants in other OECD countries are disproportionately female: 58% of Latin American immigrants in Spain are women, for example. These disparities stem in part from the prevalence of male-dominated temporary (and sometimes irregular) migration patterns between countries that are closer geographically, such the United States and its near neighbours in Mexico and Central America. The sex ratio of migrant flows is closer to balance for migrants from higher-income countries in South America, whether their destination is the United States or elsewhere in the OECD.

Female migrants have lower labour-force participation rates than their male colleagues, are more likely to work in jobs below their educational level and suffer greater wage gaps against native workers

Female labour-market participation rates in the host country are usually lower than for men or native-born women. (This disparity tends to disappear for their (non-migrant) daughters; see OECD, 2007.) Undocumented immigrant men tend to have very high labour participation rates (94%), compared to women in similar situations (54%) (Passel, 2007). Migrant women are more likely to find themselves in jobs that do not reflect their qualifications (OECD, 2007) although the emigration rate of highly-skilled women is generally higher than that of high-skilled men (Dumont *et al*., 2007). The skill composition of female migrants may affect whether they are complements or not of the native-born women. In a case study on Nicaraguan migrants in Costa Rica, Nicaraguan migrant women of lower skill working in domestic service were found to be substitutes for less-educated Costa Rican-born women of the same skill and occupation, while more educated Nicaraguan women were working in roles complementary to Costa Rican women. These results were not found for men (Gindling, 2009).

Women also tend to suffer very large wage gaps. In the United States, for instance, the wage gap between native-born and immigrant workers is larger than that between the sexes. As immigrant women are in both groups, they face a double disadvantage.

Migrants Going Home

Return home, sometimes involuntary but often planned from the outset, is very much part of international migration today. What drives this return is imperfectly understood

Migration is not a one-way street, "a path the migrant will never tread again", to paraphrase Antonio Machado from Chapter 1. Migrants do indeed go home, and this return migration is a complex phenomenon. Until recently migration specialists tended to view return migration as associated with either life stages (for example on retirement) or a "failure" in the emigration episode (perhaps as a result of false hopes about the host country, integration difficulties, unemployment, family considerations). Migration flows are now recognised as considerably more heterogeneous and dynamic; return flows reflect a mix of all

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of these stimuli, and even simple – and rational – preferences to consume or to invest "back home". The global crisis has provoked considerable debate about whether the declining economic outlook will prompt Latin Americans (and other migrants) to leave the OECD countries to which they have migrated. In some countries this has gone so far as to see the adoption of policies specifically to encourage return migration. Some of these links between the crisis and patterns of return migration are considered further in Chapter 3.

How many migrants return home? For many international migrants, return is built into their migration status: they hold fixed visas or other rights, and must – or at least should – return home when their time is up. Arguably, a more interesting question is how many migrants with a right to remain in the country of destination ultimately go home.

The evidence – imperfect, admittedly – on return migration tells us that the rate depends on the age profile of migrants (higher return by younger and older cohorts), on skills (again higher at the tails of the distribution), and on some temporal and geographical "fixed effects" (country of destination and period of time considered).

Estimates by the OECD (2008*a*) for European OECD countries and the United States indicate that between 20 and 50% of immigrants leave within five years of their arrival, either to their home country or to a third one. The rate of return from Spain or the United States for migrants from Argentina, Brazil, Chile, Costa Rica or Mexico is lower: ranging from 16% (Chileans leaving Spain) to 4% (Argentinians from either host country, and Mexicans from the United States). These figures probably obscure considerable variation: a study by Reyes (1997), for example, looking at families in western Mexico found substantially higher rates of return and shorter stays abroad. About 50% of migrants in the Reyes study returned from the United States after only two years, and by ten years, almost 70% had returned. Return was particularly common among less educated migrants.

There is evidence that returning migrants do better in their home job market but it is not clear whether this is directly a result of their experience abroad

Return migrants, whether permanent or as part of seasonal or circular mobility, often re-enter home labour markets – with variable success[13]. Gitter *et al.* (2008) found that Mexican return migrants were more likely to find employment back home than those who had never left, but suggested that the causality runs in reverse: migrants were more likely to return home when employment prospects were better. Mexican return migrants (like Mexican migrants to the United States more generally) were typically low-skilled workers and commanded higher earnings upon their return than those who did not migrate. Nevertheless, it is not clear that this is due to faster accumulation of on-the-job human capital by the migrants – it may instead be that migrants tend to have higher earning power than those who never left (Lacuesta, 2006).

There are significant differences between Mexicans going back home and other Latin American return migrants (OECD, 2008*a*). The distributions of both educational attainment and occupations of returning Mexicans are very similar to that of the overall Mexican population (Figures 2.8 and 2.9). In contrast, migrants returning to Argentina, Brazil, Chile and Costa Rica tend to have higher levels of human capital than their national average and find work in higher-skilled occupations.

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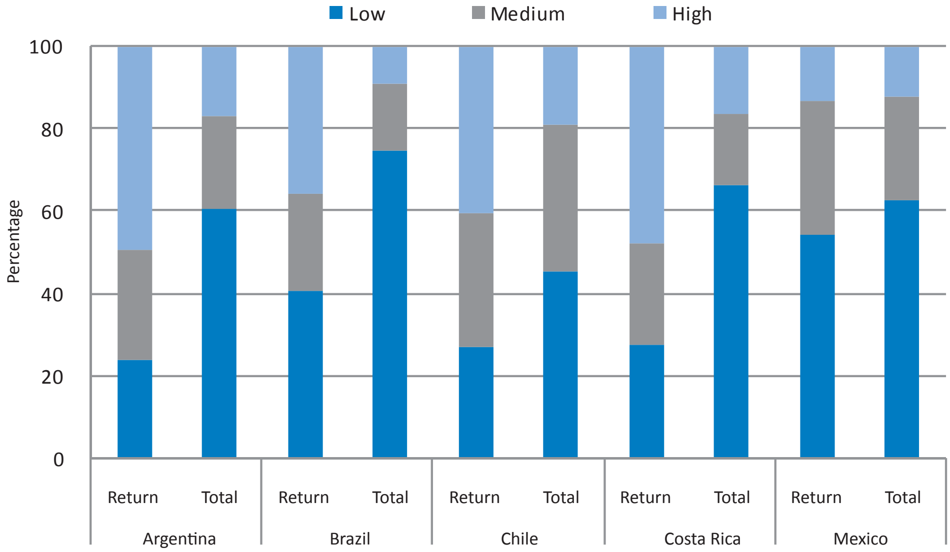
Figure 2.8. Educational Attainment of Return Migrants
(Persons aged 30 years or over, circa 2000)



Source: OECD (2008*a*).

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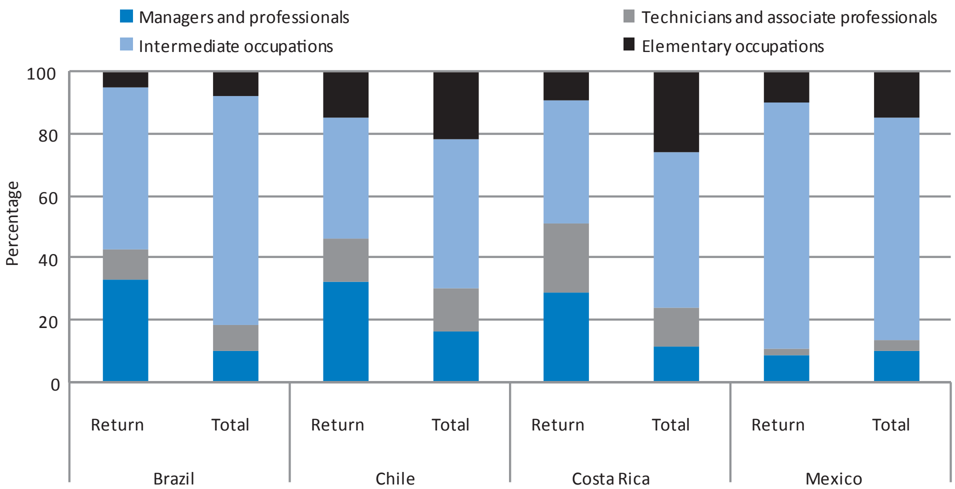
Figure 2.9. Occupations of Return Migrants
(Persons aged 25 years or over, circa 2000)



Note: Occupations are recorded according to the International Standard Classification of Occupations (ISCO-88, cf. ILO 1990). "Managers and professionals" correspond to groups 1 and 2, "technicians and associate professionals" to group 3, "intermediate occupations" to groups 4 to 8 and "elementary occupations" to group 9 of the ISCO classification.

Source: OECD (2008*a*).

StatLink http://dx.doi.org/10.1787/715775544257

Many return migrants invest in entrepreneurial activities and thereby may fuel labour markets, both formal and informal. Savings accumulated abroad allow return migrants to be self-employed and, frequently, to shift among sectors of the economy[14].

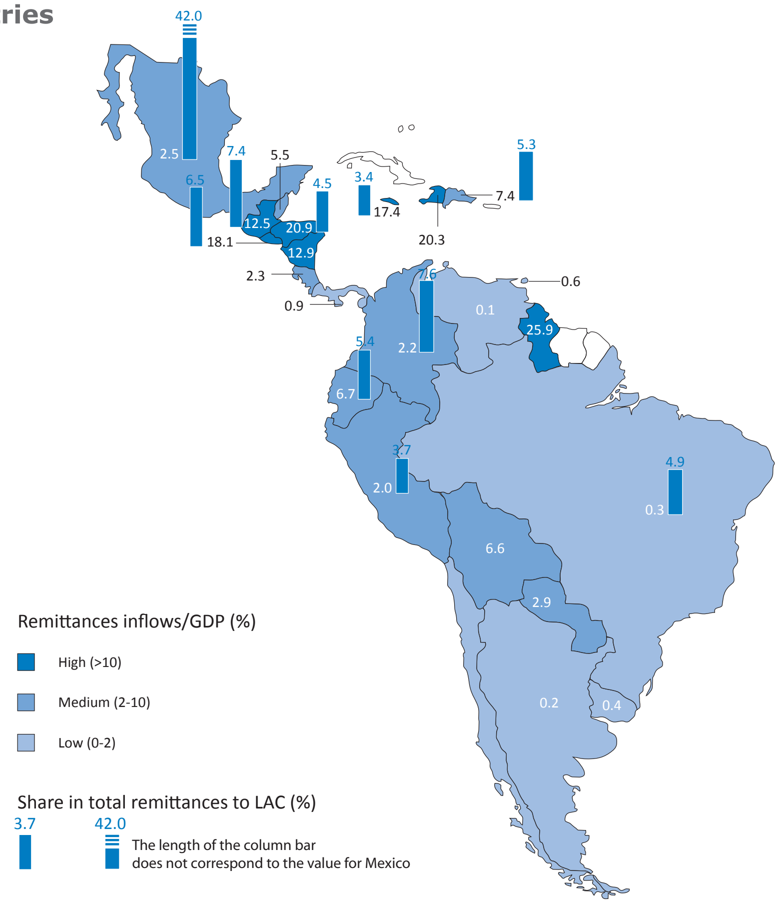
It is to that money, earned abroad but employed in the economy of origin that this chapter turns now.

REMITTANCES TO LATIN AMERICA AND THE CARIBBEAN: HOW MUCH?

Remittance flows are large in absolute terms and represent an important share of GDP for many countries in Latin America and the Carribean

The money that migrants send home has captured the attention of policy makers, entrepreneurs, community-development organisations and others – unsurprisingly, given the amounts involved in both absolute and relative terms. Figure 2.10 shows that workers' remittances represent an important share of GDP in several countries in Latin America and the Caribbean. This is particularly the case in relatively small economies in the Caribbean (Jamaica, Haiti and the Dominican Republic) and Central America (El Salvador, Guatemala, Honduras and Nicaragua). For these remittances exceed 10% of GDP. Several of the larger economies in Latin America, notably Ecuador and Bolivia, have remittances making up a high proportion of GDP when compared with other countries in the region of similar size. In terms of absolute amounts of money Mexico is by far the largest recipient: more than 40% of total remittances to Latin America and the Caribbean go to Mexico, a reflection of the predominance of Mexican migrants in the United States discussed above.

Figure 2.10 Workers' Remittances to Latin American and Caribbean Countries



Note: a) Remittances are measured using the estimates of workers' remittances in the balance of payments current transfers account. *b)* Three different clusters have been identified (high, medium and low). *c)* The columns correspond to the ten countries having a higher share in total remittances to LAC – Mexico (42.0), Colombia (7.9), Guatemala (7.4), El Salvador (6.5), Ecuador (5.4), Dominican Republic (5.3), Brazil (4.9), Honduras (4.5), Peru (3.7), Jamaica (3.4).

Source: OECD Development Centre calculations based on IMF *International Financial Statistics* and Balance of Payments Statistics databases.

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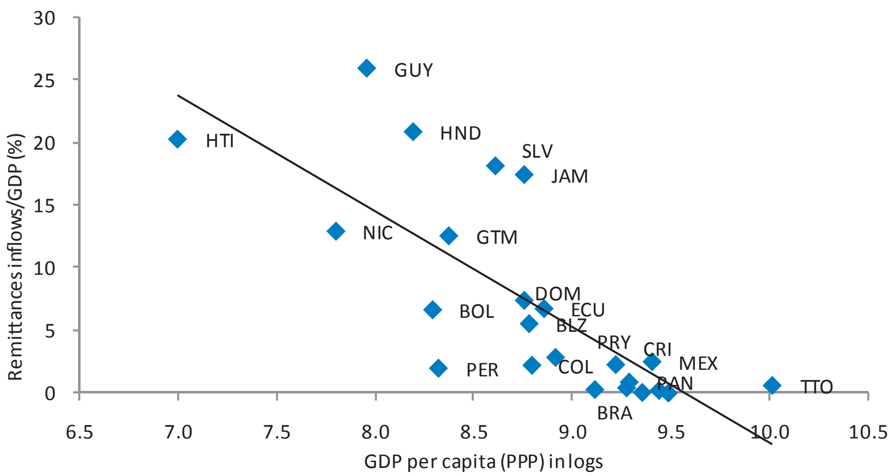
It is important to point out that the numbers in Figure 2.10 and elsewhere in this *Outlook* (except where explicitly noted) refer to official balance of payments data regarding "Workers' Remittances" drawn from the IMF *International Financial Statistics* database. Other studies (see World Bank, 2008) have used a broader concept of remittances that includes two additional balance-of-payments items: Compensation of Employees and Migrants' Transfers. However, as discussed in detail in Chami *et al.* (2008), these items capture rather different phenomena. Migrants' Transfers are mainly asset transfers in connection to people moving across borders or even merely changing their legal residence for tax purposes. Compensation of Employees includes payments by resident firms to non-resident workers (debit) and remuneration received by domestic workers from non-resident firms (credit). This item tends to capture seasonal workers' compensation, often related to temporary movements within multinational firms.Nor do these data net out the part of income spent in the host country. Chami *et al.* (2008) also demonstrate that these categories show very different movements over time and with the business cycle. Therefore, we follow their recommendation and use only Workers' Remittances[15].

That definitional question settled, there remain severe problems of measuring remittances in the balance of payments statistics. Many remittances, for example, are sent through informal channels and hard to capture statistically. Furthermore, as discussed in Box 2.2 below, new technologies are changing the relative costs of channels creating new measurement challenges.

Unsurprisingly, the ratio of remittances to GDP tends to be higher in poorer countries and lower in relatively more prosperous ones. Figure 2.11 illustrates this significantly negative association within Latin America and the Caribbean. Partly this relationship reflects the stronger incentives to migrate from poorer countries[16]. But the level of variation between countries suggests that this cannot be a complete answer. For example, countries with similar levels of development – say, Paraguay and Guatemala – experience very different remittances flows. Factors affecting propensity to migrate (discussed above) are clearly at work. Guatemala is both closer to the United States and has the additional push factor of a recent civil war.

It is for poorer countries that remittances tend to represent the highest share of GDP

Figure 2.11. Correlation between Remittances and Income Levels
(2007)



Note: Remittances are measured using the estimates of Workers' Remittances in the Balance of Payments Current Transfers Account.

Source: OECD Development Centre calculations, based on IMF *International Financial Statistics* and Balance of Payments Statistics databases.

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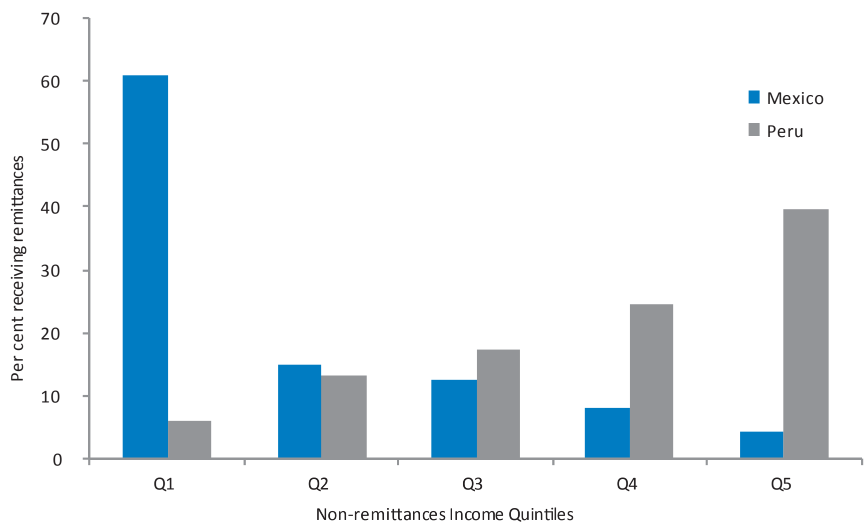
Who Gets These Remittances?

Which families benefit most from remittances varies country by country: it may be the poorest as in Mexico, or the better off as in Peru

The literature on remittances and development emphasises the role of remittances as a potential tool for poverty reduction. For example, combining aggregate cross-country panel data and household surveys, Acosta *et al.* (2008*a*) find that remittances reduce average poverty and inequality in Latin America. At the individual level, however, this impact depends very much on the characteristics of the migrants and their household of origin. The heterogeneity in the social and educational background of migrants, discussed above, is reflected in a similar heterogeneity in the socio-economic conditions of remittance-receiving households. Figure 2.12 illustrates this by contrasting the incidence of remittances across the income distribution in Peru and Mexico. In Mexico, households at the bottom of the income distribution (before remittance income) are much more likely to receive remittances: 60% do so in the poorest quintile compared to only 4% in the richest quintile. In Peru the situation is completely reversed: the richer the household the higher the likelihood of receiving remittances. Thus, it is clear that the impact of remittances on poverty and income inequality can differ sharply depending on these patterns.

Figure 2.12. Position of Households Receiving Remittances in Income Distribution, Mexico and Peru, 2002



Source: Acosta *et al.* (2008*a*)

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What Are They Used For?

Remittances are overwhelmingly used to boost consumption. To criticise this may be to miss the corresponding boost to human capital formation, through increased education or health for example

How do migrants' families back home use the remittances they receive? All the evidence is that remittances principally boost consumption. A survey of Salvadoran households sheds some additional light; for households that receive relatively smaller total remittances some 80% of the transfers are used to finance consumption. That share drops for households receiving relatively larger remittances and those who get most devote less than half of the money received to consumption. This latter group of households channel a relatively larger share of remittances to savings.

Many have lamented this propensity to use remittances to fuel consumption. Surely, runs the reasoning, remittances would better promote development

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back home if they were invested in productive projects. While it is true that increased investment in Latin America is likely to have dynamic benefits for growth and development, it is not necessarily true that consumption by migrants' families is not productive. Much of what is commonly classified as consumption is really investment in human capital, which for a host of reasons is more socially productive than investment in physical or financial capital. For the poorest households, after all, consumption can be an investment if it raises the future productivity of household members. This can be true of better nutrition or of more schooling[17]. In that sense, consuming rather than saving today will raise rather than diminish future consumption possibilities. Moreover, using remittances to buy consumer durables – the refrigerator is a prosaic but potent example – can improve well-being in important ways: a refrigerator can allow households to buy food in larger quantities, saving money; it can reduce the risk of sickness from infection and other problems from unrefrigerated perishables; it can even serve as equipment for a micro-enterprise. Using remittances to improve the physical quality of one's house improves health and well-being in analogous ways. The appropriate policy objective in such circumstances should not necessarily be to raise the share of remittances devoted to investment in a narrow sense, but rather to ensure that no bottlenecks such as poor penetration of the banking system (see Chapter 4) prevent families from investing remittances if they choose to.

A World Bank study (Fajnzylber and López, 2008), systematically assesses consumption patterns among households that do and do not receive remittances in seven Latin American countries. Their analysis shows that the trends revealed by the Salvadoran evidence hold for many remittance-receiving households in the region, and confirms that the impact of remittances on household behaviour differs between richer and poorer households. Higher-income households are more likely to invest remittances in education (except in Mexico, but only because remittance-receiving households at all income levels use remittances to keep their children in school longer). Lower-income households are more likely to increase their savings rates – an effect consistent with the Salvadoran pattern discussed above, if poorer households are also those that receive more remittances.

Remittances on the Macroeconomic Stage

Remittances in Latin America are not only large relative to the size of local economies, they are also large relative to other capital inflows. Remittances inflows to the region are comparable in size to foreign direct investment (FDI) flows and greater than official development assistance (ODA) or other non-FDI flows. As Figure 2.13 shows, in 2007 remittances were around twice the size of non-FDI private capital inflows and ten times larger than ODA flows to Latin America.

Remittances across the region have grown from less than 0.1% of GDP in 1980 to more than 1.5% in 2007. They now rival FDI and are comfortably greater than ODA

And total remittances – or at least measured remittances – are growing. In the last ten years, remittances to the region have increased by a factor of 3.3 in real terms. This is a figure to be treated with caution, given improvements in the measurement of remittance flows in balance of payments statistics as well as the probable substitution of informal channels by formal ones in response to the decline in costs of the latter (see Box 2.2 below and Orozco, 2006). Even so, for the region as a whole remittances have been progressively increasing as a proportion of GDP: from less than 0.1% in 1980 to more than 1.5% in 2007.

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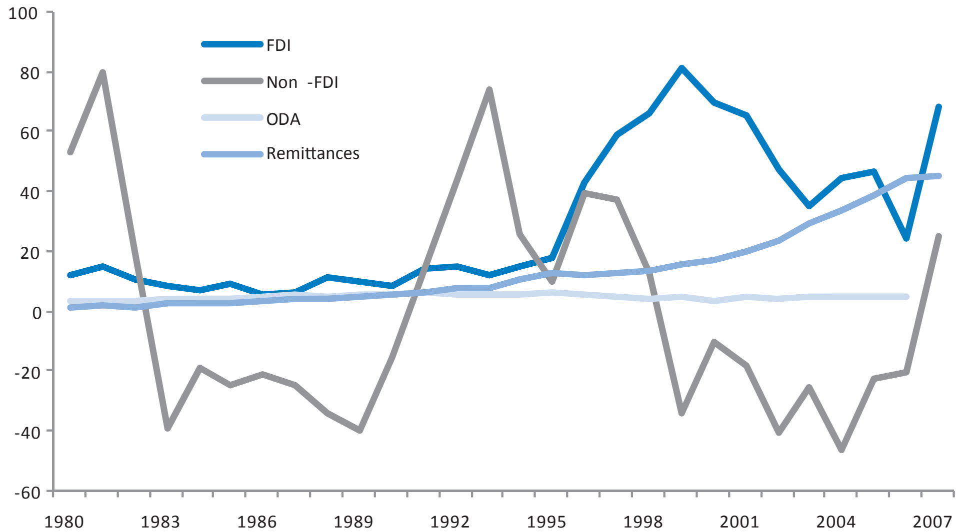
Figure 2.13. Net Capital Flows to Latin America
(Constant prices, USD billions)



Note: Remittances are measured using the estimates of workers' remittances in the balance of payments current transfers account.

Source: OECD Development Centre calculations, based on IMF *International Financial Statistics* and Balance of Payments Statistics databases.

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Another characteristic of remittances clearly apparent from Figure 2.13 is that they tend to be much less volatile than other flows, even exports. Furthermore, the remittance flows to the region are negatively correlated with private capital flows[18]. These results are consistent with similar findings for developing countries more generally[19]. Therefore, remittances provide a relatively stable flow of funds and can reduce the volatility of the capital account and so macroeconomic volatility, an issue explored in further detail in Chapter 5.

The question of how remittances relate to the business cycle is more complex, and there have to be two parts to the answer: the correlation between remittances and economic conditions in the home country, and between remittances and conditions in the host country.

Remittances are less volatile than other international flows. Evidence about how they correlate with the economic cycle is mixed however

If the correlation with home-country conditions is negative, remittances may provide an important buffer against economic downturns; this would be the situation if migrants were prompted to increase the amount they send in respsonse to news of economic problems at home. Not surprisingly, the evidence is somewhat mixed. For example, while Giuliano and Ruiz-Arranz (2005) found that remittances in general presented a positive correlation with the home country's business cycle, Chami *et al.* (2005) found a negative correlation, and Sayan (2006) a great deal of heterogeneity across countries. In part these different results stem from different samples, econometric methods and data used by the authors of these studies. In a study of Latin American countries that paid careful attention to these methodological issues, Acosta *et al.* (2008*b*) confirmed a wide dispersion within the region of the cyclical patterns of remittances. The results of a similar analysis are shown in Figure 2.14[20]. While for Mexico and Ecuador remittances are counter cyclical, for Nicaragua and Peru they are highly pro-cyclical, and for many countries basically acyclical. For 13 out of 23 countries, the correlation is negative. On average, the correlation is slightly negative but not statistically significant, and again it is difficult to draw conclusions about a pattern within the region.

Box 2.2. Remittances and the Current Crisis

The Inter-American Development Bank (IDB), through its Multilateral Investment Fund (MIF), has been providing estimates of remittance flows to its member countries in Latin America and the Caribbean since 1999.

According to these estimates worldwide remittances to Latin America and the Caribbean reached USD 69.2 billion in 2008, an increase of just under 1% over the prior year. Despite the challenges faced by migrant workers and their families in 2008, as remittance senders they proved to be remarkably resilient. The financial crisis, however, has raised new obstacles to migrant workers' ability to send money home.

A recent MIF survey of remittance senders showed that remittances to the LAC region are estimated to decrease by 11% in 2009, marking the first downturn since the IDB began tracking these flows. Approximately 4 million people in the region will be affected by the decline in remittances.

The slowing US economy and a loss of jobs in sectors that traditionally attract immigrant labour, such as construction, have been mirrored in other countries with significant migrant communities from the region. Spain, for example, is experiencing a downturn in construction proportionately at least as bad as the decline in the US housing sector. Japan, an important source of remittances to Brazil and Peru, has seen declining industrial production as export demand has slumped.

The survey of migrants in the United States found that they are sending money with less frequency and in smaller amounts. However, the survey also pointed out that even people who have lost their jobs are still sending money home, usually by dipping into savings. Migrants are employing different strategies to keep making remittances, even during the downturn, including cutting their expenses, taking second jobs, or working more hours.

Flows in 2008 were also affected by exchange-rate considerations particular to that year. In contrast to the slow depreciation of the US dollar during the first three quarters of 2008, the onset of the financial crisis saw a dramatic appreciation of the greenback against major Latin American currencies. The effect this had on purchasing power certainly affected remittance-transfer behaviour. In October 2008, immigrants from Mexico, Brazil and Colombia saw the value of a dollar sent home rise by 20 to 30% in home-currency terms. As a result, migrants sent home remittances in record amounts. The continued strength of the dollar since will go some way towards offsetting the effects of a decline in the volume of dollars sent. Dollarised countries and those with currencies pegged to the dollar do not benefit from this trend, of course.

The experience of Andean countries with significant diasporas in Europe (principally in Spain) was different: they were hurt by the rapid decline in the value of the euro between July and October of 2008. This weakness persisted into first three months of 2009 and the value of remittances to Andean countries that are more dependent on European flows is likely to suffer as a result.

These dynamics have very different effects, depending on specific exchange-rate regimes and the countries from which remittances are sent. Since October 2008, remittances to Latin America and the Caribbean as a whole have grown in local currency terms, even though in dollar terms they have declined. Together with slowing inflation in the region the overall impact on the purchasing power of remittance recipients (at least until the first quarter of 2009) is positive.

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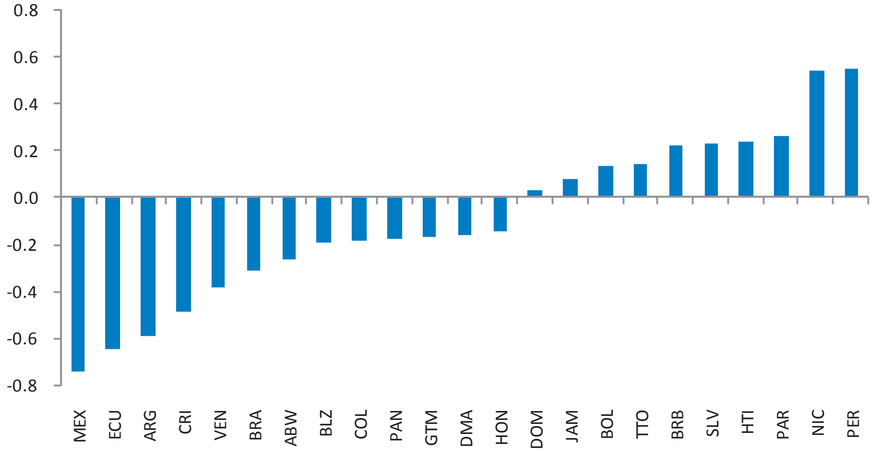
Figure 2.14. Cyclical Correlation between Remittances and GDP Output Gap



Note: Time spans are determined by the availability of national data.

Source: OECD Development Centre calculations based on IMF *International Financial Statistics* and Balance of Payments Statistics databases.

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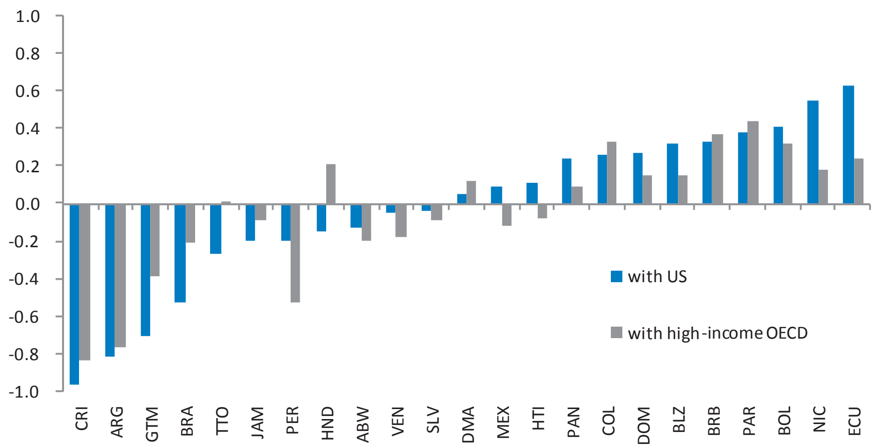
Perhaps a greater concern in the current context of continuing economic crisis in the United States is the correlation of remittances with economic conditions in the host (rather than home) country. Roache and Gradzka (2007) show that remittances flows to Latin America are relatively uncorrelated with the US business cycle, while Acosta *et al.* (2008*b*) present some evidence of a positive correlation between the business cycle and remittances to Latin America (and developing countries in general). Figure 2.15 presents some data in this regard. On average, remittance flows seem rather insensitive to host-country business cycles, but the situation again varies widely across countries. For example, even within Central America, remittances to Guatemala exhibit a significantly negative correlation with the US business cycle; El Salvador exhibits basically no correlation, while in Nicaragua there is a positive correlation.

Figure 2.15. Cyclical Correlation of Remittances with the Sending Country's Output Gap



Note: Time spans are determined by the availability of national data.

Source: OECD Development Centre calculations based on IMF *International Financial Statistics* and Balance of Payments Statistics databases.

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The result that remittance flows to Latin America and the Caribbean are relatively immune to fluctuations in host-country business cycles suggests that remittances can play a stabilising role for the home country. However, such a conclusion is of little value to an individual country or its policy makers who must look to country-specific factors in forecasting impacts on flow or cyclicality. Furthermore, the discussion in this chapter is based on relatively small fluctuations in economic activity compared with the current shock; a simple linear interpolation from past trends to the current context could lead to mistaken complacency regarding the stability of remittances flows. Futhermore, as Box 2.2 makes clear, variability is not merely a question of home and host pairings but also movements in relative exchange rates.

Remittances can be stablising for home economies. However their impact is very dependent on the relevant migration corridor and policy decisions should reflect this

This chapter has sought to sketch out some of the characteristics of the modern migration phenomenon. As always, the headline numbers conceal a more varied reality and in migration this is compounded by the difficulty of including the many irregular migrants, who – by definition – are undocumented. Careful work with national censuses has proved revealing and this can be updated with annual flow data to form a better picture in the long gaps between census rounds. Resolved at greater level of detail, migration proves to have different aspects along each migration corridor. Most migration may have an economic motivation at its heart (even family reunification, for example, relies on there having been a "prime mover" in the first place). How that finds expression though is diverse in terms of who goes, where they go, what they do when they get there and how long they stay. Policy makers must be alert to the risk of applying a "one size fits all approach". The migrant who returns home is probably not given enough weight in any analysis, and this is a group that will be seen more and more given the increasingly "transnational" approach to life adopted by migrants.

One very apparent sign of these stocks of migrants round the world is the remittances they send home – with great reliability and in apparently ever increasing amounts, though both of these characteristics may be tested by the current crisis. Remittances are important to the families that receive them. The fact that the overwhelming majority of the money is spent on immediate needs is eloquent testimony to this. Such expenditure is sometimes seen as wasted in a development sense, but to do so may be to fail adequately to take into account how families may be building their human and social capital as a result. Perhaps government is best seen as an enabler or influencer here.

This *Outlook* does not set out to suggest a migration policy. Rather it asks how policy can respond to the migration (inward and outward) that it finds around it. The following chapters will now look at this in detail.

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NOTES

1. It would be interesting to plot emigration rates against the difference in wages between countries of origin and countries of destination, since the purpose is to illustrate the responsiveness of emigration to earnings opportunities. Such a graphic would require substantially more data, given that emigrants from any given country typically go to many destinations, requiring that the wage differential be a weighted average of the relevant wage differences; unfortunately, for many countries in the figure data on the relative importance of various destinations is not readily available. The emigration rates reported in the table refer not to the overall level of emigration from each country, but only to the portion of the country's population that emigrates to OECD countries. Therefore, to see the "income differential" that might motivate emigration decisions, one can consider the difference between a given country's income per capita, and the average income in OECD countries. Thus the further a point is to the left, the greater the income differential between the country of origin. The average income for OECD countries in 2000 was approximately USD 23 000, on a PPP basis. The log of this is 4.4, which is indicated in the graph by a vertical line.

2. Hatton and Williamson (2009) projects that the relative share of sub-Saharan Africans in global human mobility can be expected to rise in the next two decades as emigration rates in currently high-emigration zones of the developing world slow, and even decline.

3. Migration flows between the Democratic Republic of the Congo and its African neighbours are substantial (both immigration and emigration); indeed, the DRC is among the most important sources and destinations in the international migration of Africans. This is a reminder that flows from developing countries to OECD countries are only part of the story of international migration. See Lucas (2006) for evidence on intra-African migration, which dwarfs African migration to other continents; a stark contrast to the Latin American pattern, where "South-South" flows are small in comparison to "South-North" flows.

4. The Caribbean region is defined as the 15 CARICOM countries (Antigua and Barbuda, The Bahamas, Barbados, Belize, Dominica, Grenada, Guyana, Haiti, Jamaica, Montserrat, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Suriname, Trinidad and Tobago) plus Cuba and the Dominican Republic.

5. The authors attempt to control for "positive selection" of migrants: unobserved differences between migrants and non-migrants such as entrepreneurship or risk-aversion, which might of themselves inflate the observed wage difference between the two groups. In this effort they are aided by an ingenious study by McKenzie *et al.* (forthcoming), which looked at earnings of Tongans who had applied to a New Zealand lottery-based immigration programme. They found that Tongans who won a place in the New Zealand labour market saw their earnings rise by about 500%.

6. EFE, "Panamá y Costa Rica firman acuerdo para controlar migración indígena panameña", 16 May 2009.

7. Associated Press, "US-Mexico border fence almost complete", 27 January 2009.

8. For Spain, Gabinet d'Estudis Socials (2007) considers various estimates of the undocumented immigrant population, which range from 440 000 (the government estimate) to 1.6 million (the estimate of the conservative opposition). The basic approach is to compare the numbers provided in the *Padrón Continuo* of the National Statistics Institute (a form of continuously updated census drawn from municipal registers), with estimates of the documented population (from social security records, for example).

9. Hanson and Spilimbergo (1999), for example, use detentions at the border as a measure of the level of immigration-policy effort in a paper studying the mutual sensitivity of wages in the United States and Mexico. Also see OECD (2007*a*, pp. 47-49) for a discussion of various estimates of unauthorised immigrant populations in certain OECD countries.

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10. See also Hanson (2006) for an extensive discussion of the phenomenon, and Smith (2009) for an assessment of recent statistics.

11. Zero return is a simplifying assumption. If a certain proportion of unauthorised migrants returns home every year – as is almost certainly the case – then the gross annual inflow required to produce the growth in the stock reported in Table 2.2 would have to be even higher than the back-of-the-envelope figures presented here.

12. This section draws substantially on OECD (2008*b*), pp. 18-21; see also Massey *et al.* (2006). Temime (2007) provides a useful taxonomy of different modes of female migration based on the history of immigration in France. The lone male worker who sends for his wife and family at a later date, like that which characterised migration from the Italian Piedmont and Liguria to the Mediterranean Midi in the mid-19th century, would imply a highly masculine sex ratio among early migrants. On the other hand, Polish migration to France in the 1920s was sometimes a matter of an entire village moving: this would imply a sex ratio identical to that observed in the society of origin.

13. For instance, Arif (1996) found that in Pakistan individual human-capital characteristics were more valuable than economic factors (such as savings) in helping return migrants find employment upon return. Similarly, Thomas (2008) found that in Uganda returning migrants with university degrees or vocational credentials were more likely to find employment than non-migrants and immigrants.

14. Chevannes and Ricketts (1997), for Jamaica, is an early example of this research literature, highlighting the relevance of the social and economic environment. Evidence on the impact on entrepreneurship can be found in Kule *et al*. (2002), Kilic *et al*. (2007) and Piracha and Vadean (2009) for return migrants to Albania, McCormick and Wahba (2001) for Egypt, Black *et al.* (2003) for Ghana, Arif and Irfan (1997) and Ilahi (1999) for Pakistani, and Mesnard and Ravallion (2006) for Tunisia. Colton (1993) reviews some of the (institutional) difficulties in attempting an occupational change for return migrants in Yemen. Finally, Radu and Epstein (2007) show that for Romania return migration can be seen to influence the activities of returnees in three ways: income premiums, switches in occupations and increased entrepreneurship.

15. The exception is Chile for which the remittance data reported here include Compensation of Employees, given that these items are not further analysed in the Chilean balance of payments statistics.

16. The simple correlation coefficient for 2007 is -0.77 which is statistically significant at conventional levels.

17. This argument is laid out theoretically by Dasgupta (1993, section 9.7) for the case of nutrition. The premise that early negative shocks to childhood consumption have long-term effects on health, and presumably labour productivity, is shown empirically in a long-term panel study by Hoddinott and Kinsey (2001). It follows that early childhood consumption of nutrition is an investment, if initial levels of consumption are below an adequate threshold.

18. This result holds if the trends in the data are removed.

19. See, for example, IMF (2005) Chami *et al.* (2008) and Buch and Kuculenz (forthcoming).

20. The Spearman correlation coefficient between the rankings of countries reported in Figure 2.14 and Acosta *et al.* (2008*b*) is 0.8.

STATISTICAL ANNEX

Table 2.A1. Stock of migrants by region of origin and country of residence
(Persons aged 15 or over, circa 2000)

		Region of origin						
Region/country of residence		**Africa**	**Asia**	**Europe**	**North America**	**Oceania**	**Latin America and Caribbean**	**Other and unknown places of birth**
Latin America and Caribbean	Argentina	1 775	27 918	426 156	8 944	597	969 193	22 939
	Bolivia	.	2 560	6 010	3 670	240	50 300	
	Brazil	14 840	115 295	381 249	10 269	351	128 469	686
	Chile	1 233	7 322	30 468	7 834	1 222	112 175	2 375
	Colombia	457	4 313	11 606	7 350	269	50 450	1 983
	Costa Rica	116	4 250	7 623	7 750	49	225 541	
	Dominican Republic	218	2 260	8 106	2 255	29	69 454	
	Ecuador	273	3 505	10 467	7 096	173	64 571	858
	Honduras	25	978	1 153	2 318	12	17 616	348
	Mexico	809	9 877	44 678	112 192	631	73 089	186
	Nicaragua	35	388	1 506	1 929	9	17 454	1 207
	Panama	254	15 567	5 624	3 873	87	48 332	
	Peru	316	6 805	16 338	6 821	557	29 431	
	Paraguay	193	7 223	5 377	2 077	39	129 773	
	Salvador	24	523	1 272	2 308	16	25 940	11
	Venezuela	2 230	33 820	200 750	7 840	.	900 480	12 750

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		Region of origin						
Region/country of residence		**Africa**	**Asia**	**Europe**	**North America**	**Oceania**	**Latin America and Caribbean**	**Other and unknown places of birth**
OECD countries	Australia	166 094	1 043 140	2 098 131	70 356	407 047	74 278	1 169
	Austria	22 397	59 036	823 133	7 625	1 770	9 731	
	Belgium	232 434	62 280	689 183	14 141	1 259	19 992	13
	Canada	277 500	1 886 860	2 306 685	246 360	50 010	587 470	325
	Czech Republic	1 787	20 690	405 833	1 983	296	1 446	4 931
	Denmark	26 026	96 503	177 736	9 652	1 855	7 529	
	Finland	8 075	15 130	83 505	3 550	615	1 555	
	France	2 745 341	432 843	2 282 800	48 500	5 566	85 148	
	Germany	177 560	965 858	5 370 220	39 080	.	52 760	1 226 481
	Greece	50 957	83 830	807 861	31 021	20 032	6 210	
	Hungary	1 775	10 297	259 702	2 493	212	1 015	
	Ireland	21 525	24 957	258 915	17 988	6 405	2 928	270
	Italy	407 470	188 783	1 119 202	67 993	18 035	219 451	
	Japan	5 069	868 649	27 148	39 973	8 061	193 467	
	Luxembourg	5 326	3 635	117 318	1 120	119	1 367	876
	Mexico	809	9 877	44 678	112 192	631	73 089	186
	Netherlands	213 944	323 352	529 479	14 122	8 661	291 372	39 010
	New Zealand	30 021	153 246	270 240	17 892	148 563	4 131	
	Norway	28 932	93 160	153 126	15 077	1 376	13 836	416
	Poland	1 998	9 645	703 419	5 799	336	1 056	15 480
	Portugal	332 393	15 689	159 686	10 391	856	66 917	
	Slovak Republic	274	1 443	110 351	854	41	212	
	Spain	372 120	79 300	715 020	19 880	3 660	724 940	
	Sweden	56 470	224 730	579 695	13 695	3 140	56 100	
	Switzerland	61 628	93 513	1 131 246	24 527	4 191	50 061	89 019
	Turkey	4 349	71 926	1 033 359	10 752	1 905	.	8 261
	United Kingdom	762 575	1 475 375	1 552 005	193 335	156 804	324 096	39 276
	United States	838 233	7 831 800	5 429 571	868 809	255 638	16 165 286	579

Source: OECD Development Centre calculations based on OECD (2008*b*), Database on Immigrants in OECD Countries and the 2000 round of national censuses in Latin America (Processed with ECLAC Redatam+SP online).

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Table 2.A2. Stock of Latin American and Caribbean Migrants by Country of Destination
(Persons aged 15 or over, circa 2000)

		Country of origin										
Region/country of residence		**Argentina**	**Bolivia**	**Brazil**	**Chile**	**Colombia**	**Costa Rica**	**Cuba**	**Dominican Republic**	**Ecuador**	**El Salvador**	**Guatemala**
Latin America and Caribbean	Argentina		214 338	32 212	207 380	3 457	218	2 355	1 295	1 827	165	189
	Bolivia	12 810		10 320	3 710	1 040	200	560		490		
	Brazil	25 759	19 231		16 070	3 357	229	1 076	143	1 045	481	135
	Chile	35 057	10 527	5 958		3 735	426	2 954	241	7 879	217	207
	Colombia	2 048	555	1 457	1 395		454	1 392	242	9 332	264	271
	Costa Rica	983	244	363	1 231	4 959		3 830	717	832	8 282	1 738
	Dominican Republic	664	78	254	547	1 281	353	1 973		241	87	130
	Ecuador	1 891	537	936	4 274	45 346	306	1 136	127		199	149
	El Salvador	167	35	192	188	455	657	106	49	92		6 057
	Honduras	117	95	153	195	540	482	421	88	312	5 742	2 602
	Mexico	5 886	1 277	1 929	3 410	5 525	1 804	6 266	744	1 105	5 282	21 578
	Nicaragua	137	39	91	98	328	3 006	717	45	79	1 711	731
	Panama	704	165	659	968	19 118	3 746	1 541	5 109	1 709	1 925	509
	Paraguay	45 877	921	73 681	2 125	280	32	230	13	86	33	31
	Peru	4 611	4 091	3 506	4 234	4 373	219	768	138	2 829	82	124
	Venezuela	8 230	1 820	3 770	14 980	581 060	1 160	8 650	13 060	27 200	870	410

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		Country of origin										
Region/country of residence		Haiti	Honduras	Jamaica	Mexico	Nicaragua	Panama	Paraguay	Peru	Uruguay	Venezuela	Others Latin America and Caribbean
Latin America and Caribbean	Argentina	77	138	14	2 774	191	342	305 557	79 757	114 291	2 375	241
	Bolivia		280		8 190			2 160	8 390	350	460	1 340
	Brazil	14	126	17	1 110	451	496	22 637	10 095	24 226	1 649	122
	Chile	45	226	22	1 528	237	486	954	35 588	2 131	3 423	334
	Colombia	84	240	40	1 681	442	1 166	150	3 687	315	23 939	1 296
	Costa Rica	49	2 623	159	1 990	184 887	8 386	57	2 596	224	887	504
	Dominican Republic	56 583	102	126	440	100	111	14	544	377	3 091	2 358
	Ecuador	36	144	16	781	148	330	90	5 114	366	2 367	278
	El Salvador	4	9 355	8	1 284	6 282	371	10	184	64	197	183
	Honduras	31		18	809	5 138	239	22	250	42	57	263
	Mexico	331	3 351	78		2 391	1 508	177	3 492	1 245	2 372	3 338
	Nicaragua	20	9 083	16	611		273	5	178	30	115	141
	Panama	279	745	521	1 844	4 588		28	2 476	237	751	710
	Paraguay	1	23	2	1 728	22	36		1 483	3 009	112	48
	Peru	36	122	5	1 119	134	228	339		446	1 827	200
	Venezuela	1 580	190	130	2 670	1 850	1 020	220	32 720	4 880		194 010

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		Country of origin										
Region/country of residence		Argentina	Bolivia	Brazil	Chile	Colombia	Costa Rica	Cuba	Dominican Republic	Ecuador	El Salvador	Guatemala
OECD countries	Australia	10 236	442	4 185	22 466	3 729	117	225		1 101	8 786	86
	Austria	844		2 407	804							
	Belgium	1 288	581	3 281	3 341	2 132	127	582	878	1 036	206	397
	Canada	12 710	2 265	12 455	24 235	15 830	2 160	4 900	4 525	10 670	36 975	12 525
	Czech Republic	299	42	102	28	66	8	476	5	35	13	7
	Denmark	931	103	1 419	1 260	787	82	214	74	274	40	61
	Finland	170	50	250	200	105	25	125	35	20	20	10
	France	9 127	938	13 082	9 864	9 196	350	1 562	327	1 142	698	678
	Germany											
	Greece	605	15	1 968	388	364	24	187	141	42	33	30
	Hungary	110	23	136	92	54	9	296	10	39	1	1
	Ireland	219	18	1 116	147	102	12	111	6	27	21	21
	Italy	48 755	1 745	34 848	7 921	12 888	647	8 224	12 892	12 155	3 620	956
	Japan	1 963	2 200	157 870		1 324						
	Luxembourg	109	11	440	116	92	5	26	147	19	2	10
	Mexico	5 886	1 277	1 929	3 410	5 525	1 804	6 266	744	1 105	5 282	21 578
	Netherlands			2 088								
	New Zealand	378	102	612	705	186						
	Norway	479	148	1 282	5 522	2 119	128	336	243	273	61	201
	Poland	183	21	216	18	57	6	156	3	33	3	
	Portugal	959	46	45 185	170	331	14	358	34	195	23	22
	Slovak Republic	58	5	9	5	10	3	61	4	2		4
	Spain	92 680	12 360	29 280	15 520	143 500	1 200	45 200	36 800	190 040	1 800	1 440
	Sweden	2 360	2 195	3 345	26 195	5 750	225	1 505	265	1 115	2 210	495
	Switzerland	4 765	1 123	12 974	4 910	4 633	387	1 062	4 480	1 403	359	392
	United Kingdom	6 450	1 027	13 992	4 756	10 850	328	1 013	439	2 406	405	294
	United States	120 777	50 093	199 585	75 843	472 027	68 068	851 669	633 267	280 542	775 004	446 094

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Region/country of residence		Haiti	Honduras	Jamaica	Mexico	Nicaragua	Panama	Paraguay	Peru	Uruguay	Venezuela	Others Latin America and Caribbean
		Country of origin										
OECD countries	Australia	15	32	536	889	539	28	145	5 054	9 176	847	5 644
	Austria				628				817			4 231
	Belgium	927	77	204	1 014	107	90	170	1 655	335	540	1 024
	Canada	49 690	3 950	116 370	37 470	9 050	2 325	4 970	16 550	6 010	7 090	194 745
	Czech Republic	21	2	4	67	16	9	31	66	34	42	73
	Denmark	47	66	119	471	91	39	39	532	186	381	313
	Finland			40	145	35	15	5	170	50	40	45
	France	18 717	431	374	5 205	395	326	661	5 752	1 588	2 800	1 935
	Germany											52 760
	Greece	29	31	52	332	26	130	47	157	115	788	706
	Hungary	1	1	6	34	7	7	8	61	36	62	21
	Ireland		3	132	267	9	12	21	138	15	69	462
	Italy	294	585	201	3 732	513	698	628	28 799	4 739	34 205	406
	Japan				1 094			1 033	27 220			763
	Luxembourg	9	2	9	54	3	8	8	144	28	72	53
	Mexico	331	3 351	78		2 391	1 508	177	3 492	1 245	2 372	3 338
	Netherlands											289 284
	New Zealand			105	210				381			1 452
	Norway		17	34	380	20	3	20	513	41	134	1 882
	Poland		3	6	102	6	24	3	96	9	54	57
	Portugal	7	10	24	193	15	92	17	190	124	18 539	369
	Slovak Republic				9	6	1	2	12	7	2	12
	Spain	300	2 620		16 580	1 020	2 120	2 100	47 900	21 780	60 160	540
	Sweden	75	165	205	1 170	410	200	170	4 645	2 250	485	665
	Switzerland	964	232	431	2 502	219	262	341	5 053	1 035	1 816	718
	United Kingdom	163	373	141 850	4 480	206	433	325	3 797	938	3 586	125 985
	United States	391 298	263 613	528 872	8 250 885	205 915	131 465	9 170	261 922	24 655	99 232	2 025 290

Source: OECD Development Centre calculations based on OECD (2008*b*), Database on Immigrants in OECD Countries and the 2000 round of national censuses in Latin America (Processed with ECLAC Redatam+SP online).

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CHAPTER THREE

Migration, Labour Markets and Social Protection

DEVELOPMENT EFFECTS OF PEOPLE FLOWS

Are the people flows described in the previous chapter a good or bad thing? The answer may depend on whose perspective you adopt. The costs and benefits of these migration flows can be assessed from the perspective of at least three parties: migrants themselves (the focus of the previous chapter), the countries to which they migrate, and their home countries. Economic research has been almost exclusively devoted to the second of these groups, the countries of destination, and particularly those that are OECD countries; to a lesser extent, studies have looked at migrants' own experience. Furthermore, while a great deal has been said about the effects of remittances on development – a discussion reviewed in detail in the following two chapters – little has been said about the effects, economic and otherwise, of the outflow of 20-plus million people.

To understand the full development impact of migration it is necessary to look at both countries of origin and destination, and to consider the skills and work of the migrants

The overall impression from the empirical literature is that the socio-economic effects of immigration (wages and employment, basically) tend to be minor. However, these results are blurred by various composition effects, particularly skill levels: established low-skilled migrants and low-skilled natives are more prone to be affected by new migration flows. A particularly worrisome equilibrium is the one in which high-skilled migrants end up working in low-skilled activities. In this "lose-lose-lose" situation, the home country loses human capital (the "brain drain"), the host country and the migrant are not fully employed ("brain waste", or skill mismatch in the jargon of labour economics), and low-skilled workers in host countries (both earlier migrants and natives) can find themselves excluded from the market. Focusing on the home country, the (still scarce) microeconometric literature for emerging countries shows positive effects, both in wages and future human capital accumulation, at the expense of immediate brain drain.

The chapter surveys the effect of Latin American people flows, first on the societies and economies of migrants' countries of origin, followed by a consideration of the effects on host countries[1]. The lens through which we study these effects is that of labour markets and social protection. Indeed, employment is the nexus of well-being for most people in the world and, despite the considerable attention to the potential impacts of remittances back home, one would look first for impacts of migration through this channel. The related question of social protection networks, in particular their coverage and portability, is highlighted. A third section then discusses the prospects for migration flows and forward-looking policies in the context of the current global economic crisis.

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THE "FORGOTTEN" SIDE OF MIGRATION: ECONOMIC IMPACTS IN HOME COUNTRIES

Starting from the logic of economic textbooks, what would we expect the effects of emigration to be in a perfectly functioning and complete labour market? Economic theory suggests that when the supply of one good decreases its price increases, other things being equal. Thus if – perhaps through migration – there is a decrease in the number of individuals looking for jobs on the labour market, wages would be expected to rise. The real-world effect is more complicated, however, for example because those migrants may take with them their savings, implying some simultaneous drop in the demand side of the labour balance.

Besides, emigration is not a homogeneous phenomenon, especially in developing countries. People are not removed from the local labour market in a random fashion. For instance, if migrants tend to be those with lower abilities, average wages in the home country may rise simply due to a composition effect – rising because on average the pool of remaining workers is more highly skilled than before. While increasing wages and employment levels may seem like a good outcome for development, emigration may also mean detrimental formal labour shortages and quantitatively important levels of brain drain. A further complication is that labour markets never work the way they do in textbooks, not just because of heterogeneous nature of labour inputs (for example particular skills), but also owing to labour market institutions such as wage-bargaining arrangements, union power or employment-protection legislation.

Latin American Labour Markets

Informality in its labour markets is a particular factor to be taken into account in Latin America...

In order better to understand the empirical effects of migration in Latin American and Caribbean economies, it is necessary first to sketch some of the characteristics of their labour markets. A salient feature is the high level of informality. Leaving aside the difficulties in measuring or defining informality (see OECD, 2008*a*, and Jütting and de Laiglesia, 2009), informal employment accounts for more than 50% of total non-agricultural employment in Latin America, ranging from 75% in Ecuador and 68% in Peru, to 38% in Colombia and 36% in Chile. The extent of informality in a country is related in part to lower per capita income, but as Figure 3.1 shows, this does not explain everything. For instance informality in Argentina and Ecuador is nearly 20 percentage points higher than their per capita income would imply.

It is fair to say that not all informal workers are poor and unproductive (nor do they all work outside the legal or indeed the formal economy). Nor are they all excluded from the formal sector; some of the informality observed responds to a voluntary exit, not to an exclusion[2]. Even so, many of them do lack adequate employment protection and social safety nets, being more prone to fall into poverty when they get sick, lose their job or retire. How should a government pursue its migration policy when as much as half of the economy is informal? Informality is, above other considerations, a constraint for many of the policies discussed in this chapter (portability of social rights does not matter for those who have no access to them; increasing the burdens of formality may stimulate the flow to informality).

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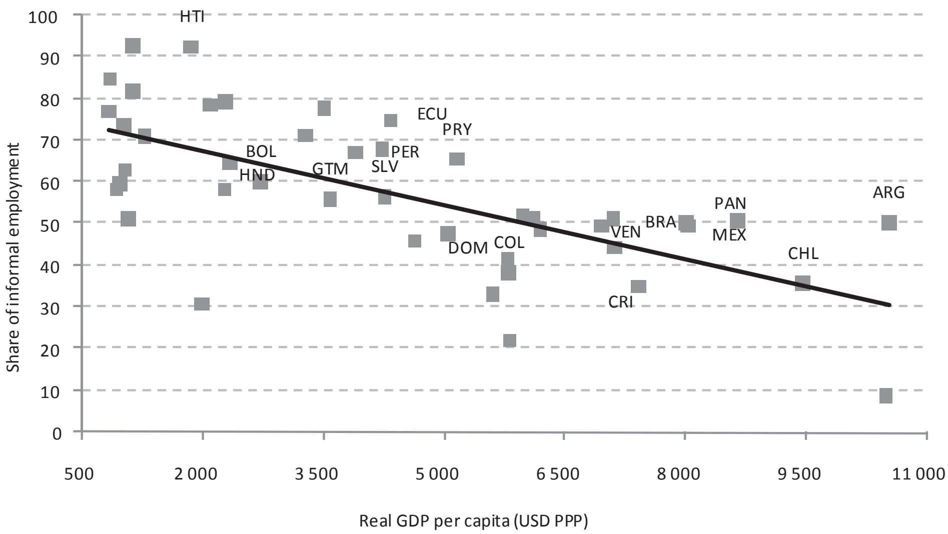
Figure 3.1. Informal Employment and GDP Per Capita, Around Mid-2000s

(Percentage of informal employment in total non-agricultural employment in emerging countries)



Source: Jütting and de Laiglesia (2009).

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…as is the region's "demographic bonus" – its relatively high proportion of working age people

Another key element that should enter the analysis of migration in Latin America is the so-called "demographic bonus". According to the latest projections of the United Nations, Latin America is in the second stage of its demographic transition, in which the ratio of dependants (defined as people under 15 and over 60) to working-age population is low and decreasing (ECLAC, 2008). The region will enjoy this demographic bonus during the next two decades; Cuba and Chile for a shorter period, while Guatemala or Bolivia may expect to benefit for more than 50 years. The net increase of potential workers created by the demographic bonus (projections already take into account net migration flows) can offset some of the labour consequences of migration such as labour shortage and upward pressure on wages. Moreover, this development may reduce expenditure pressures from primary education and so free budgets for the spread of secondary education, offsetting brain drain and solving one of the main challenges of the region.

What does the literature actually show about Latin American labour markets when people leave or circulate? Given that the body of research on this aspect of the migration phenomenon is still rather thin, we draw upon studies from throughout the developing world, and not only for the region. Moreover, much of the evidence discussed here is microeconomic in nature, so any generalisation to other economies or to the macroeconomic level should be taken with caution. Nevertheless, these studies provide a rich inventory of explanatory mechanisms for understanding the links between migration and employment outcomes.

Left Behind: How Does Outward Migration Affect Wages?

The handful of economic studies that address the impact that migration has on wages in developing countries focus on labour supply (labour-market participation) and productivity. Mishra's (2007) study of the impact of emigration from Mexico to the United States on Mexican wages finds that emigration has had a strong

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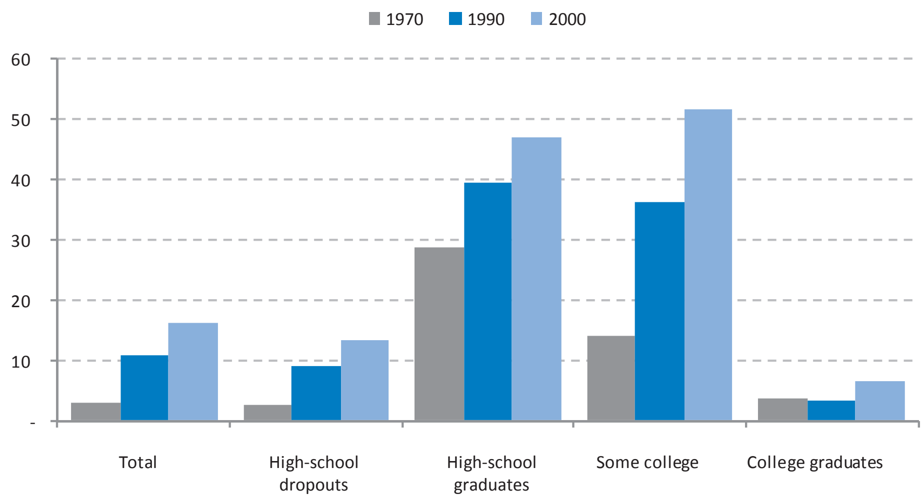
and positive impact on wages. Considering several groups of Mexican workers, distinguished by level of schooling and work experience, she finds that if one such skill group declines in size by 10% as a result of emigration, the average wage for remaining workers in that group rises by about 4%. Based on these elasticities, between 1970 and 2000 emigration to the United States increased real Mexican wages by some 8%. This increase was higher for the better educated and more experienced because proportionately these groups had higher outflow. Figure 3.2 shows a cumulative emigration rate of 16% in 2000, which includes 52% of those who attended some college. This distributional effect explains part of the increase in wage inequality in Mexico over the same period.

Figure 3.2. Impact of Emigration on Labour Supply in Mexico, by Level of Schooling

(Emigrants as a percentage of workers in Mexico)



Source: Mishra (2007).

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Emigration can prompt strong rises in wages for those who stay behind and can encourage the economic empowerment of women

Emigration inevitably leads to adjustments in labour markets back home, which can be difficult to predict. For example, the emigration of the high-skilled might increase unemployment for the low-skilled, if it means the loss of the entrepreneurs associated with the expansion of labour-intensive industries (Chaudhuri, 2005)[3]. These adjustments may have a great deal to do with gender, too. Carletto and Mendola (2008) find that male and female participation in the labour market in Albania respond differently to current and past migration episodes of people in the household. If a household member is abroad, women work less in the labour market for pay, and increase the time devoted to unpaid work. On the other hand, women whose household members have been abroad in the past are significantly more likely to be self-employed and less likely to perform unpaid work. These patterns are not observed among men. These findings suggest that over time Albanian emigration – which is male-dominated – may lead to women's economic empowerment.

In some settings in developing countries – remote or rural regions, for example – labour markets may be virtually non-existent. If labour markets are missing in this sense, labour lost to migration cannot be replaced by hired labour; thus, the consequences of migration may be severe for labour-constrained rural households in particular. But, at the same time, migration may complement productivity growth in the agricultural sector by substituting for other missing markets, such as markets for credit or insurance. Remittances can provide working capital and migrants' earnings in distant labour markets provide a form of insurance, as they are uncorrelated with local, often weather-related, risk. The net impact of emigration in the context of many missing markets will depend on the relative magnitude of all these effects, including labour shortages[4]. For rural Mexico, evidence shows that mass migration of members of agricultural households to the United States has raised land marginal productivity (Taylor and López-Feldman, 2007).

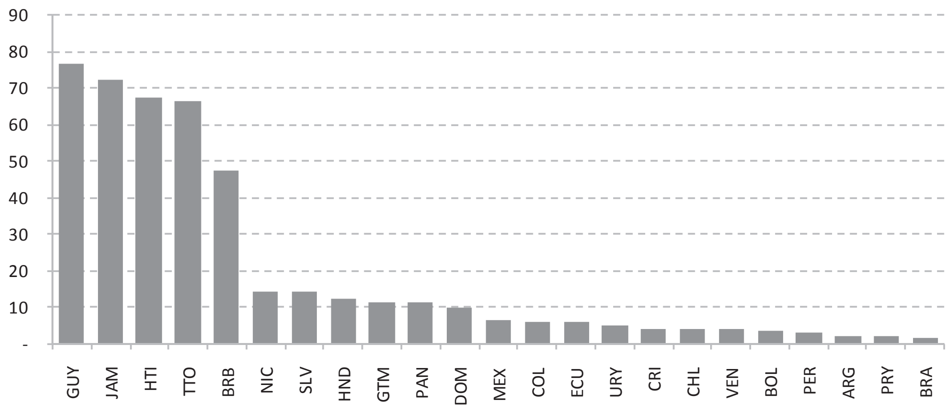
Is Brain Drain Robbing Latin America of Its Most Skilled People?

Figure 3.3 shows the rate of emigration to OECD countries of people with a university education for all Latin American and Caribbean countries for which data are available. (Mexico, which is in both the OECD and Latin America, is included both as a source and a destination. This is the case throughout this *Outlook* except where otherwise noted.) The numbers in the figure correspond to the share of people with university-level education who reside in OECD countries. To put these in context a simple unweighted mean of these brain-drain rates for *all* countries for which data are available is about 15%; the rate for the United States is 0.4%; for the United Kingdom it is 10.3%; for France 4.2%.

Emigration's effects may be more negative for labour-constrained households or where it represents a loss of skilled labour. This "brain drain" is very marked in the Caribbean

Figure 3.3. Emigration Rate of University-Educated to OECD Countries, 2000

(University-educated emigrants in OECD countries as a percentage of total number of university-educated nationals from the home country)



Source: OECD Development Centre calculations based on data from Barro and Lee (2000) and the OECD Database on Immigrants in OECD Countries (OCDE, 2008*b*).

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By this measure, few South American countries are truly hard hit, in stark contrast to the Caribbean countries, many of which have brain drain rates in excess of 50%. These are among the highest observed rates of skilled emigration in the world. The next group down are the poorest of the Central American countries. In many cases, of course, high rates of brain drain reflect small numbers of highly educated people to begin with. To illustrate this starkly, it would not be alarming if two university graduates from a small country were to emigrate; but in an economy with only three university graduates, that would imply a staggeringly high rate of loss. Small numbers of university-educated nationals

– "brains" – overall, in turn, might arise from at least two factors. It may be that the population as a whole is small to begin with. Or it may be that the economy is poor and cannot provide higher education to many of its citizens. Both factors are at work in many of the highest ranked countries in Figure 3.3, though not always to the same degree. In Guatemala, with a brain drain rate of 11%, the poverty factor is more important than the population effect; in Barbados, with a rate of 47%, the reverse is probably true.

Brain drain may be a symptom as much as a cause of development problems. And it may bring benefits in terms of incentives to education and skills transfer

Surely these numbers provide cause for concern for policy makers in those countries worst affected, given that every doctor, nurse, teacher or engineer who leaves reduces the resources available at home to confront important development challenges, before adding the losses of positive externalities and tax revenues from educated workers, and the (sunk) opportunity cost of public funds spent in their instruction. But there is growing debate about the magnitude of the harm that might be done to developing countries by this brain drain. Some argue, for example, that it brings benefits. The prospect of emigration may raise the incentives to pursue an education, for example[5]. If not all brains leave, and if there are spill-over effects from the number of brains who remain at home, there may be economic gains for the home country in terms of growth or increased productivity. The highly skilled abroad, meanwhile, may benefit their home country through the remittances they send home (the subject of Chapter 4 of this *Outlook*) or the trade and investment channels that they can access. As such, the potential value of links with emigrants may outweigh the costs. The authors of a study on India dub the latter the "optimal innovator diaspora"; they find that the emigration of innovators in India harms local knowledge access (on average), but that the innovator diaspora transfers important knowledge back home (Agrawal *et al.*, 2008). We will come back to this point later. Others argue that the costs of the brain drain might be simply overstated. That is not to deny crises in the provision of certain public services, such as health care, but rather to argue that the underlying cause is not always limited to emigration. Nurses, for example, may be working in a sector other than health care at the point they emigrate. The problem in that case is not brain drain but a health-care sector that cannot retain trained people. These are important debates but there is little consensus regarding the true burden of the brain drain; moreover, experiences almost certainly vary widely among countries[6].

Labour-Market Effects of Remittances

Remittances fuel consumption and investment, leading to important economic effects in migrants' home economies; these effects will be reviewed in the following chapter. But remittances can also affect labour markets and employment. First, they may allow the households that receive them not to work, or to work less (or to increase what economists call "consumption of leisure" if the income-effect prevails). Remittance-receiving households appeared to reduce the amount of time worked in Nicaraguan urban areas (Andersen *et al.*, 2005). The same effect was seen for Mexican females in rural areas (Amuedo-Dorantes and Pozo, 2006), though this was not repeated among Mexican remittance-receiving households as a whole (Taylor and López-Feldman, 2007)[7]. Andersen *et al.* (2005) concluded that remittances reduce vulnerability to poverty as long as they do not become the dominant source of income. Remittances may additionally allow household members to work in different ways, perhaps considered informal but nonetheless central to the household economy (such as home production)[8].

Remittances may also allow household members left behind to invest in education rather than working, which will make those individuals – and potentially the household and the economy as a whole – more productive. Such an effect may

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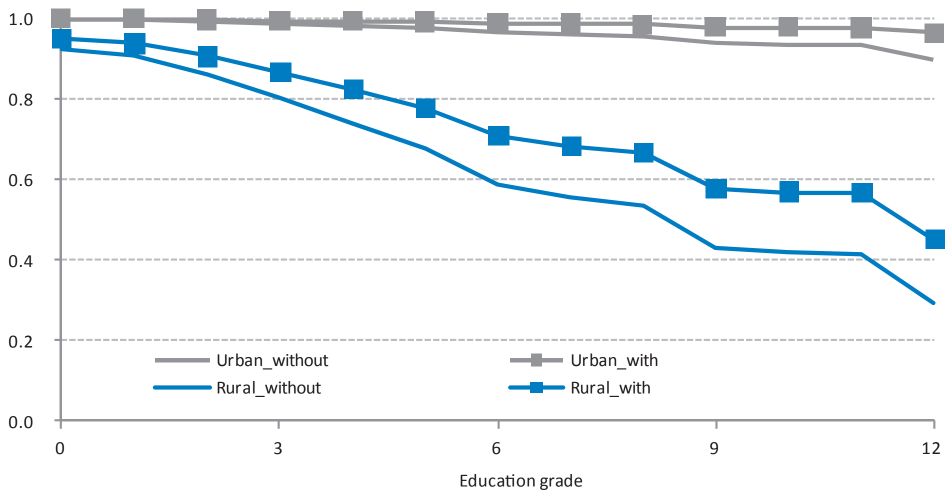
be interpreted as an inter-temporal change in human capital stock: a present loss due to emigration in exchange for a future increase thanks to longer schooling financed by remittances. Figure 3.4, taken from Cox and Ureta (2003), shows that children in remittance-receiving households in El Salvador are substantially more likely to remain in school longer[9]. The propensity to complete secondary education (grade 12) is dominated by a rural/urban divide, but the ratio rises 7 percentage points in urban areas (from 89 to 96%), and 16 points (from 29 to 45%) in rural ones where the family receives remittances. In Ecuador, too, receipt of remittances is associated with higher levels of school enrolment and lower levels of child labour, especially among girls and in rural areas (Calero *et al.,* 2008). Cardona Sosa and Medina (2006) for Colombia, and López-Cordova (2005) for Mexico reach similar conclusions.

These encouraging results are not universal, though. For example, Mexican adolescents who live in households with a migrant abroad are less likely to finish junior high school (for boys) and high school (for boys and girls alike). The effect is weaker for the very poorest households with migrants abroad, but for the majority of rural Mexican children, family migration depresses educational attainment (McKenzie and Rapoport, 2006). In the case of Mexican migration, dominated by low-skilled flows to the United States, migration may send a signal to family members back home that is the *opposite* of the brain-gain hypothesis: namely, that migration and higher earnings abroad do not require much schooling. At the same time, migration accompanied by insufficient or absent remittances risks increasing child labour, since children may have to make up the income lost to the household, as shown for Haiti (Amuedo-Dorantes *et al.*, 2008).

Remittances may reduce participation in the formal labour market. They may boost education (though migration opportunities may pull in the opposite direction) and are an important source of capital for micro-enterprises

Figure 3.4. Probability of Staying in School in El Salvador, With and Without Remittances



Source: Cox and Ureta (2003).

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Finally, if remittances are invested in the development of micro-enterprises, they can increase employment opportunities for working people who remain back home, either by creating jobs or by increasing productivity and the earnings associated with existing jobs. On balance, however, remittances appear to give rise to little job creation, although they may be an important source of investment in micro-enterprises. In Mexican rural regions, remittances spent on land, cattle and tools allow rural households to continue their farming activity and

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thereby improve their standard of living. While only 5% of Mexican remittances are invested in small businesses (Coronado, 2002), this nevertheless accounts for a fifth or more of the capital invested in those businesses (Orozco, 2003; Woodruff and Zenteno, 2001).

Diasporas and Transnational Migrant Entrepreneurs: Networking Brains

Diasporas can be a source of contributions to home countries beyond remittances, through the transfer of intangible resources, such as ideas, know-how and capabilities[10]. Keeping one foot in their country of origin, diasporas represent a potential source of benefits for both host and home countries, especially when its members develop entrepreneurial activities with links to their origin country, becoming "transnational migrant entrepreneurs".

Migrant communities can be an important source of ideas as well as money. The region contains good examples of initiatives to harness these

These transnational migrant entrepreneurs mitigate the effects of brain drain – to some extent at least – by knowledge transfer to their country of origin. This transfer may occur through the ownership of business in their homeland, through trading contacts or simply through return visits. Portes *et al.* (2001) concluded that compared to domestic entrepreneurs and salaried employees, transnational entrepreneurs consistently engaged in activities which required regular cross-border contacts such as importing or exporting goods – so integrating their country of origin with global markets – or managing firms with local workers.

This transnational approach seems potentially relevant for Latin America. The latest National Immigrant Survey in Spain (Instituto Nacional de Estadística, 2007), shows that Latin American migrants are the migrant group which keeps most contact (by phone, mail and email) with their countries of origin (nearly 94% of the Latin Americans polled reported regular contact with family and friends in their origin country). In the United States, Latin American migrants also keep contacts, but to a lesser degree: 63% of such immigrants sent remittances, made return trips or telephoned relatives (Pew Hispanic Center, 2006).

Governments in Latin America are increasingly recognising the importance of their diasporas for the development and welfare of their countries and consequently they have opened specific channels of communication[11]. Some efforts have already been made in support of transnationals' economic activities. An example of good practice here is the network *ColombiaNosUne*, and its business sub-network *ColombianosNegocian.* Thanks to support from the Colombian government, this network serves "as interface between Colombians living abroad, Colombian firms operating abroad and domestic Colombian firms promoting business, tourism and investment opportunities". At present, this network has contacts in 71 countries, and incorporates more than 3 200 firms. In Argentina, the government through its network ECODAR (*Encuentro de Cooperación Diáspora Argentina*), jointly with the World Bank, is developing the project *Mendoza Emprende*, helping young Argentinians to transform their innovative ideas into concrete business projects. The Chilean government, through its network *ChileGlobal*, also seeks "to leverage the international experience, the ideas and the contacts of members of the network, in order to attract business opportunities and to promote knowledge and know-how transfer".

A Silver Lining to the Economic Downturn: Reversing Brain Drain?

One option open to country-of-origin governments, either on their own or with the co-operation of international organisations, may try to promote circular or

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return migration of their skilled nationals, as a way to remedy brain drain. These programmes date back to the 1960s, when Chinese Taipei and Korea started to offer research facilities and high salaries to those of their emigrants with skills in science and technologies. Other Asian economies, China and India notably, are now emulating these schemes, on a larger scale (Newland *et al.*, 2008).

Since the 1980s, Latin America has been establishing a network of official institutions and programmes to pursue the same goal. The National Science and Technology Council and the *Repatriación y Retención* programmes in Mexico, the National Commission for Repatriation and the Programme for the Development of Basic Sciences in Uruguay, or the National Council of Scientific and Technological Research and the National Commission for the Return of Argentinians Abroad in Argentina follow the same basic strategy (other examples are summarised in OECD, 2008*c*). Based on financial incentives (for moving and start-up costs, competitive local wages and soft loans for innovative enterprises) and infrastructure guarantees (in the institutions that hire those professionals), these policies may reverse some of the costs from brain drain.

Migrant communities can also be a fertile recruiting ground for skilled workers. The current crisis may present an opportunity here

Could this be a collateral benefit of the crisis, a reverse flow from OECD countries of managers and engineers who might be highly productive in the economic recovery in Latin America and the Caribbean? Unfortunately, neither hard data nor assessments of these reinsertion programmes are available so it is difficult to say how useful such incentives would be in the current context. Moreover, these "assisted return" programmes can be criticised on the grounds of equity: why make special benefits available to a Uruguayan MBA-holder recently laid off on Wall Street, but not available to a Uruguayan MBA-holder who has just been laid off in Montevideo?

THE ECONOMIC IMPACT OF MIGRATION IN HOST COUNTRIES

Ongoing controversy surrounds the effects of people flows on the economies of destination. This debate is particularly lively at the moment in OECD countries with large immigrant populations from Latin America and the Caribbean. Public opinion frequently looks askance at the entry of immigrant workers, suspecting that the effect will be to reduce wages or increase unemployment (or both) among native-born workers. Such sentiments grow decidedly more acute in economic downturns.

The economic crisis has reawakened popular fears that immigration may depress wages. The reality is more complex

Their arguments are the converse of those presented earlier for countries of origin: here, economic theory suggests that an increase in the number of individuals looking for jobs on the labour market means wages may fall. If wages do not adjust swiftly, unemployment may rise. This is not the totality of the expected impact: immigrants may increase aggregate demand, thus increasing the demand for labour and offsetting the downward pressure on wages. And there will be effects both ways on public finances as well: increased expenditures as pressures rise on schooling and housing; and increased revenues as more working-age people pay into social security schemes.

My Job, Your Job: Assessing the Effect of Migration

So much for the textbook predictions; what really happens to wages, employment, unemployment and labour-force participation of native workers in the presence of

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large immigration flows? A substantial amount of research in the United States, and a growing body of work in Europe, has found that the negative effects of immigration on local labour market conditions are much harder to detect than one might suspect. This work is summarised in recent narrative surveys[12].

Complementary evidence based on meta-analysis techniques[13] is presented by Longui *et al.* (2008). They conclude, based on 45 empirical papers, that the impact of immigration on the labour-market outcomes of the native-born population is very small and in more than half the cases statistically insignificant. Their results suggest that the negative impact of immigration may be greater on labour-force participation and on employment than on wages. (In fact the effect of further immigration is only statistically significant on the wages of earlier immigrants.) In companion papers, the same authors estimate that on average a 1% increase in the share of immigrants lowers wages by about 0.12%; the effect on employment is to reduce the native employment rate by 0.02%.

The wage effect of immigration appears to be minor. In practice migrants and the native-born are often not in competition for the same jobs

In broad-brush strokes, this research finds little or no negative effect (or has to search very hard to find it) because immigrant workers do not always compete with native-born workers for the same jobs, and can be complementary (Münz *et al.*, 2006). Immigrants tend to fill labour-market gaps avoided by natives, such as jobs that are dirty, dangerous or difficult, or respond to seasonal shortages of labour (in, say, farming, road repair or construction) or fill unmet demand for skilled labour in skill- and knowledge-intensive industries (such as the IT sector). At the same time, migration usually spurs labour participation rates directly (migrants exhibit higher participation rates than natives) and indirectly (many female migrants are hired in domestic service sectors, favouring an educated female labour supply; see Oficina Económica del Presidente, 2006, or Farré *et al.*, 2009, for Spain, and Cortés and Tessada, 2009, for the United States). Finally, some migrants engage in entrepreneurial activities. In this case, not only do they fill vacancies in the job market of the host country, but they actually generate jobs (see Oliveira and Rath, 2008; and Kloosterman and Rath, 2003). In these senses, immigration contributes to labour-market efficiency.

For the United States, Card (2005) reviews the evidence regarding immigration and unemployment. The main lesson drawn is that, although immigration has a strong effect on the relative supply of labour of different skill levels, the observed relationship between immigration and the wages of low-skilled native workers is surprisingly weak. Card argues that the demand for low-skilled labour increases at the same time as immigrants enter the market, so any downward pressure on wages is mitigated (or even reversed). Moreover, these changes in the demand for low-skilled labour might be related to the presence of immigrants: employers in particular sectors (such as agriculture, the textile, apparel and footwear industries and a set of low-skilled service industries) are much less likely to adopt labour-saving technology if a large supply of unskilled labour is readily available[14]. This argument is supported by Lewis (2003) or Dustmann and Glitz (2008), who show for the United States and Germany that industries adapt their use of labour inputs and their technology to local supply.

This evidence should not be taken to mean that immigration might not increase the vulnerability (if not the wage or employment levels) of native low-skilled workers (and, indeed, of other migrants). Borjas *et al.* (2006) suggest that illegal immigration in the United States has hurt African-Americans, even contributing in part to the observed increase in incarceration rates amongst this group[15]. Nevertheless, the small size of the measured impacts, together with the huge potential gains of international migration to many parties, should encourage policy makers to target policy measures at vulnerable, low-skilled workers (native and foreign-born alike) in a more effectively organised labour mobility system.

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Do Migrants Give to the Public Purse, or Take From It?

Research has also flourished in the related area of the impact of immigration on the welfare state in host countries, notably on pension systems. The theoretical literature has focused on the political economy of migration, and results are controversial. The early literature suggested that all natives may lose from low-income migration. However, Razin and Sadka (1999) argue than all native citizens (skilled or unskilled, young or old) can be better off at the time of migrants' arrival in a dynamic context. The rationale is that even in the case most unfavourable to natives of redistributive pension systems and unskilled immigration flows (where migrants are net beneficiaries), the potential burden can be shifted forward indefinitely to following cohorts, while in the short-term, immigrants bolster public revenues.

Whether immigrants are net beneficiaries or net contributors to the public coffers remains an empirical issue, depending on immigrants' labour inclusion and characteristics (age profile and family composition, skill level, actual use of social services), immigrants' decisions (duration of their stay), and the characteristics of host country institutions (eligibility criteria and generosity of social benefits, bilateral agreements with migrants' home countries, and so on). Immigrants who are young, healthy, unmarried temporary workers tend to be net contributors to public finances as a whole, and to the pension system in particular. An accounting exercise carried out by the Spanish government (Oficina Económica del Presidente, 2006) revealed that the short-term impact of immigration on public finances had been both high and positive. Nearly half of the government surplus in 2005 in Spain (EUR 4.8 billion, 0.5% of GDP) could be attributed to the positive immigration shock, one third of it coming from Latin America (mostly from Ecuador and Colombia). Box 3.1 provides further details of the labour and macroeconomic impacts on Spain.

The impact of migrants on the public purse depends on factors such as date of arrival, national origin and length of stay...

Econometric-based evidence on immigrants` use of welfare services in the United States (for instance, Borjas and Trejo, 1991, or the references in World Bank, 2006, p.40) found that the effects on host-country public finances differed from one immigrant cohort to another (more recent immigrants use public services more), the national origin mix (black, Hispanic and Asians have higher welfare use) and the length of the time immigrants reside in the country. In sum, the literature suggests that the impact of the average immigrant, if he or she is reasonably well integrated in the host country's labour market, is positive, although not very large, and decreases over time.

The fiscal impact of unauthorised migration – which entails expensive enforcement and border control costs – is even less clear cut. The United States Social Security Administration, for example, estimates that three-quarters of unauthorised migrants working in the country are in fact declared by their employers under false or borrowed social security numbers. As such, these migrants earn at least minimum wages, and more to the point, contribute to social security. An "Earnings Suspense File" of payments to social security accounts for which the names and numbers do not match, has accumulated more than USD 500 billion and is growing by more than USD 7 billion per year (OECD, 2009*a*); analysts surmise that the biggest contributor to this public pot is the population of unauthorised migrants working in the United States.

...unauthorised migrants may contribute to the public purse by paying taxes without gaining entitlement to the corresponding benefits

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Box 3.1. Immigration Boom, Employment and Economic Growth in Spain

Spain has experienced one of the most intense immigration flows among OECD countries in recent history. Between 1996 and 2006, the immigrant population grew fivefold, reaching 4.5 million people (approximately 10% of total population and almost 15% of the labour force). This positive shock had and is still having significant impacts on the country's social and economic institutions.

A report from the Spanish government published in 2006 (Oficina Económica del Presidente) quantified the macroeconomic impact of immigration flows in Spain. Based on a growth-accounting approach, immigration could explain one-third of total Spanish GDP growth between 1996 and 2005, accounting for 1.1 of an annual average of 3.6 percentage points. The benefits were two-thirds attributable to the direct contribution of immigration to population growth (0.8 percentage points) with the balance being their positive impact on per capita GDP growth (0.3 percentage points), thanks to the increase in the working-age population and the employment rate (and despite their apparent negative impact on productivity, since they tended to be employed in low-value-added industries). The overall contribution of immigration to GDP growth rose to nearly half in 2001-05, when immigration flows were particularly high. The Spanish think tank Fedea obtains similar figures (Dolado and Vazquez, 2008).

The government report highlighted other favourable labour market indirect impacts, based on standard econometric estimations. One-third of the increase in the female participation rate and a significant reduction of structural unemployment (via wage moderation and lower geographical mismatch) could be attributed to immigration. The latter result has been complemented by Bentolila *et al.* (2008), using a New Keynesian Phillips curve – the relationship between unemployment and inflation. These authors estimate that the curve has shifted inwards and flattened; that is, the fall in unemployment since 1995 would have led to a significantly higher inflation rate in absence of immigration flows.

Finally, Izquierdo *et al.* (2007) calibrated a dynamic general-equilibrium overlapping-generations model, with heterogeneity between immigrants and natives, to compute the impact of immigration on the Spanish economy since 1995. Overall, its impact on per capita GDP is positive in their model, but not large, owing to a higher estimated negative effect on productivity. By contrast, immigration increases employment thanks to the impact on working age population, and to their higher employment rate.

In sum, the empirical literature in Spain is robust in refuting the fallacies of lump of labour and of immigration "labour robbing". It highlights the benefits and challenges (mostly in skills and socio-economic assimilation) that immigration entails.

The Path Less Travelled: Studies of South-South Migration

Latin American migration is predominantly South-North, but there are important corridors within the region. Do these exhibit the same labour market effects?

Much of the foregoing discussion is based on the assumption that people flows inevitably originate in developing or emerging economies and end in industrialised ones: from South to North. Certainly, as Chapter 2 illustrated, this is not a gross distortion of international migration for Latin America and the Caribbean, given that some 86% of migrants from the region are in OECD countries. Nevertheless, for a small but growing number of Latin American and Caribbean countries, immigration is becoming a major public-policy concern. Indeed, for some countries, like Argentina and Brazil, immigration never stopped being an issue for the policy maker. More generally, the World Bank estimates that half of world migration is South-South in this sense. Ratha and Shaw (2007) show that South-South migration is primarily driven by proximity (a common border) and networks, and only to a lesser extent by income differences (two-thirds of

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migrants from low-income countries move to other low-income countries). Do any of the lessons of immigration in OECD countries transfer to the analysis of immigration in Latin American countries?

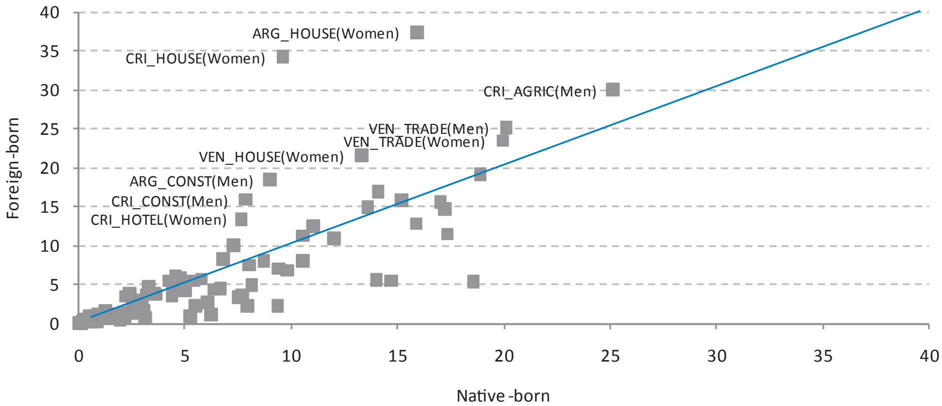
Unfortunately, the available economic research is too thin on the ground to provide much insight into the impact of immigration on wages or unemployment in Latin American countries. Using the LINKAGE general-equilibrium model developed at the World Bank, Ratha and Shaw (2007) simulate the change in wages in destination countries resulting from a cumulative 50% increase in South-North and South-South migration up to 2025 (from 6 to 9% of the labour force). They conclude that the effects on natives would be negligible in both cases, while existing migrants' wages would be less negatively affected by the South-South case (down 7% against 13%). Moreover, gains from new migrants (both at host and home countries) would more than compensate for wage decreases. However, these results are dependent on the assumptions made, especially the degree of substitution between migrant and native workers.

In the OECD context one important conclusion has been that immigrants and native-born workers (even low-skilled ones) frequently do not compete for the same jobs. Is this simply an artefact of labour-force differences between North and South or does it hold true for Latin American South-South migration? Figure 3.5 compares the occupations in which immigrants work in the three main Latin American destination countries (Argentina, Costa Rica and Venezuela), and compares this distribution to that of the native-born labour force, differentiating by sex. Each point in the figure represents the share of the male or female immigrant and native populations working in a given sector. If a point lies on the 45-degree line, it indicates that the relative proportion of immigrants and native populations working in that sector is the same (again, considering men and women separately). The further the observation departs from this line, the more probable that immigrant and native workers are complementary; that is, that they do not compete with each other for the same jobs[16].

Complementarity is also seen in labour markets subject to South-South migration

Figure 3.5. Sector of Activity of Natives and Foreign Workers in Argentina, Venezuela and Costa Rica

(Percentage of native and foreign workers, circa 2000)



Note: Sectors of activity are recorded according to the International Standard Industrial Classification, Rev. 3 (ISIC, cf. UN, 1989). The following abbreviations are used AGRIC: Agriculture and fisheries; CONST: Construction; HOTEL: Hotels and restaurants; HOUSE: Employment in private households; and TRADE: Wholesale and retail trade, repair of motor vehicles, motorcycles and personal and household goods.

Source: OECD Development Centre calculations, based on the 2000 census round in Latin America (processed with ECLAC Redatam+SP online).

StatLink http://dx.doi.org/10.1787/716031185842

Male immigrants in Argentina and Costa Rica are concentrated in agriculture and construction, while the concentration of natives in these industries is significantly lower. This complementarity is highest in the case of female immigrants in Costa Rica and Argentina, who are concentrated (between 35 and 40% of all immigrants) in household services, more than three times the percentage of Costa Rican and Argentinian women who perform these tasks. Immigrants in Venezuela (both women and men) seem to strengthen the trade sector, probably reflecting public policies implemented in the 1970s that attracted mainly skilled immigrants. On the other hand, immigrant workers are – not unexpectedly – under-represented in public sector administration activities, education and health assistance (the majority of the points under the line). By contrast, male immigrants tend to compete with natives in the manufacturing sector in the three countries, and in the trade sector in Argentina (both men and women). All in all, this graphical analysis tends to support the hypothesis that migrants often fill gaps in the host country's labour market, especially in the case of women. The same approach applied to the United States and Spain, the main Northern destinations for Latin Americans, shows that complementarities in South-North flows are lower (especially when comparing Argentina and Costa Rica with the United States). Therefore, negative employment and wage effects on Southern host countries may be lower than those found in the South-North literature, which are themselves already weak.

One of the rare empirical papers on these issues studies the impact of Nicaraguan migrants in Costa Rica (Gindling, 2009). The author finds, similarly to the research for OECD countries reviewed earlier, no evidence that Nicaraguan inflows had affected total average earnings in Costa Rica. However within this the earnings of Costa Rican women were indeed affected. High-skilled Costa Rican women saw their earnings increase while less-skilled Costa Rican women experienced a drop in wages, suggesting that Nicaraguan immigrants are complementary in the first case (as previously shown for the United States and Spain), and substitutes in the second.

Brain Waste: Avoiding "Lose-Lose-Lose"

"Brain waste", the mismatch of a migrant's skills and employment, is particularly notable among the region's migrants to the United States

A final point on skills and migration relates to the phenomenon we earlier called "brain waste". Most research on migration assumes that workers are employed in activities that correspond to their skill level. However, in practice workers may be employed in sectors characterised by skill requirements quite different from their educational or training background. In particular, migrants may be overqualified for the work they do. As Mattoo *et al.* (2005) and Niimi and Özden (2008) show, this is the case for for Mexicans, Central Americans and Andean university-educated migrants working in the United States (though not so for Caribbean and South Americans). Despite their tertiary degrees, these groups rarely hold highly skilled jobs. Worse, they may even be at the lower rungs of the skill ladder: 44% of tertiary-educated Mexicans migrants in the United States are working in unskilled jobs.

This equilibrium represents a lose-lose-lose situation: the home country loses human capital ("brain drain"), the host country and the migrant him/herself are not fully employed ("brain waste"), and the low-skilled workers in host countries (both migrants and natives) can be pushed out of the market (given that they compete with these higher-educated workers for jobs). In part, this outcome might be explained as a results of efficient market forces: employers may value a higher spending per student in some countries than others, a better performance at school, or even English-speaking proficiency (variables not usually captured in the common education measures), and migrants, even university-educated ones, may suffer in comparison to highly educated natives. But at least some

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part of the brain waste observed arises from the non-recognition of foreign qualifications or by the imposition of burdensome requalification requirements on foreigners. Alquezar *et al.* (2009) highlight that even in the European context where the harmonisation of social and educational structures is quite advanced, and several initiatives are under way (notably the Bologna process, the European Qualifications Framework, and the Europass), more progress is still needed. This is an area that needs to be addressed internationally and may best be tackled in the forum of the General Agreement on Trade in Services within the World Trade Organization.

MIGRATION, ECONOMIC POLICY AND THE CRISIS

The economic crisis, the most acute for Latin America since the 1980s, is the last ingredient of our analysis. How will migration respond to the crisis? This question is difficult to answer because some of the characteristics of the current economic crisis – especially its synchronised nature – mean that the economic push and pull factors of migration may not change dramatically in relative terms. That is, employment opportunities may be declining in both the industrialised countries of destination and the countries of origin at the same time, leaving the net difference in earnings prospects for the potential migrant little changed. In spite of hopeful talk of "decoupling" early in the crisis, the economic prospects of emerging economies have deteriorated sharply, in line with the slowdown in industrialised economies.

Although the income gap will remain notably favourable in industrialised economies, Hatton and Williamson (2009) argue that when economic conditions deteriorate at both source and destination, in the short term host country conditions dominate. According to the same authors, history suggests a simple "10% rule": if immigration policies are not too restrictive, every 100 jobs lost in a high-immigration country results in 10 fewer immigrants. This drives us directly to a second, more relevant and more uncertain factor: the policy response.

Empirical evidence suggests that economic crises are a time for policy reform

Even though crises are delicate times to implement policy reforms, recent anecdotal evidence and some empirical tests for OECD countries (Hoj *et al.*, 2006) show that big economic crises are generally associated with higher overall reform activity (although reforms in certain specific labour market areas – tax wedges, job protection and benefit systems – tend to take place in periods of strong upswings). As regards immigration, a protracted crisis can certainly provide more opportunity for anti-migration positions. We will concentrate on two areas of public debate: financial incentives to encourage migrants to return home, and the portability of social rights. A third area, the tightening of border controls and the reduction of immigration quotas, are outside the scope of the present analysis, but may be equally relevant to migration movements level and composition in the months ahead (see OECD, 2009*b*).

Old Policies in a New Crisis: Promoting Return Migration

Migrant-return policies can be focused on supporting the effective management of temporary migration, or may involve assistance for voluntary return (see OECD, 2008*c*, for an exhaustive review). In the second category, some countries are offering financial incentives to encourage return migration; such measures are deemed necessary to compensate the "place premium" discussed in Chapter 2. In addition the absolute benefits of remaining in OECD countries are declining

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in the crisis. Immigrants are over-represented in the construction sector and other activities greatly exposed to the economic cycle, they are overwhelming on temporary contracts, and they are usually less skilled than natives[17].

Return migration programmes have been started, notably in Spain. The evidence from the use of these in the 1970s and 1980s is mixed

Among the most noteworthy initiatives for promoting return migration is a Spanish programme established in November 2008 (under *Real Decreto-1800/2008*). Unemployed immigrants legally resident in Spain, from countries with whom Spain has a bilateral social security agreement, and who decide voluntarily to return to their country of origin, are entitled to receive their entitlement to statutory unemployment benefit as a lump-sum[18]. In the most favourable case (an immigrant who has continuously contributed for six years at the upper earnings limit and who has two dependent children), that would amount to slightly more than EUR 32 000. Based on official records of actual social contributions made by immigrants, the average benefit will in fact be around one third of this figure. Unemployed immigrants from the Dominican Republic, Mexico and from all South American countries except Bolivia are entitled to seek this lump sum payment. Beneficiaries receive 40% of the benefit when their application is approved, and the rest on personal application to the Spanish consulate in their country of origin. They are thereafter prohibited from returning to Spain for three years, but with the commitment that any request to return thereafter would be given priority. According to Spanish officials, around 5 000 immigrants (mainly from Ecuador, Colombia and Argentina) had applied to the programme by May 2009, though the potential universe is well over 100 000 people[19].

These policy measures are very much in line with German and French experiments in the 1970s and 1980s, widely regarded as having failed (see Dustmann, 1996, and the references therein). These countries had implemented a *laissez-faire* migration policy in the previous two decades to address labour shortages (in contrast with the strict regulations to ensure the return of migrants in Switzerland, for example), which attracted many southern European (Greek, Spanish and Portuguese) and North African workers. Potential drawbacks became evident from the mid 1970s, when economic growth and employment slowed, but a significant part of these "guest workers" stayed. As a response, the German government enacted in 1983 a programme which used financial incentives to spur the return of short-term unemployed (plus reductions of return barriers): a return payment of DEM 10 500 (equivalent today to some EUR 6 300) plus the equivalent of EUR 900 per child, and a refund of their retirement contributions. Around 300 000 immigrants left Germany, more than the 250 000 initially forecast. The net effect of the measures, however, is estimated at half this amount, since many migrants decided instead to settle more permanently and bring their families to Germany, spurring further immigration.

France too launched return migration programmes in the mid-1970s, likewise based on financial incentives. From 1977, non-EEC nationals were paid their travel expenses, an *aide au retour* of FRF 10 000 per worker (equivalent today to some EUR 5 000); plus similar benefits for the partner if unemployed and the equivalent of EUR 2 500 per child. Those entitled had to renounce any claims on social insurance, and to return residence and work permits. A second programme was implemented in 1984, mainly for non-EEC short-term unemployed workers in the automobile industry, and entailed the capitalisation of two-thirds of unemployment benefits (though not of retirement funds), a grant of up to the equivalent of EUR 3 500 for self-employment projects, and a compensation payment from their former employer. Overall, about 150 000 immigrants participated in these programmes, though there are no available estimates of how many might have been "free riders" – those who would have returned even in the absence of the programmes.

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The Spanish return migration programme is more generous than these precedents. The lump sum payment amounts are larger, since all unemployment benefits are capitalised versus two-thirds in France and nothing in the German case. Moreover, bilateral social security agreements with migrants' home countries ensure that retirement pension rights will be respected; in the French programmes they were lost, while in Germany the employer contributions reverted to the German pension system. But, at the same time, the restriction to nationals of countries with bilateral agreements with Spain effectively cuts in half the number of potential beneficiaries. Most significantly, as long as return migration is driven by the *relative* economic prospects in origin and destination countries the prospects of the programme are equally modest, given that economic conditions are for the time being worsening at home as well as in Spain[20].

Return Migration: Better if You Can Take Your Pension With You

A major barrier to return is the potential loss of accrued social security rights, particularly pensions. Lack of portability also penalises those who are unlikely to complete minimum qualifying periods

As flows of money, people and ideas across borders increase, the portability of accrued social security entitlements – that is, the capacity to move pensions and health-care benefits between host and home countries – is of increasing relevance. As highlighted in the *Decent Work* agenda of the International Labour Office, social protection models should adjust to social change, including this mobility from and among emerging countries. Research suggests that assuring portability of pensions might be a more effective return migration policy than the kind of financial incentives discussed above[21]. Pension and health benefits are part of the income differential between host and origin country, since they constitute a deferred and/or substitution salary for workers who no longer work because of old age or disability, incorporated in non-wage compensation[22]. This is simply the international version of the limits that the non-portability of pension benefits from one employer to another in many countries places on internal labour mobility.

This is a topical concern for the many migrants who have only recently come to OECD countries: only a quarter of immigrants in Spain and fewer than half in Italy have been in the country for more than 10 years (OECD, 2009*b*). In the absence of institutional arrangements for portability, these immigrants will not qualify for minimum contributory pensions, typically restricted to people who have made contributions to the system for at least 10 to 25 years. Portability can also generate beneficial effects for the host country, by increasing incentives for job creation in the formal sector. With portability contributions are linked to benefits and not seen as a pure labour tax. It is likely, moreover, to be associated with better social and economic integration of immigrants.

Full portability, that is, the capacity to migrate with your social entitlements, requires four basic rules or adjustments:

- a totalisation of the periods of contributions (years of contributions in varying jurisdictions are added to determine whether a migrant qualifies for a contributory pension; the *aggregation rule*),
- a totalisation of contributions (accumulated social contributions are considered to set the pension replacement rate, with a pro-rata formula reflecting the time spent in each country; the *apportionment rule*),
- the payments of pensions across borders,
- specific regulations to avoid double taxation (especially for civil servants and temporary expatriates).

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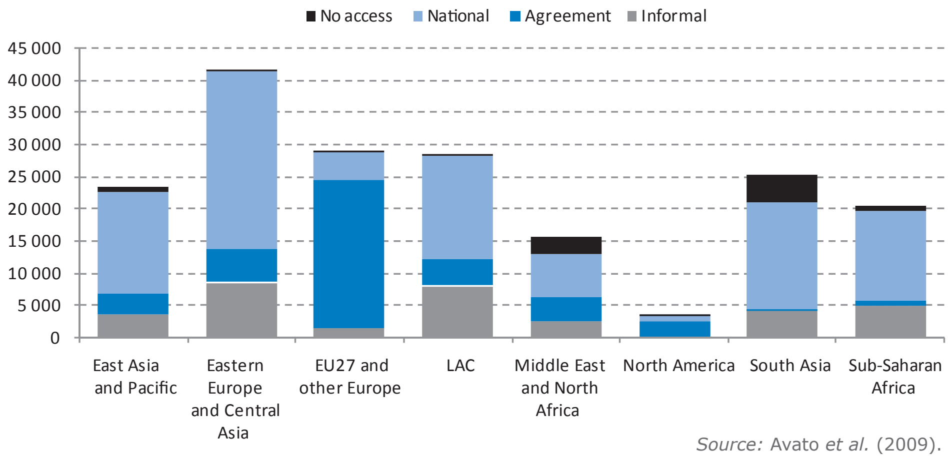
These arrangements need to be made between social security administrations and can be implemented on a bilateral or multilateral basis (for instance within the ILO framework), and potentially cover old-age, disability and survivors' pensions, and health and long-term assistance.

Despite the importance of pension portability, comprehensive official data are limited, so statistics rely on sometimes heroic assumptions. Avato *et al.* (2009) update the seminal work of Holzmann *et al.* (2005), and find that only one in four world migrants are covered by bilateral agreements. More than half of migrants (nearly 102 million people) have an incomplete access to social security, with portability losses, and another fifth (almost 33 million) are informal sector workers, with very limited access at best[23].

Migration between OECD countries is overwhelmingly covered by portability arrangements. This is in sharp contrast to the experience of those moving from Latin America or the Caribbean

The situation for low and low-middle income countries, and particularly Latin America migrants, is worse[24]. As shown in Figure 3.6, only 4.1 million Latin American migrants (15%) are covered by social security agreements, while the broad majority (16.1 million people, almost 60%) are subject to portability losses. By contrast, almost all migrants (98%) moving within high-income OECD countries are covered by bilateral agreements. Non-coverage because of informality is the highest among all regions of migrant origin in the world, affecting nearly 30% of the migrants (7.9 million people) against a worldwide average of 18%.

Figure 3.6. Pension Portability Regimes
(Thousand international migrants by region of origin, 2000)



Source: Avato *et al.* (2009).

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Portability and Pension Agreements in Latin America

This poor situation is driven by the situation of Mexicans, and particularly Mexicans in the United States. Some 5.1 million Mexican migrants (46% of the total) work in the informal sector of the host country (overwhelmingly the United States). Across nations 53% of them (nearly 6 million people) have incomplete access to social security, and less than 1% (56 000 Mexicans) work under bilateral social-security agreements. Excluding Mexico the percentage of Latin American migrants covered by social-security agreements increases to 24% (see Figure 3.7), the highest among emerging economies.

On pension arrangements, Spain (with around one million people arriving from Latin America since 2000) has led the way in good practices[25]. Spain has signed bilateral agreements with 20 countries, including all the major economies of South America other than Bolivia. The process started with Ecuador, in effect since 1975, the source of the second-largest immigrant community in Spain (after Moroccans). The most recent agreement, signed in 2008, covers migrants from Colombia, the second most numerous Latin American immigrant community. These texts cover pension benefits and, in some cases (from Latin America: Brazil, Chile, the Dominican Republic, Ecuador, Peru and Venezuela), health assistance[26]. According to government data, around 75 000 Spanish nationals in Latin America benefit from bilateral agreements, while around 35 000 Latin Americans receive pensions in Spain from their governments.

Among host countries, Spain is an example of best practice, with some 20 bilateral agreements covering most of its immigrants...

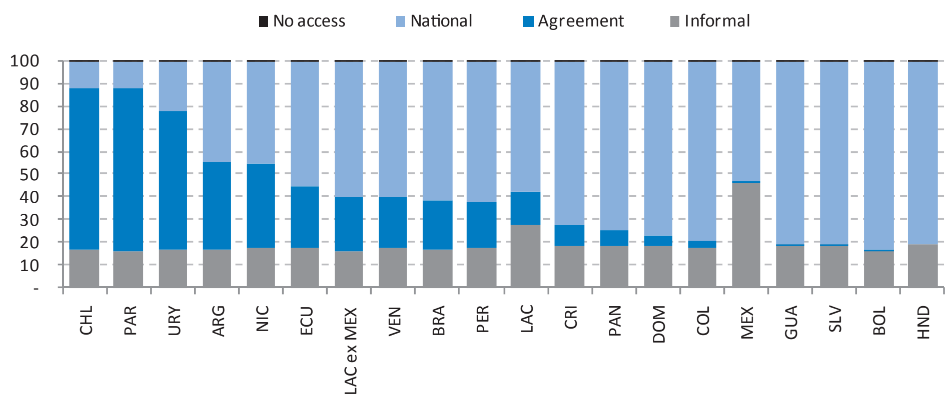
Chile has also been particularly active and now has 23 bilateral agreements, starting with Argentina in 1972, and most recently with Peru in 2004 and Ecuador in 2008. Among the major economies in the region, only Bolivia, Colombia, Mexico and Venezuela are not yet covered. Chilean agreements cover pension benefits and typically provide for equal access to health assistance for natives and immigrants[27]. As a result of this network of agreements more than 70% of Chilean migrants benefit from full portability of pensions, leading the region (Figure 3.7).

...while within the region, Chile has agreements covering 70% of its migrants

Chile was the host for the XVII Ibero-American Summit in November 2007 at which a multilateral agreement on social security was adopted (*Convenio Multilateral Iberoamericano de Seguridad Social*). When ratified by member states, it will entitle around six million citizens who work outside their country of origin to totalise both qualifying years and monetary contributions for old-age, disability and survivors' pensions. (It also contains measures to improve co-ordination between the relevant social security administrations.) At present, the agreement has been ratified only by El Salvador and Venezuela, though Spain is expected to do so during 2009. This agreement will join the existing regional agreements between CARICOM countries (effective since 1997, covering nearly half a million people), and the more recent one between MERCOSUR countries (effective since 2004, benefiting nearly one million people).

Rapid ratification of the Convenio Multilateral Iberoamericano de Seguridad Social would be highly desirable since it would benefit around six million citizens who work outside their country of origin

Figure 3.7. Pension Portability Regimes in Latin America
(Percentage of total migrants by country of origin, 2000)



Source: OECD Development Centre calculations based on data from Avato *et al.* (2009).

StatLink http://dx.doi.org/10.1787/716045828441

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The lives of many migrants would be improved by the ratification of the Ibero-American Convention and the US-Mexican bilateral agreement

In the list of pending accords, the United States-Mexico social security agreement stands out because of the number of migrants involved and because of the potential benefits that would accrue to them were this agreement ratified. Signed by both countries in 2004, the agreement has yet to be ratified by the United States Congress and reviewed by the Mexican Senate. The agreement incorporates the totalisation of periods and contributions (with the usual pro-rating), and would significantly lower the number of years to be eligible for at least some contributory pensions, to one year in Mexico (against 24 years at present), and 1.5 years in the United States (against ten years). Health coverage is not included and, indeed, the largely private nature of health care and health insurance in the United States precludes the kind of agreements that Spain, for example, has struck with other countries.

The highly asymmetric flows between the countries, both in size and skills, and the uncertainty surrounding the cost of the agreement for public finances in the United States appear to explain the slow progress with ratification. (The US Government Accountability Office estimates some 50 000 Mexican migrants would potentially benefit; by contrast, the Social Security Administration assesses the financial impact of the agreement on the US pension system as negligible.) Either way, such an agreement would make a huge difference to the social protection of individual Mexican migrants.

In general terms, it makes sense for policy makers to seek full coverage of workers under bilateral social agreements, preferably within a multinational framework. A model may be the EU regulation governing the portability of social security benefits[28]. When moving within the European Union even third-country migrant workers enjoy the same rights as EU nationals with respect to the portability of social security and benefit entitlements after five years of residence. However, as Avato *et al.* (2009) point out, challenges for emerging economies may be greater owing to informality, lower administrative capacity and social-security systems that are less developed (the same problems faced by the native-born in many areas). Some preconditions, notably guaranteeing basic social rights for both natives and migrants, should nonetheless be in place.

Such reforms would ensure that migration is not deterred by institutional settings – that is, that imperfect social protection is not in effect an indirect form of immigration control – and would respect acquired social rights for those compelled to migrate. Defined-contribution, fully-funded pension schemes (backed by assets at market prices), popular in Latin America since the Chilean reform in 1981, are best equipped to provide full portability (for a broad analysis on the impact of structural pension reform on the labour market, see Box 3.2). Greater efforts are needed on the portability of health benefits, which are poorly covered by many current agreements. Finally, broader and more regularly updated data concerning pension portability and best practices would be of great utility to policy makers.

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Box 3.2. Pension Reform and Labour Market Gains: Asking Too Much?

The World Bank's 1994 report *Averting the Old Age Crisis: Policies to Protect the Old and to Promote Growth* set the agenda for structural pension reform. Rapid demographic transition, the weakening of informal protection networks, and the present and expected financial burdens justified putting in place a multi-pillar pension system, managed by the public and the private sector. Latin America has broadly adopted this reform agenda: Peru in 1993, Colombia in 1994, Argentina in 1994 (though reformed again in 2008), Uruguay in 1996, Mexico and Bolivia in 1997, El Salvador in 1998, Costa Rica and Nicaragua in 2000 and the Dominican Republic in 2003 (all joining the pioneering 1981 experience of Chile).

According to the same report, "structural pension reformers" (those countries which introduced mandatory individual capital accounts, managed by the private sector) would enjoy various positive macroeconomic effects: increased employment and productivity, higher domestic saving and investment, and the development of domestic capital and financial markets (in a similar line, see Lindbeck and Persson, 2003; or Barr and Diamond, 2006, for a more sceptical view). Focusing on the labour market, this type of pension scheme provides, at least in theory, better incentives than the traditional defined-benefit pay-as-you-go schemes, leading to a higher structural employment rate, lower levels of informality, and higher labour supply. These effects flow from the higher "linkage effect", that is the stronger perceived link between contributions made and benefits secured. Social contributions have no negative effect on the equilibrium employment rate if agents perceive a full linkage effect, since they are seen as deferred salary instead of a tax (see OECD, 2007, pp. 157-206).

Evidence on these labour impacts remains controversial. First, tax wedges were not so distorting in some of the old pension schemes (Gruber, 1997, showed that social taxes in Chile were borne by employees, and did not affect labour costs; by contrast Kugler and Kugler, 2003, argued that less than one-fifth of social taxes in Colombia were borne by workers).

Second, even taking into account the relatively short period of time since the reforms were adopted (around 15 years on average, and generally with lengthy transitional rules), the incentives to join the formal sector and pay contributions to the new system have proved weaker than expected. Informality, following the ECLAC definition (the ratio of urban employees to micro-firms, domestic service, unskilled self-employed, and family workers), has stubbornly remained between 40 and 60% in all the economies in the region (except Chile) since 1990. (See Jütting and de Laiglesia, 2009, for a detailed discussion of statistics, causes and consequences of informality.) This poor take-up lies at the heart of low coverage and low projected pension levels.

According to Gill *et al.* (2005) this may reflect a combination of myopia and lack of information on the part of workers; labour and social legislation, such as mandatory minimum wages; and mostly rational decisions based on volatile returns, high start-up fees and social preferences for anti-poverty (rather than savings) programmes. Chile seems the only country bucking this regional trend. Labour market informality is slightly under 26% (according to the same ECLAC figures), 9 percentage points lower than in the early 1990s. Using data for 1981-2001 Corbo and Schmidt-Hebbel (2003) estimated that the pension reform had been responsible for formal employment rising between 3 and 8%, informal employment decreasing by around 1%, and had taken between 1 and 2 percentage points off the unemployment rate.

All in all, two lessons emerge. First, the lasting effects of reforms can only be evaluated in the medium term, with the benefit of more experience and data. And second, pension reform needs to be underpinned by appropriate social, labour and macroeconomic institutions.

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NOTES

1. For a more general view, the OECD Development Centre's *Gaining from Migration project* (Dayton-Johnson *et al.*, 2007) exhaustively reviewed the evidence surrounding migration and economic progress in both sending and receiving countries. Dayton-Johnson *et al.* (2008) examined many aspects of the migration-employment relationship.

2. This heterogeneity responds to two dominant schools of thought, reviewed in Perry *et al.* (2007). On the one hand, the *exit* or voluntary view argues that entrepreneurs and workers opt for informality, based on a cost-benefit analysis. By contrast, the *exclusion* view supports the theory that workers are excluded from formal activities. Jütting and de Laiglesia (2009) argue for an additional third way, based on the non-existence of clear boundaries between formality and informality. In this framework, workers are not 100% formal or informal; they may pay direct taxes, but not social contributions, for instance.

3. The experience of labour markets in countries that have recently joined the European Union may provide examples of relevance to Latin America. In Lithuania, the free movement of workers has helped to relieve pressure on the domestic labour market, drive down unemployment and create upward pressure on wages, although this has caused major labour shortages in certain industries (Thaut, 2009). In rapidly growing countries such as Romania, emigration in the midst of growing labour demand has forced the country to turn to immigration to compensate for the gap (Silasi and Simina, 2007). Historically, emigration has contributed to real wage convergence towards that of rich countries by slowing the growth of domestic labour supply, such as in the case of Ireland (Boyer *et al.*, 1993).

4. This is a point made in the "New Economics of Labour Migration" literature. See Stark (1991), and the empirical analysis by Carletto *et al.* (2006) for Albania, or Taylor *et al.* (2003) for China.

5. Beine *et al*. (2008) found a positive effect of skilled migration prospects on pre-migration human capital formation. Analysing specific cases, they found that countries combining relatively low levels of human capital and low emigration rates are likely to experience a beneficial brain drain. See also Özden and Schiff (2006).

6. Stark (2004) discusses the "brain gain" hypothesis linking emigration to incentives to acquire schooling.

7. Azam and Gubert (2006) find that in Mali and Senegal remittances reduce labour supply in migrant households. Their conclusion suggests that while rich families are more likely to send a household member away, and in the process get more remittances, they often earn less in the home village owing to a moral-hazard effect caused by the receipt of these remittances. A similar conclusion is reached by Rodríguez and Tiongson (2001) for the Philippines and Jadotte (2008) for data on Haiti. Other studies showing this include the cross-country study by Chami *et al.* (2003).

8. In Moldova, Görlich *et al.* (2007) found that living in a migrant household implies a higher probability of intra-household labour substitution (for instance to home production) and higher enrolment in education.

9. See also Acosta (2006) on El Salvador and Mansuri (2006) on Pakistan for similar conclusions. Epstein and Kahana (2008) provide a theoretical framework. Analysing a slightly different mechanism, Yang (2006) found that an increase in remittances (via an appreciation of the receiving country's currency) positively affects investment in education and entrepreneurship back home. In particular, he found that child labour decreased and investment in education of children increased.

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10. There is no agreed definition of diaspora. The term derives from the Greek *diaspeirein*, meaning "to scatter seeds widely". The International Organization for Migration's glossary defines a diaspora as "people or ethnic population that leave their traditional ethnic homelands, being dispersed throughout other parts of the world". IOM also states that this term conveys the idea of transnational populations, living outside their homelands while still maintaining relations with them. The increasing opportunities for developing new forms of transnational relationships make it possible to use the term "transnational community" as a synonym of diaspora.

11. Although this section highlighted the importance of transnational migrant entrepreneurs for the home country, there are also positive effects for host countries, namely business network externalities such as: creating trust, providing cheaper market information and reducing transaction costs (thanks to the elimination of language barriers, better knowledge of the culture, values, laws, or best practices). These networks can promote trade and foreign direct investment between host and home countries.

12. See Borjas (1999) for a model-based approach; and Jean *et al.* (2007) and European Commission (2008) for review studies based both on area studies and a factor-proportion approach.

13. Meta-analysis, the state of the art in literature surveying, departs from the compilation of an exhaustive sample of literature and the choice of the dependent variable (in this case, the impact of immigration on wages or unemployment). A general set of variables that could be influencing this result (theoretical model, sample, among others) is selected, and tabulated in each study with dummy variables. The meta-regression of the dependent variable on these moderators allows quantification of the "true dependent variable", that is, the consensus result of the whole empirical literature after controlling for methodological differences.

14. Borjas (2003) disputed these results, finding evidence that increased labour supply due to immigration reduces wages for native workers, if the groups of workers are sufficiently carefully defined (so that one is comparing groups with similar education and experience).

15. Moreover, some might argue that the effect of immigration on wages operates as an implicit threat against workers who seek higher wages. Employers have recourse to immigrant labour – a kind of "reserve army" whose potential employment acts as a credible threat against strikes or other actions by workers already in place (whether native-born or not). In this regard, unauthorised immigrants working with false papers– the kind of workers targeted by recent mass raids in the United States (described in Chapter 1) may be doubly useful to cunning employers, given that their availability to work at prevailing wages may discourage workers from mobilising, but also because their precarious situation makes unauthorised immigrants themselves less likely to seek higher wages. These are compelling hypotheses but more empirical research will be needed to substantiate them.

16. A more extensive analysis and the original database can be found in the Statistical Annex of the Country Notes of this publication. This graphical approach should be seen as a first-cut analysis of labour complementarity. Additional controls by skill level, type of work and age, and estimates of the impact on wages within their skill groups, would be needed in a more complete study.

17. See OECD (2009*b*) for a description of recent policies implemented in industrialised countries.

18. See www.inem.es/inem/ciudadano/prestaciones/retorno_extranjero.html. This programme complements other existing support policies, mainly focused on consultation and humanitarian aid.

19. The programme is supplemented by another for Romanians unemployed in Spain (who numbered 71 000 in the first quarter of 2009), under which they can continue to receive the full amount of their Spanish benefits following a return to Romania.

20. A similar evaluation can be found in OECD (2009*c*). Moreover, Dustmann (1996) argued, based on Germany-Turkey return migration data, that migrants who base their return decision on financial support schemes are more likely to regret this decision afterwards, and to suffer reintegration problems in their countries of origin.

21. See, for example, Holzmann *et al.* (2005), from the World Bank, or OECD (2008*c*). However, Bonin *et al.* (2008) analysed different hurdles to mobility, including problems of transferability of pension benefits with European data. These pension-portability barriers impact positively but not significantly on expected future mobility. By contrast, individual factors, such as language skills, job prospects and cultural adaptation dominate.

22. Alternatively, the non-portability of these entitlements can be seen as an additional monetary cost to migration. The empirical literature on the determinants of migration flows has identified a set of important socio-economic and political "pull and push" factors (generally expressed in differences between origin and destination countries): level of income per person, stock of nationals (networks), extent of the informal economy, welfare state generosity, quality of political institutions, physical and cultural proximity, and migration laws (see Table 1.1 in Chapter 1: Changing Schools of Thought on Motives for Migration).

23. See Chapter 5 of the 2009 edition of the *Outlook* for a discussion of informality in the region and statistics on the proportion of working people who do not contribute to social security systems (OECD, 2008*a*).

24. The Persian Gulf region is a clear outlier, since many workers do not access social protection in the host country.

25. It should be stressed that these policies are institutionally well rooted, and do not represent an immediate response to recent phenomena, in particular the crisis.

26. See www.seg-social.es/Internet_1/Internacional/Conveniosbilaterales/index.htm. Accessed 15 October 2009.

27. For the complete list and contents, see www.safp.cl/573/propertyvalue-1654.html. Accessed 15 October 2009.

28. Regulation (EC) 883/2004 of the European Parliament and of the Council of 29 April.

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CHAPTER FOUR

Remittance Flows and Financial Development

THE STRONG LINKS BETWEEN REMITTANCES AND DEVELOPMENT

Improving an economy's financial system matters for national growth and development (Levine, 2004; World Bank, 2007). Financial systems can provide information about investment opportunities and help to allocate productive capital in the economy. Moreover, financial development and capital mobilisation are interrelated since financial instruments facilitate the reallocation of investment towards higher return activities, with positive implications for growth (Acemoglu and Zilibotti, 1997). In sum, economic growth and poverty reduction go hand in hand with financial development[1].

A country's financial system has an important role in its development. Though often overlooked, remittances can play a strong part in this

This linkage makes the steady increase over recent years in remittances to Latin America of interest far beyond the immediate benefit they bring to receiving households. The link between remittance flows and economic development has been analysed from a variety of perspectives, and the empirical evidence shows that these flows can have a positive impact on economic development and poverty reduction. Adams and Page (2003), for example, find that remittances have a significant impact on reducing poverty and a similar conclusion is reached in the IMF's 2005 *World Economic Outlook*.

For the case of Latin America, at the microeconomic level at least, remittances are found to have had a generally positive effect. Studies on infant mortality and birth weight in Mexico have shown that migration and remittances help reduce infant mortality and are associated with better childhood health[2]. Remittances also have significant effects on the living standards of the households that receive them (Cardona Sosa and Medina, 2006). Remittances can fuel business start-ups for example. In a study examining enterprise formation in a sample of 30 communities in Mexico, Massey and Parrado (1998) showed that earnings from work in the United States were an important source of start-up capital in 21% of new businesses. Dustmann and Kirchamp (2001), similarly, found that the savings of returning migrants could be an important source of start-up capital for micro-enterprises. Remittances have also been shown to improve educational outcomes for children in the households that receive them[3].

While the contribution made by remittances to education, health, poverty reduction and enterprise formation have been robustly demonstrated in a series of studies, less is known about their consequences for financial development. Nor do we have clear evidence regarding the role of remittances in overcoming the "financial inclusion" gap that characterises most remitting migrants and their families. Migrants and their families frequently have no bank accounts, do not borrow money from banks, and do not avail themselves of other services from the formal financial sector. Studies of this phenomenon often refer to this as lack of "bankarisation" and – in the interests of brevity if not beauty – we will use this term in what follows.

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This will provide some insight into the implications of remittance flows for the bankarisation of both senders and recipients, and study to what extent remittances facilitate access to finance. In terms of the three-flow conceptual framework introduced in Chaper 1, remittances are the money flows that accompany people flows. This will examine the notion that they are also part of the ideas flow: that remittances might, for example, broaden and deepen financial markets bringing collateral benefits to migrants' families and their home communities and regions more generally. Likewise, it will look at how remittance flows may create a market for innovative new goods and services, such as mobile banking.

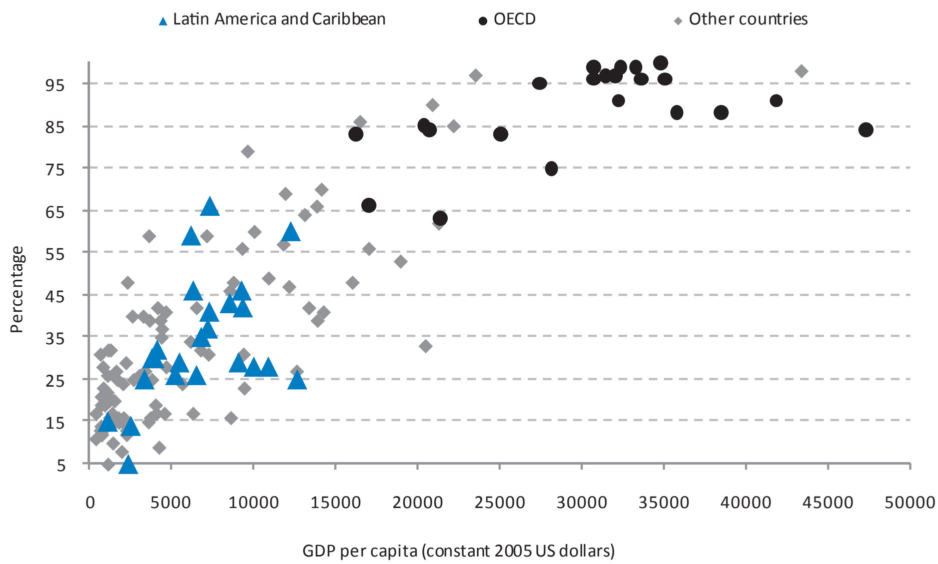
REMITTANCES AND ACCESS TO FINANCIAL SERVICES

Can Remittances Help Bankarisation in Latin America?

Higher per capita income and better access to financial services go hand in hand

Guaranteeing access to financial services for the poor has been an important objective for policy makers in Latin America. Higher levels of financial access in the population are usually accompanied by higher per-capita income levels. This is illustrated in Figure 4.1, which also serves to highlight the vast differences both of bankarisation and of average income between Latin American and Caribbean countries on the one hand and OECD countries on the other. (For the majority of migrants these two groups correspond to countries of origin and countries of destination, respectively.)

Figure 4.1. Share of the Population with Access to Financial Services against GDP Per Capita



Notes: The Latin American and Caribbean countries identified are Argentina, Belize, Bolivia, Brazil, Chile, Colombia, Costa Rica, Dominica, Dominican Republic, Ecuador, El Salvador, Grenada, Guatemala, Guyana, Haiti, Honduras, Jamaica, Mexico, Nicaragua, Panama, Peru, Uruguay and Venezuela.

Source: OECD Development Centre calculations based on Honohan (2006).

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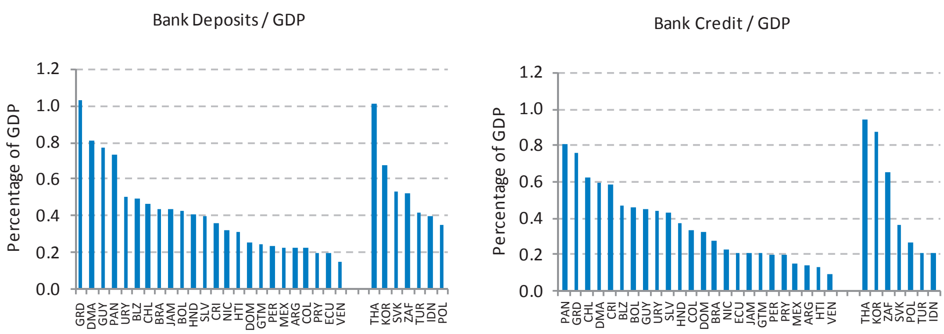
How do remittances affect financial development? The answer is by no means obvious[4]. One version would have it that remittances permit certain sectors of the population to access financial products and services that would be otherwise unavailable to them. When banks become more willing to extend financial services to remittance recipients, financial development is increased. If remittance receivers put the money transferred into the bank, the resulting increase in deposits can have an effect on bank assets, and therefore facilitate further credit to other sectors. The opposing view is that remittance recipients are *less* likely to ask for credit: their financial constraints are lower than their neighbours', given that they receive money from abroad, so their demand for loans might be lower as well. In this view, remittances could depress loan demand, even as they increase the potential supply of funds. Aggarwal *et al.* (2006) found that remittances had a positive and significant impact on financial development, by analysis of indicators such as outstanding credit and bank deposits as proportions of GDP. Their result was less significant in Latin America than other regions, however. The fact that the region had not fully taken advantage of the remittance flows for strengthening its financial infrastructure may suggest that additional measures are needed in order to secure the benefits of financial deepening observed elsewhere.

Empirical evidence supports the view that remittances foster financial development. This is significant for a region with low bankarisation and high remittances

Whatever indicator is used for financial development, Latin America consistently scores poorly. Figure 4.2 compares the region with others using the same standard measures which were the basis of Aggarwal's analysis.

Figure 4.2. Bank Deposits and Bank Credit in Latin America
(Average 2000-06)



Source: Beck *et al.* (2000, updated 2008).
StatLink http://dx.doi.org/ 10.1787/716067004406

Financial development is measured not only by depth indicators such as credit or deposits relative to GDP, but also by the coverage and intensity of use of the financial system (Figure 4.3). Indicators of coverage such as the number of automated teller machines (ATMs) or branches per inhabitant show Latin America and the Caribbean well behind: on average there are 8.5 branches and 15 ATMs per 100 000 inhabitants in the region, compared with 31 and 64, respectively, for developed countries (Beck *et al.*, 2005). Moreover, indicators of intensity of use such as number of loans or non-cash transactions per 100 000 inhabitants confirm this picture of a region with low levels of financial development. So too with indicators of financial development not related to households: in terms of market capitalisation, liquidity or corporate bond issuance, Latin America is well below other emerging regions such as East Asia or Eastern Europe (García Herrero *et al.*, 2003; de la Torre *et al.*, 2006).

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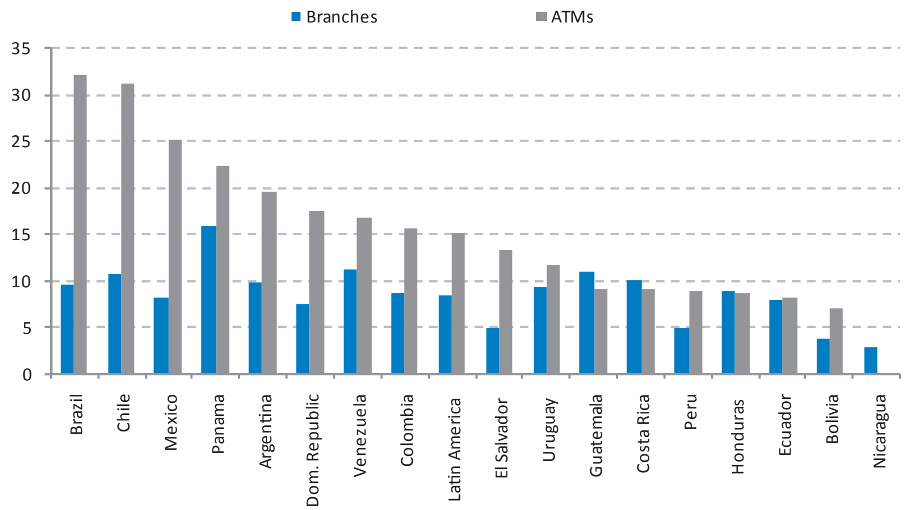
Figure 4.3. Number of Bank branches and Automated Teller Machines (ATM) per 100 000 Inhabitants



Source: Felaban (2007).

StatLink http://dx.doi.org/10.1787/716120851540

Many factors may lie behind this phenomenon, including low confidence in the banking sector, low capacity of households to accumulate savings, low bank penetration, inadequate competition, inefficiency and high intermediation costs. There is certainly a large gap in terms of the financial literacy of a large part of the population[5]. Many are simply unaware of the advantages (and costs) of financial services. One study (LIRS, 2005) reported that nearly 50% of Latin immigrants in the United States did not have a bank account for transactions. More than 40% of Latin workers said they "knew nothing" about investing or saving for retirement, compared to 12% for all workers. Cultural differences in the region are also important in explaining the success or failure of new platforms or technologies for sending remittances.

Low bankarisation may reflect characteristics of the financial sector such as high concentration, or public mistrust of financial institutions

At the institutional level, deficiencies in the legal framework have undermined efforts to increase financial access. It may also be that Latin America's long history of credit default and crisis has left a general sentiment of mistrust towards the financial sector. Although some progress has been achieved in the regulation and supervision of the financial system in some countries, Latin American households remain sceptical about the soundness of financial sector and memories of banking crises are long. The finger has also been pointed at concentration in the banking sector which is relatively high in most Latin American countries, potentially reducing competition[6]. The arrival of foreign banks in the 1990s (after a decade of banking crisis) was intended to spur competition and increased efficiency in the sector, through the introduction of new technology and marketing expertise. However, the industry's capacity – and appetite – to reach the less favoured sectors of the population has still been questioned.

The banks certainly do not seem to have fully seized the opportunity presented by the "remittances bonanza" of the last decade (see Chapter 2), since this has not led to a deepening of bank access in the region. The development of specialist remittance businesses may provide a new avenue. Until recently, most migrants used largely informal channels to transfer money home. A number of Money Transfer Operators (MTOs) grew up in response to this opportunity and have proved to be efficient in terms of distribution – reaching remote villages, if needed – if not always in terms of percentage cost. Their growth seems recently

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to have awakened the banks to the possibilities of this market. The banks' task is likely to be difficult, however, given the incumbent status of MTOs, their arguably efficient service and generally lower sending costs.

It is argued that formalising the platforms through which remittances are sent home is a way of encouraging increased bankarisation. Financial inclusion for both migrants and remittance-beneficiaries is certainly a valid policy goal for leveraging the benefits of migration, but should cover both migrants' capacity to accumulate deposits, and their access to credit. In practice, however, it is not always clear that higher levels of bankarisation (measured by deposits) have led to better access to credit and broader financial services for remittance-dependent households. In sum, although increasing *banking access* is a legitimate step on the way, policy should not lose sight of the true objective of increased *financial inclusion*.

Enhancing banking access for remittance-senders should be accompanied by increased financial inclusion, lowering credit barriers

Getting the Framework Right

The response of financial institutions, in Latin America and the Caribbean and elsewhere, to the rise of remittances has been diverse. Within the evolution of the operational framework through which remittances are sent private banks, saving banks and co-operatives have all taken steps to provide services for their (potential) migrant client base[7].

The specialised MTOs were the first to focus on this market, well before the commercial banks, and quickly built an advantage in terms of the their know-how, reach and – not least – the financial networks they had developed. As a result they had this market much to themselves for years. It is only really in the last decade that the commercial banks have seen in the remittances business model not only an opportunity to reach out to an enlarged client base but also a profitable financial service in itself.

Figures on access to banking among the migrant population in OECD countries demonstrate the difficulties the banks face. This has led some institutions to adapt their business model specifically to target the migrant and among these two general strategies can be identified: a policy where migrants are provided with the same services as native clients; or one where banks have established specific branches for the migrant client, offering a range of services tailored to the migrant population, such as repatriation insurance, free money-transfers, residence certificates, low-cost travel services, legal advice and housing loans. In order to extend their networks "the final mile" in the delivery of remittances banks and saving banks have either created their own money-transfer operator (as have BBVA and Santander in Spain), or have associated with one or more MTOs to complete their transactions.

One of the main challenges for any operator in developing an infrastructure for remittances has been the need to deal with the myriad different payment systems that cover the region. Payment systems are clearly a fundamental part of the financial infrastructure and proper functioning of any financial system, as it is through them that funds are transferred between agents[8]. The need for local paying agents in each recipient country has prompted a variety of responses from the participants in the remittance market, with the diversity reflecting both their own business models and the financial context in each recipient country. Having been on the fringes for many years, MTOs are at pains to point out that they now comply with the requirements of payment systems in the countries where they operate, and their transfers go through local banking institutions or the banking payment system (see BIS, 2007). MTO-transfers are thus more integrated into the financial system than before.

Payments systems in the region are diverse and MTOs, though now more closely integrated than before, are another complexity. There are gains to be had from harmonisation, particularly across borders

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Latin America still has a plethora of payment systems which do not integrate well, if at all. Harmonising these is a priority for promoting financial integration in the region. A number of initiatives are currently under way in this regard[9]. One of the most successful in promoting cross-border bank-to-bank transfers is *Directo a México*, established between the US Federal Reserve and the Bank of Mexico specifically to handle remittances. *Directo a México* was conceived as an account-to-account service using a common payment system and marginal transaction costs are therefore low. As a result the scheme can offer highly competitive exchange rates to clients[10]. Another feature of the scheme is that these exchange rates and the charges for a transfer are independent of the transfer amount. The success of *Directo a México* suggests that a similar platform should be considered for other remittance corridors in the region.

Bilateral agreements between institutions or at a national level are useful. Cross-border accords are needed though

Financial institutions in OECD countries have recently been active in reaching agreements with institutions in the remittance-recipient economies. Efforts to reach agreements with financial institutions in the migrant's country of origin have multiplied, generally either seeking to "twin" institutions (particularly among co-operatives) or as joint venture or commercial agreements (for example with local MTOs). These have had some impact on prices and scale economies. Other agreements have looked to respond to regulatory demands in the recipient countries, by creating alliances with local actors that comply with these requirements. In parallel with these agreements at the level of the individual financial institution framework agreements between industry bodies or regulators have developed. An example is the agreement reached by the Spanish Government in 2007 with the Spanish Banking Association (AEB) and the Spanish Confederation of Savings Banks (CECA) with the aim of facilitating money-transmission services and reducing costs. Another is the initiative of the Central Bank in Ecuador to make it easier for co-operatives to access the national payment system. These, though, are still only national agreements. More effort is needed to secure cross-border accords.

Going Further: Ways to Enhance Bankarisation

One of the main obstacles to bankarisation through remittances is the weakness of the banking system in the remittance-receiving country understood in terms of depth, coverage and utility for the recipient family, comparative indicators of which were provided earlier[11]. Differences in financial infrastructure mean different bankarisation strategies are needed throughout Latin America and the Caribbean. Furthermore, the factors influencing the attractions of bankarisation depend on country-specific conditions such as the form and level of taxes on financial transactions.

The use of post offices as a base for enlarging remittance services has found a number of advocates in recent years. Post offices certainly have a significant level of coverage among the population in some countries. However, (and often for this very reason) exclusive legal arrangements between post offices and international MTOs can be anticompetitive and encourage the development of remittance monopolies. There are signs of this in some African countries today.

Remittances do not of themselves guarantee financial inclusion at either the sending or receiving end

It is estimated that, although 80% of migrants sending remittances have a bank account, only 20% of remittances are sent through banks. Similarly, only 43% of remittance-senders have a bank account in their country of origin. Globally, Latin American and Caribbean migrants are in the median range of groups using the banking system for their transfers. These differences are signs of some mistrust on the part of senders or recipients about the banking system.

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Migrants may avoid the banking channel for many rational reasons. High charges, either because of regulation or the low density of the financial system, is an obvious example. Taxes on financial transactions can also be a significant push towards informal channels in some countries[12]. To these can be added the multiple administrative requirements for opening a bank account or getting access to credit, and (often) the lack of financial products tailored to the rural situation.

How have financial institutions attempted to encourage bankarisation? Agreements between banks and co-operatives with local counterparts have been a first step. Governments' support for this objective has been crucial. Account-to-account transfers are a first step in encouraging other forms of engagement between the beneficiaries and financial institutions, and there has been some success in promoting these: there was an increase, for example, from 4 to 20% in their share of total transfers from Spain between 2005 and 2007. Various programmes can then seek to build on this initial relationship, for example clients of Banco de Crédito del Perú can use remittances as credit guarantees and other institutions have introduced insurance plans for their clients. An innovative instrument introduced by some institutions, which has enjoyed some success, is the *remesa finalista*: a remittance in which the sender specifies the use to which the money will be put[13]. And it is certainly the case that when remittances arrive through the banking system they have a higher probability of staying within it.

Promotion of account-to-account transfers has seen their share rise from 4 to 20% in Spain

The feminisation of remittances to Latin America and the Caribbean – the growing role that women play in the transfers sent – is to a great extent explained by the current economic crisis. Gender differences in the amounts and frequency of migrants' transfers were observable in Latin America before the current crisis: proportionately more remittances were initiated by women and they also tended to transfer more than men. Still, the gap today appears to be widening. In Spain women are responsible for about 60% of total remittances sent though they account for less than 60% of the migrant population[14]. Differential unemployment rates between male-dominated sectors such as construction and female-dominated ones such as domestic service and care giving is a factor behind this shift. This increasing female engagement contrasts with the traditionally low access of women to financial services in developing countries[15]. In spite of it, however, the lack of specific products directed towards women is still notable. Micro-finance initiatives – which often target women – have contributed to narrow this financial gap, but much remains to be done.

Analysis of remittance flows suggests that they are dependent on external macroeconomic fundamentals, like the exchange rate. Though stable compared to other flows workers' remittances can suffer when the exchange rate of the target currency appreciates against the sending one. Remittance recipients can see their real purchasing power eroded, or may worry about possible future fluctuations. This creates a potential role for governments in providing instruments that at least smooth proceeds from remittances. These could involve transfer of currency risk from migrants to an official body or through commercial hedging. Just as Stabilisation Funds have been set up to deal with excess returns during commodity-price booms, a similar fund could be established to ensure that recipients collect remittances on the basis of a long-term, less-volatile exchange rate, with the condition that transfers are through bank channels[16]. By doing so governments would mitigate currency risk while promoting bankarisation.

Given the observable impact of currency fluctuations on remittances, there may be a case for promoting instruments to mitigate this risk

Learning From History

There is nothing new about sizeable remittance inflows (Esteves and Khoudour-Castéras, 2009; see Box 4.1). In the mass migration period of 1870-1913 proportional migration rates for many countries exceeded those witnessed today

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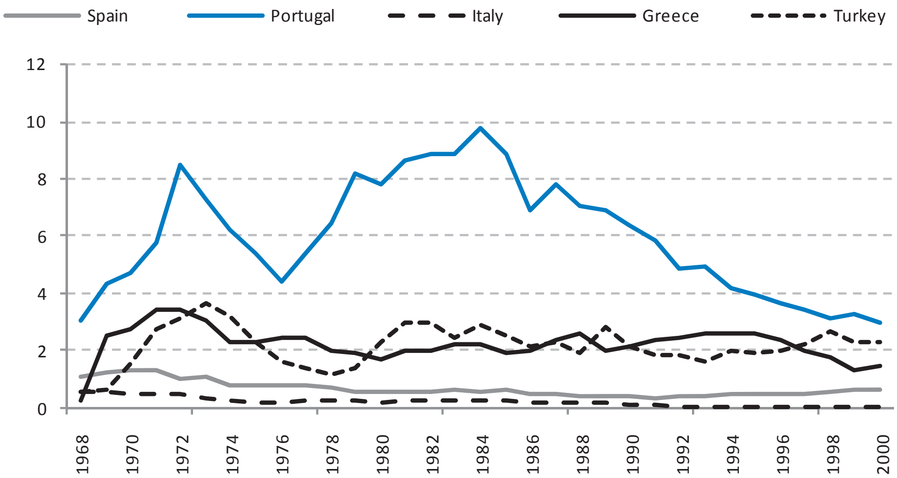
and were accompanied by the development of sophisticated financial services to address migrants' needs. More recently, Greece, Italy, Portugal, Spain and Turkey experienced migration booms from the 1960s, accompanied by upsurges in remittance flows. In fact, it was only at some point between 1950 and 2000 that individual southern European countries switched from being countries of origin to countries of destination (Venturini, 2004). This long experience of emigration left them recipients of remittances for many years, as shown in Figure 4.4. In the case of the southern Mediterranean countries remittances continued to rise until the early 1980s[17].

Figure 4.4 Incoming Remittances for Selected OECD Countries
(Percentage of GDP)



Source: Venturini (2004).

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The mechanisms used to send these remittances are similar to those seen today. Venturini (2004) identified four main channels used: formal financial transfers (through banks, post offices and so on); informal transfers through unofficial networks; buying and sending goods directly; and transfers by means of a system of financial compensation.

The 20th-century experience of remittance receiving countries in southern European countries is instructive. Their policies, though, reflect the very different financial framework of the time

Among these countries can be found policies through which remittances had an impact on the financial system. Some OECD countries offered incentives including bank accounts aimed at remittance-senders, for example, offering higher interest rates or lower credit barriers. Spain, for instance, had a most highly developed system. Its "convertible-peseta" policy allowed non-resident nationals to hold bank accounts denominated in foreign currencies with the aim of encouraging the repatriation of remittances. To this end, the Spanish government also provided tax benefits to migrants who opened convertible-peseta accounts[18]. Although the Spanish model was successful in encouraging remittances, it is unlikely that it could be replicated today given how it relied on its context of substantially less liberal financial markets. Moreover, the model was based on the expectation of high rates of return migration, which, as Chapters 2 and 3 of this *Outlook* illustrate, may not hold today. It also required migrants' trust in the financial system of their country of origin.

As remains the case, migrants then chose to remit via the banking system if it was the best among the options available to them, importantly if bank branches were conveniently located for them in the host country and their relatives back home. When they chose to remit through the banking system, remittances promoted banking development in these OECD countries; at the same time, more developed banking systems encouraged greater use of official channels (banking and MTOs) by remitting migrants. The growth in the banking network of Greek and Italian banks, for example, had a positive effect on remittance flows by Albanian migrants through official channels during the period 1994-2006 (Karafolas and Sariannidis, 2009).

Policy makers must reassess the structure of incentives that encourage or discourage bankarisation and the extension of banking services to populations traditionally excluded. Favouring the development of agreements among financial institutions is a first step. More importantly, the provision of instruments targeted towards the migrant population of the type described above merits further consideration.

Policy should promote incentives for extending financial services to new sectors of the population. Facilitating agreements between financial institutions is an important first step

Box 4.1. The Impact of Remittances on Pre-1914 European Financial Development

Surprising as it may seem, sending money home before World War I was not much more complicated than it is today. The business of international money transfer developed rapidly during the second half of the 19th century to meet the growing demand from transatlantic migrants. The vast amounts of money transferred home as a counterpart to the mass migration in this period contributed to the development and penetration of financial services in countries of destination and of origin. Concentrating on the latter, Esteves and Khoudour-Castéras (2009) studied a sample of then-emerging economies on the European periphery characterised by large emigration flows. Their results imply that remittances had a significant impact on financial development, measured as the ratio between total deposits in the banking system and GDP. They also found that migrants' transfers during the mass-migration period (broadly speaking 1870-1913), did more to promote the domestic financial sector than other international capital flows. This positive influence of emigrants' remittances can be explained through a triple process of institutionalisation, densification, and bankarisation.

At the beginning of this period, most migrants used informal transfer channels. They could send coins and banknotes through registered or ordinary mail. They could also entrust envelopes of money to a friend or family member travelling back home, or carry their own savings when returning (Douki, 2001; Magee and Thompson, 2006a). But as the number of migrants increased, a growing demand for more formal channels emerged. As a result, new actors appeared in the remittance market, giving rise to a gradual process of "institutionalisation", that is, the development of a structured network of financial intermediaries. In Spain for instance, mercantile houses entered the remittance business, and progressively turned into banking houses or became integrated into the branch network of national or foreign banks (García López, 1992). New banks, oriented towards the remittance business, also appeared, such as Banco Hispano Americano in 1901 (today part of the Santander group). In Italy, the institutionalisation process was encouraged by public authorities through a 1901 law on emigration that aimed at channelling remittances through official financial institutions, namely by expanding the post office network in rural areas (Douki, 2001).

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At the same time, financial institutions began to open more branches and to offer more services, which contributed to the "densification" of the European financial sector. New banks appeared to answer the growing demand for money transfers and to attract returnees' savings (Alves, 1993; García López, 1992). Local operators also faced competition from national banks interested in capturing a share of the market, as in Italy with the territorial expansion of the Banca Commerciale Italiana, the Banco di Roma, or the Credito Italiano (Douki, 2001). Foreign banks entered domestic markets too, such as the Banco Español del Río de la Plata, an Argentinian bank that set up several branches in emigration-intensive areas in Spain.

Remittances also helped many families to gain access to banking services, thereby accelerating the bankarisation process in European countries. The need for faster and safer international transfer channels, for example, increased the demand for account-to-account transfers, and consequently for deposit accounts both in sending and receiving countries. In addition, the recipients' ability to save part of their remittances, as well as the increasing number of returnees, favoured the development of savings accounts (Magee and Thompson, 2006b). Financial institutions adapted to this new clientele by offering attractive interest rates and, as a result, the number of account holders significantly increased. Italy saw the share of emigrants' savings in total postal accounts rise from 0.03 to 4.4% between 1890 and 1913 (Istat, 1958).

Compared with the contemporary findings of Aggarwal *et al.* (2006), Esteves and Khoudour-Castéras's results imply that the contribution of remittances to financial development was higher in pre-1914 Europe than in today's developing countries. Part of this can probably be put to the lower starting levels of development in the historical sample. But it also means the potential for positive spill-overs from migration to financial development could still be enhanced in present-day developing economies, not least by policies aiming at promoting financial democracy. In particular policies that facilitate access to banking services, provide information about the remittance market, and help to guarantee the transparency of the financial system could act as catalysts (Orozco and Fedewa, 2006; Terry and Wilson, 2005).

REMITTANCES AND MOBILE BANKING

Mobile payments represent a new and rapidly developing form of financial service. Operators are active throughout the region

Remittances represent not only flows of money; they can also be a catalyst for innovation. A potentially important example is the growing use of mobile telephony to undertake banking services, including international transfers of funds. This is a classic case of innovation from multiple perspectives: mobile payments and mobile banking represent the development of new business models, as well as the application of a recent technology – the mobile telephone – to new economic problems. Could remittances bolster this innovative new sector?

The emergence of new technological platforms has been a major transformation for the money-sending business model (as the telegraph was for the 19th century institutions in Box 4.1). Today, using "mobile payments" a person can use his or her mobile phone to pay for items in a shop, settle a restaurant bill, receive government payments and, not least, transmit money to and from other mobile-phone users. This type of transfer has the potential to become an essential tool for remittances. Recuero Virto (2009) provides a comprehensive analysis of the impact of mobile payments and mobile banking on remittances, contrasting the experiences of African and Latin American countries. While bank branches and cash machines reach barely 10 to 20% of the population in Latin America, 80% in the region have a mobile phone number. A key element of success of mobile payments is indeed the size of their distribution networks. Moreover, transaction costs, currently around 9% on a payment of USD 200, could be substantially reduced through increased competition given the low (marginal) capital and operational costs of mobile payment operators.

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The rollout of mobile payments services are typically led by either banks or mobile-phone companies. Mobile solutions have been offered by banks in countries such as Argentina, Brazil, Chile and Mexico, mainly for accessing account information. Countries including the Dominican Republic, Paraguay and Venezuela, in contrast, are implementing mobile payment solutions led by telecommunications operators.

Among the bank-led initiatives only in relatively few cases, notably Argentina and Colombia, are payments possible. These solutions are instead typically directed towards users already having a bank account, adding a new distribution channel to the traditional ones of branches and ATMs. The extent to which bank-led models fully integrate telecommunications solutions will define the magnitude of their future customer bases in Africa and Latin America and the Caribbean. Banks need to capitalise on the size of mobile networks (or some other large distribution network such as supermarkets or lottery kiosks) to handle cash payments in and out, if they are to access the non-bankarised population on a large scale.

The term "mobile banking" commonly just refers to mobile payment services. In fact the term covers a wider range of services and customers can often check balances, transfer money between current and savings accounts and so on. Absent at the moment are good ways to integrate deposit making into this mix in order to complete a true banking offering. Partly this is because mobile banking initiatives have been led by telecoms operators whereas it is the banks who are naturally placed to take deposits. However neither banks nor mobile operators (both enthusiasts for profitable mobile payments services) are leading the way in expanding into deposit taking. Hence, while the major bottleneck for mobile payments is regulatory, for mobile deposits the problem lies with the ability and willingness of governments to provide adequate incentives for private entities to deliver these services[19].

A challenge will be to expand mobile payments to true mobile banking and to use this as a springboard to wider financial integration

Why Mobile Payments? Size Matters

The key reason for the success of mobile payments is the size of mobile operators' distribution networks. The value of this is greatest – and mobile payments most likely – in countries where access to bank branches and cash machines is low. Figure 4.5 shows the penetration of these traditional payment systems: 10% on average, though slightly higher in the Caribbean. As noted above, the size of these networks is much lower than that of mobile phone operators, which reach about 80% of the population[20].

Mobile payments for remittances have been deployed very successfully in sub-Saharan Africa[21]. Mobile phones in this region provide access to communications to around 40% of the population, while bank branches and cash machines density remains low. The commercial success of these initiatives in sub-Saharan Africa suggests that there is a scope for a similar service in rural areas of Latin America.

One of the competitive advantages of mobile payments is their reach: which is precisely what makes them so interesting for extending coverage

Mobile payments in Latin America have so far only reached customers who already have a bank account. Examples of such mobile payment systems are found in Argentina (*Red Link*), Colombia (*Redeban Multicolor*) and Mexico (*Nipper*), however these are at an embryonic stage, compared to the use of this technology for receiving alerts or accessing bank account information[22].

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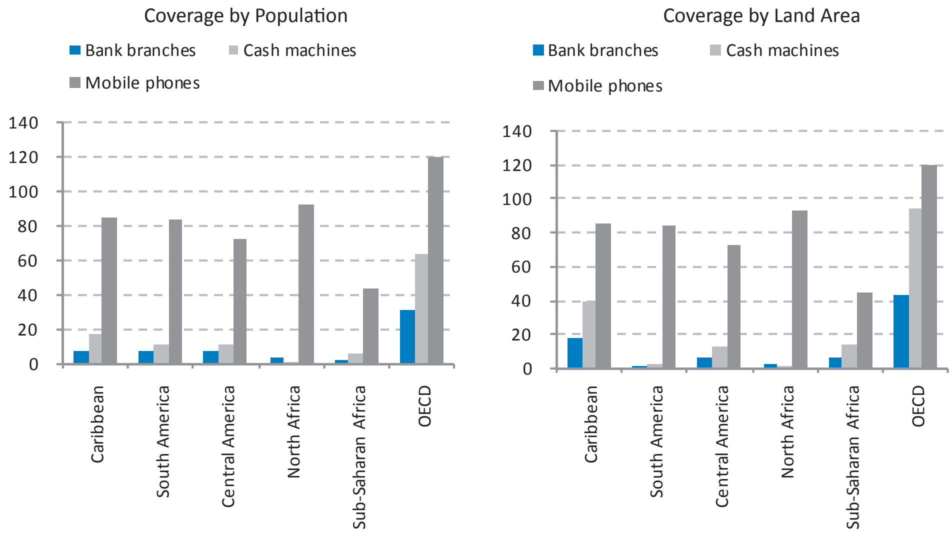
Figure 4.5. Distribution Networks – Demographic and Geographic Reach



Note: Geographic branch penetration and geographic ATM penetration refer to the number of bank branches and ATMs per 1 000 km^2, respectively. Demographic branch penetration and demographic ATM penetration are defined as the number of bank branches and ATMs per 100 000 people, correspondingly. For mobile phones, coverage refers to the number of mobile lines per 100 inhabitants.

Source: OECD Development Centre, based on Recuero Virto (2009).

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Some pioneering mobile solutions are being implemented for the non-bankarised: initiatives in international payments for example include *Halcash* between Spain and Ecuador and *Celexpress* between the United States and Colombia. In neither of these two cases, however, is the mobile contribution being fully exploited. Better examples (with operator name in brackets) may be found in Paraguay (Tigo), the Dominican Republic (Orange), Venezuela (Diemo) and Jamaica (Mobile Money). These two groups highlight the differences between bank-led and operator-led payment systems. Bank-led mobile payments tend to use mobile technology as an additional distributional channel, and hence typically do not implement business solutions that fully exploit the availability of a large network (through the mobile operator) for small cash transactions. Operator-led payment solutions target mobile phone users – who are not necessarily bankarised – and allow them pay cash in and make withdrawals through mobile network distribution points, including (potentially) any kiosk or shop that sells prepaid cards.

Why Mobile Payments? The Cost Advantage

Mobile payments are also very attractive for the sending of small payments given their low marginal cost base

High transaction costs in remittances can justify the use of mobile technology. Figure 4.6 displays percentage transaction costs when sending USD 200 to Latin American and Caribbean countries using MTOs and banks. Each point represents a particular corridor, for example money being sent from the United Kingdom to Brazil, or from Spain to Colombia.

While costs are very similar in the case of MTOs, they can vary substantially between banks[23]. On the other hand, the extent of competition, measured by the number of firms serving the corridor, appears to reduce costs to the customer more markedly in the MTO market than in the bank market.

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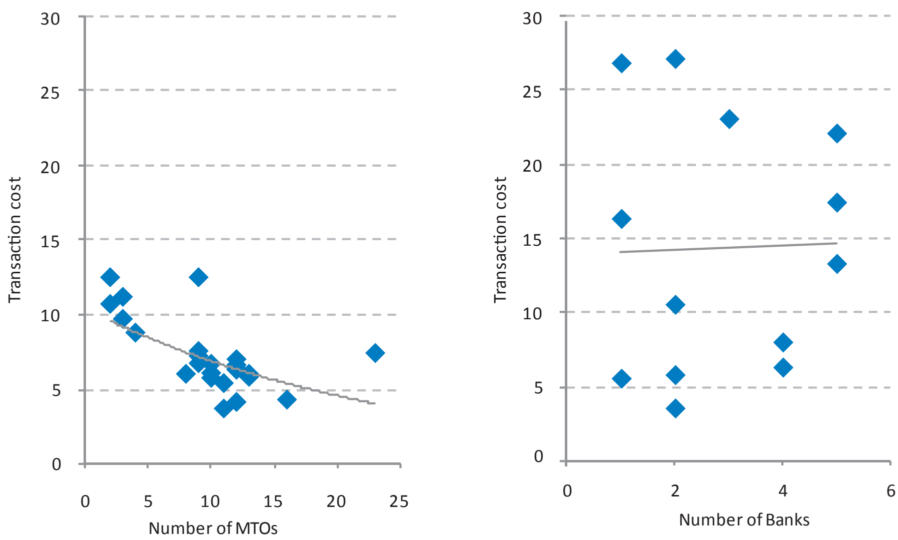
Figure 4.6. Transaction Costs for Money Transfer Operators (MTO) and Banks – USD 200
(Percentage of total)



Note: The x-axis is the number of institutions (MTOs or banks respectively) serving each corridor in the sending country. Transaction costs are the total costs of sending and receiving USD 200 along a given corridor. The trend line is shown.

Source: OECD Development Centre calculations, based on Recuero Virto (2009).

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Competition from outside the banking sector appears to be driving down transaction costs down in Latin America and Caribbean, a result consistent with the African experience noted earlier. Moreover, when comparing differences in transaction costs between countries with a high and low presence of MTOs, it is clear that costs are lower in countries where MTO competition is higher. Market conditions in the sending country appear to a large extent determine total transmission costs. In Latin America, the average sending cost from countries with low MTO presence (such as Canada, France or Japan) is about 15.5%, whereas in countries with high MTO presence (Spain, the United Kingdom and the United States) the average cost is only 6.6%.

Big Customers, Small Customers: Adapting to Both Ends of the Market

MTOs' lower cost-bases enable them to offer attractive rates for small payments. Mobile payment services may enjoy even lower marginal costs

The size of a remittance is an important determinant of the proportional cost of the transaction. For both banks and MTOs for example the proportional cost of sending USD 200 is more than 5 percentage points higher than sending USD 500[24]. Banks are still more expensive for the larger amount, but the gap between the two closes. This illustrates that banks' international money-transmission networks have historically arisen to serve the needs of relatively large (often commercial) transactions. They have high fixed costs, relatively small networks – concentrated in centres of commerce rather than population – and low economies of scale. MTOs, being new entrants, were able to design networks tailored for retail clients and frequent small transfers. Banks have required a change in their business model when seeking to address low-margin, high-frequency retail business. To do this some banks have entered into agreements with MTOs, seeking to trade the bank's infrastructure against the MTO's standardised procedures. The bank keeps its portfolio of customers and can at the same time benefit from accessing low-income consumers or those without a bank account[25].

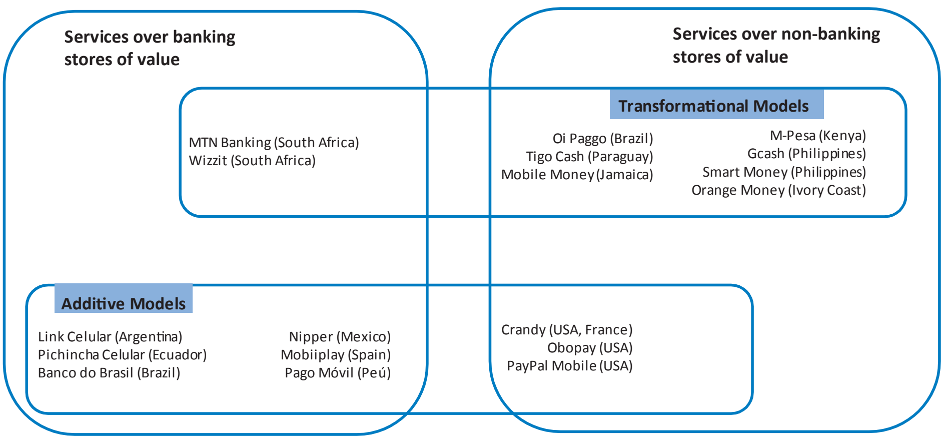
Mobile technology can undercut even the MTOs for very small transfer amounts and may do to their market what they have done to the banks[26]. Mobile phone operators are competitive when transferring small amounts because their marginal costs both in transmission and in money handling are low (vanishingly small, in fact, in the short-term for a fully automated payment made by a network SMS-type message.) Their networks are built and they are already required to maintain a cash-based network to receive payments for network services. Seen as an adjunct to their existing voice (and data) communications business, the economics can be enticing.

Regulation: The Major Bottleneck for Mobile Banking

There is no single model for mobile payments: some are led by telecoms operators, some by banks

For the time being, regulatory flexibility has permitted the emergence of a wide range of technological solutions for mobile payments[27]. While these varied technological solutions continue to spread under the monitoring of the authorities responsible for the regulation of telecommunications and financial institutions, there is a belief that there may eventually be a "standards war" and a dominant model may emerge. As noted earlier and shown in Figure 4.7 below, there is similar diversity in the business structures: some are bank-led, others operator-led, and some are joint ventures between the two. On this side of the equation, some involvement from an established bank does seem to lend the enterprise credibility.

Figure 4.7. Organisational Structures for Mobile Payments and Banking



Source: Analistas Financieros Internacionales (2009).

Regulation is a hurdle to the transformation of mobile payments into mobile banking, whether covering money laundering, the use of agents or deposit taking

In fact the main regulatory bottleneck is independent of technology or business structure. It stems from the increasingly tight international anti-money laundering (AML) regulations and those designed to combat the financing of terrorism (CFT)[28].

Non-bank agents in the market for mobile payments – shops, pharmacies, post offices and so on – require special attention from regulatory authorities. Mobile phone operators' large distribution networks constitute their main potential competitive advantage in payment services. Without an enabling regulation to permit these non-bank agents to undertake deposit and withdrawal transactions,

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operators' capacity to exploit their advantage will be hampered. Such regulations would not be completely straightforward. They may need, for example, to define the classes of business or business structures which are to be eligible, which services they can provide, whether an agent can act for multiple networks, who is responsible in case of conflict, where confidential information on customers is stored and what security measures should apply.

Fortunately, some regulations covering non-banking agents already exist in many Latin American and Caribbean countries: Brazil (since 1973), Bolivia (2000), Peru (2005), Colombia (2006), Ecuador (2008) and Mexico (2008). Brazil has the most extensive non-bank agent network, with 32 100 service points (including grocery stores and lottery kiosks) across the country, delivering payment services from Caixa Econômica Federal, Bradesco, Banco Lemon and Banco Popular.

The third regulatory issue that constrains the development of mobile payments is the increasingly blurred distinction between payments (in respect of a specific transfer) and deposits (to create a fund of money which can then be transferred). Most of the current operators do not (explicitly) accept deposits, in order to avoid being caught by deposit-taking regulations. However, the practical difference between providing payment or deposit services mostly relies on the time that the money spends in the system. Mobile operators, therefore, frequently argue that any existing balances are purely transactional in nature and do not constitute a deposit.

From Mobile Payments to Mobile Banking?

Can mobile payments lead to higher bankarisation in Latin America? One enabling feature is that mobile payments create a financial history for a customer who would otherwise not have one, and so be the gateway to credit assessment and access to loans.

To date, the rise in mobile money has been largely related to payments. Only marginally do these activities promote bankarisation. Banks have mostly ignored the opportunity to convert remittances into deposits, reflecting the higher administrative costs and lower profit margins in their business model associated with managing a large number of very small deposits. Mobile operators, on the other hand, are unwilling to take deposits and get drawn into the associated (and often onerous) regulatory regime. These are both areas where the right policy decisions could harness what is a large and growing business to the service of bankarisation.

Regulatory policy, carefully applied, may help shape the future of mobile payments to the greater benefit of development

LEVERAGING REMITTANCES

The remittance phenomenon is not new, and much can be learnt from the past. Experiences from the end of the 19th century and the period after World War II, from countries with high emigration flows such as Spain, Italy, Greece or Portugal, highlight the importance of generating an *incentive structure* that encourages the migrant to send money home, and particularly to send it through formal channels. Some of the measures for encouraging formal channelling of remittances through banks will not be applicable today (foreign-currency accounts, like Spain's convertible-peseta initiative for example). But others are proving themselves effective in attracting the migrant client today. Examples have been given above and Chapter 6 of this *Outlook* summarises these and their implications for policy making.

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To secure the greatest benefits from remittance flows, governments should promote transparency in the transmission market and provide financial literacy

Remittance flows have been increasing for many years now and have long been believed to present an invaluable opportunity for expanding access to the financial system for traditionally excluded households in the region. The results however have been relatively modest; nevertheless, there is a better understanding of the factors that hinder remittance senders and recipients from making use of formal financial services. Initiatives for encouraging bankarisation have been implemented (such as account-to-account transfers, *remesas finalistas*, induced bankarisation) with greater or lesser success. Certainly the operational frameworks and services provided are increasingly taking into account the needs of the migrant. Increase financial literacy among sectors with traditionally limited access to financial services will be a vital part of building on this, but guaranteeing competitive and contestable markets in the money-sending business is also important and in many senses its complement. Thus transparency in the remittances market could be a catalyst for bankarisation. Markets will be contestable if policy makers ensure that information regarding prices, suppliers, and other relevant factors are widely available. Costs can be driven down by encouraging agreements between financial institutions in the sending and recipient countries.

New instruments to smooth currency fluctuations could both encourage remittances and their formalisation

Carefully designed stabilisation pools or the use of currency derivatives can guarantee remittance proceeds in domestic currency for the retail client. Involvement in such a scheme brings the migrant's bankarisation as an almost automatic counterpart. By offering (or promoting) such a scheme governments mitigate the currency risk for remitters while promoting formalisation in the sending channels.

Mobile payments may develop as a spur to bankarisation or an alternative to it. Broader distribution and lower sending costs are the two main arguments in their favour. To what extent mobile payments can be extended to mobile banking depends on defining a clearer regulatory framework for these institutions which sit somewhere between telecommunications and finance.

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NOTES

1. King and Levine (1993), Levine and Zervos (1998) and Beck *et al.* (2000) document how financial development is associated with higher growth. Moreover, Beck *et al.* (2004) have shown that financial development also leads to lower levels of poverty and inequality.

2. See Kanaiaupuni and Donato (1999), Hildebrandt and McKenzie (2005), Duryea *et al.* (2005) and López-Córdova (2005).

3. Regarding education and human capital, Cox and Ureta (2003) showed for El Salvador, Yang (2006) for the Philippines, and López-Córdova (2005), for Mexico that household constraints are reduced through remittances and associated with improved schooling outcomes for children (Aggarwal *et al.*, 2006). Similarly, in Colombia remittances affect educational inputs, with beneficiary households spending about 10% more on education than non-beneficiaries.

4. See Aggarwal *et al.* (2006) for further details on the mechanisms linking remittances and financial development. Giuliano and Ruiz-Arranz (2005) and Mundaca (2009), meanwhile, show that the impact of remittances on growth can depend directly on the country´s level of financial development.

5. Financial literacy programmes have been introduced in some countries to fill this gap. Particularly for groups such as migrants that have traditionally been overlooked by the financial system financial literacy is important to orientate them about basic financial services and asset-building programmes, credit management and repair, home ownership, small business and micro-enterprise technical assistance, among others.

6. In each of Bolivia, Brazil, the Dominican Republic, Mexico, Panama, Peru and Uruguay the three largest commercial banks account for more than 60% of total system assets. See Beck *et al.* (2000, updated November 2008) and Micco and Panizza (2005).

7. The OECD Development Centre, the Spanish Ministry of Finance and the Ministry of External Affairs and Co-operation held a conference in 2007 to get saving banks, money transfer operators and other institutions to share their experiences in this area. The meeting, under the title "Remittances and their impact on development finance: Analysis of the operating framework" (*Remesas y su impacto en financiación para el desarrollo: Análisis de los Marcos Operativos*) formed part of a broader initiative of the Spanish government and others to encourage more productive use of migrants' transfers in their countries of origin. Similar initiatives have been undertaken in the United States, France, the United Kingdom and other OECD countries.

8. These systems can be classified along a number of different dimensions. They are *minor* for payments by the public through cheques, transfers and direct debits. They are *major* for operations between financial institutions or with the central bank, and financial transactions in the financial markets. Also, payment systems can also be *domestic* or *transnational*. Remittances fit into the category of minor, transnational payment systems. Payment systems can also be classified based on the transaction amount (high value v low value systems), time (real time v delayed) and compensation and liquidation mechanism (net v gross) (Analistas Financieros Internacionales, 2009).

9. In 2002 the Bank for International Settlements published *Core Principles for Systemically Important Payment Systems*, which has since provided the framework for the reform and modernisation of existing payment systems. Initiatives in Latin America have followed this framework, see for example *Comité Monetario Centroamericano* (CMCA), or the *Foro Permanente de Liquidación de Pagos y Valores del Hemisferio Occidental* (FHO) (Analistas Financieros Internacionales, 2009).

10. Currently, the rate offered is the official interbank exchange rate (FIX) less 0.21%.

11. See Alberola and Salvado (2006) for a more theoretical approach to the money-transmission market and its impact on financial development.

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12. Six countries in Latin America (Argentina, Bolivia, Brazil, Colombia, Peru and Venezuela) have recently introduced taxes on financial transactions. These were initially meant to be temporary but have been extended in the light of their contribution to government finances.

13. Some of the initiatives encouraging a long-term use of remittances at the household level are promising. Colombia through its programme *Mi Casa con Remesas,* Peru with the *MiVivienda* fund, and El Salvador through its Chamber of Industry and Construction have all sought to direct remittance flows towards local housing projects. Involving local construction firms and banks, these programmes encourage migrants to acquire housing in their countries of origin by allocating part of their own remittances. The housing fairs launched in focal points for Latin American migrants (New York, Los Angeles, London and Madrid) highlight their potential as a source of housing finance in areas where the shortage of capital is acute.

14. See More *et al.* (2008).

15. In Moldova, for instance, Orozco (2007) finds that although 65% of recipients are women their access to bank accounts is much lower than that of men. See also Armendáriz and Morduch (2005) and World Bank (2007) for gender differences in access to financial services.

16. Of course, a minimum set of conditions are necessary for the implementation of such a programme. First, any agreement between financial institutions (or pool of households) and governments would have to be long-term, and contain an exit cost for users to dissuade speculation. Second, the determination of the appropriate exchange would need to rely on quantitative parameters looked at on a long-term basis and quite independent of any political pressure. Third, given the volatility of remittance flows it would be possible to hedge only a proportion of these flows against foreign exchange risk.

17. To put these in context, by the end of the 1970s, for instance, the flow of remittances to Portugal was 10 to 17 times higher than foreign direct investment. Equally high rates were recorded for Turkey.

18. The greatest remittance booms experienced by Spain were in 1944-48 and 1953-59, largely driven by contemporary economic booms in Argentina and Cuba. See García López (1989).

19. Some experts view regulation in mobile payments as a precondition of business development rather than an enabler.

20. Strictly speaking, there are 80 mobile phone lines per 100 inhabitants. In practice, a single individual may have two or more perhaps to separate professional and personal use or to avoid cross-network charges when calling.

21. Successful examples of mobile payments in Africa are led by mobile operators: notably M-Pesa in Kenya and MTN Mobile in South Africa.

22. Brazil has 474 000 users capable of accessing bank information by mobile phone, Mexico 134 000 and Chile 87 000.

23. The most expensive is the corridor between the Netherlands and the Dominican Republic, where bank charges amount to 26% of the remitted amount. In the corridor between the United States and El Salvador, in contrast, bank charges total only 3%. Concrete examples of recent commercial offerings drawn from the corridor between Spain and Latin America are BBVA's *Dinero Express* service and Santander's *Santader Envíos*. The former charges a flat tariff of EUR 5 if the amount is cash, and EUR 3 if the transaction is carried out from a bank account, for transfers of up to EUR 3 000 with these charges waived for senders who sign up for a BBVA current account product. (Additional commissions are payable by the recipient.) Santander's service allows up to three free payments per month to a maximum of EUR 2 000 for those clients maintaining a bank account.

24. In the case of banks, sending costs rise to 11.1% (for USD 200) from 6.1% (for USD 500). The corresponding figures for MTOs are 7.2 and 4.9%.

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25. Banco Salvadoreño, the second largest commercial bank in El Salvador, is a practical example of the link between MTOs and banks. Banco Salvadoreño is present in most US states through strategic alliances with some of the biggest MTOs, including Western Union and Bancomer Transfer Services. The largest example globally is provided by the agreements between Western Union and La Poste across many African countries.

26. Indeed, in the most developed mobile transfer so far, Kenya, it is ten times cheaper to send EUR 9 through the mobile network M-Pesa than through an MTO. While M-Pesa charges 5% commission, a typical MTO would take 50% of such a small amount.

27. Three groups of solutions have emerged: Unstructured Supplementary Services Data (USSD) and the Subscriber Identity Module (SIM) toolkit, both of which use standard handsets, and Wireless Application Protocol (WAP) technology which requires an enhanced handset. USSD has been adopted by Tigo in Paraguay and permits the use of an open system independent of the mobile network operator. SIM toolkits are used in Mexico (by Banamex and Telcel). These are proprietary systems under which only members of the mobile operator's network can transfer funds. WAP is in use in Mexico (Nipper).

28. Among the AML and CFT norms, "know your customer" (KYC) requires due diligence on the individual making the transaction; such requests may not be straightforward in informal situations. AML/CFT requirements also limit daily and monthly transaction amounts. An initial pilot developed by M-Pesa of Kenya to receive payments from the United Kingdom was ultimately abandoned as a result of difficulties in complying with AML/CFT.

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CHAPTER FIVE

Remittances and Capital Markets in Latin America

By any measure, remittance flows are large. Do domestic financial institutions, and the capital markets at large, take full account of their benefits?

In many Latin American and Caribbean economies low levels of domestic savings or underdeveloped private capital markets have made foreign lenders more reliable suppliers of capital than domestic sources. This chapter asks whether remittances could do something to improve this situation. There is an analogy to their microeconomic role discussed in the preceding chapter: receipt of remittances reduces the vulnerability of households, lessening the risk that they will fall into poverty when hard times hit the home economy. Likewise, inflows at the macroeconomic level which tend to be among the least volatile of foreign flows can make entire economies more stable. Do the actors in the capital markets in recipient countries – the government and major banks at least – take full advantage of the opportunities that an inward stream of remittances provides? Do rating agencies adequately take into account this benefit of remittance inflows when they calculate sovereign risk levels? In answering these questions it is appropriate to examine first how remittances affect the development of capital markets in emerging and developing economies. This chapter approaches this from two angles: first, the financial effect and, second, the impact on sentiment.

On the financial side, remittances, or more generally the income received by migrants, are central to two kinds of securities: the securitisation of future flows of remittances and "diaspora bonds". Under the first of these a specially created financial instrument relies for interest and principal on the flows coming in from abroad through the financial sector of which remittances are a major part. Diaspora bonds are an issue of debt specially tailored for and marketed to a community of home-country investors resident abroad. The first of these securities thus depends on the remitted revenues of migrants, while the other creates a new investment vehicle for their capital.

The core of this chapter analyses the impact that remittances may have on the sentiment side of capital markets. It looks into two key channels of the balance of payments in which remittances may affect markets' perception of emerging economies: external solvency and volatility of external flows. In particular, this section studies the rating agencies – critical actors on the international capital markets – and seeks to analyse the impact of remittances on the ratings they generate. As part of this exercise, "shadow ratings" are calculated for countries not covered by the rating agencies which nonetheless have high levels of remittances.

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SECURITIES AND REMITTANCES: TWO WAYS TO BOOST CAPITAL MARKETS

Future-Flow Securitisations: Getting Value for International Operations

A "future-flow securitisation" is a debt instrument whose payment of principal and interest to investors is secured by flows on future receivables. "Diversified Payment Rights" (DPR) issues represent the biggest group of such transactions. These are securitisations of international wire transfers, typically arising from export-related financing, foreign direct investment, portfolio investment and workers' remittances. Workers' remittances can be a significant part of DPR flows for countries with large populations of migrant workers, and this is certainly the case for South and Central America (Standard & Poor's, 2008). In recent years a number of Latin American financial institutions have successfully securitised such flows as a way of raising capital.

Future-flow securitisations can be attractive, since subject flows arise outside the local economy and they are typically denominated in foreign currency

DPR securitisations can be attractive to investors for several reasons. The underlying flows are dollar-denominated and generated outside the emerging economy. This makes them resilient to uneven economic conditions in the issuer's market and helps mitigate sovereign risk – since the obligation to the investors arises before the receivables enter the issuer's home country. Investors are also often attracted to securitisations based on remittances for their acyclical or counter-cyclical nature relative to some Latin American economies: in many cases, workers send more money home during periods of economic crisis in their countries of origin[1]. (This pattern does not hold universally however: see Chapter 2 for an analysis of the relationship between remittances and home country GDP growth.)

Financing costs are the most important (though not sole) motivating factor for DPR issuers. In many cases a DPR securitisation with strong legal and structural elements can achieve a rating that is above the sovereign ceiling otherwise applicable to foreign-currency debt obligations issued directly by such countries. This has brought a number of DPR issues up to investment grade, allowing them to tap large institutional investors such as pension and mutual funds.

Figure 5.1 illustrates these benefits of DPR securitisation using data from the primary market[2]. The righthand panel compares the rating given by Standard & Poor's to selected Latin American DPR issues in 2002-09 with the corresponding sovereign rating (matched for country and maturity). In all cases the DPR issue gets a higher rating. The lefthand panel captures the benefit of this lower perceived risk, comparing the cost at issue of the DPR bonds and equivalent sovereigns. The total yield (bond spread plus zero-risk yield) of the DPR issues is lower than sovereign bonds.

DPR issues can secure funding at lower rates than could be achieved by the relevant sovereign, and may allow access to international markets at a time when they would otherwise be closed

A striking example of how the market views sovereign bonds and DPR issues very differently is provided by a Brazilian DPR issue in June 2002 (the third issue in Figure 5.1). In 2002 the growing success of Luiz Inácio Lula da Silva's presidential bid was perceived as a populist threat to the continuity of the credible economic policies of incumbent President Fernando Henrique Cardoso. Brazilian sovereign bond spreads increased dramatically, investment banks' recommendations shifted to the sell side and rating agencies downgraded Brazil's bonds. In March 2002, the Brazilian government issued its last international bond prior to the election with a rating well below investment grade and at a spread of more than 1 000 basis points in the primary market. From that point

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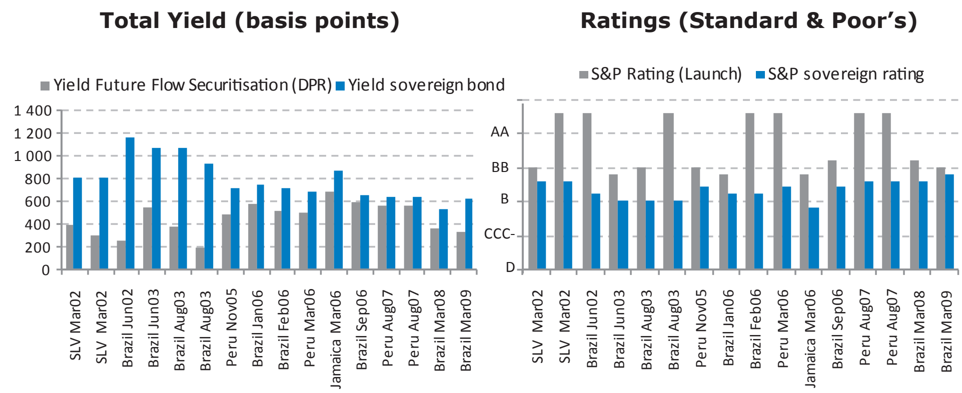
the international capital markets were effectively closed to Brazil as a sovereign issuer. Nevertheless, in June 2002 – in the final approaches to the election – a DPR issue was successfully completed at a yield-spread of around 200 basis points, and with an investment grade rating.

Figure 5.1. DPR and Sovereign Bond Issues at Launch



Notes:

a) The DPR issues, selected on the basis of data availability, covered are (name of the country and date, dd/mm/yyyy, of issue in parenthesis): Banco Agricola DPR Funding Ltd. (El Salvador, 12/03/2002), Banco Agricola DPR Funding Ltd. (El Salvador, 12/03/2002), Dollar Diversified Payment Rights Finance Co. (Brazil 27/06/2002), UBB Diversified Payment Rights Finance Co. (Brazil, 13/06/2003), International Diversified Payment Rights Co. (Brazil, 12/08/2003), International Diversified Payment Rights Co. (Brazil, 12/08/2003), CCR Inc. MT-100 Payment Rights Master Trust (Peru, 22/11/2005), Jamaica Diversified Payment Rights Co. Series 2006 – 1 (Jamaica, 15/03/2006), Brazilian Diversified Payment Rights Finance Co. (Brazil, 20/09/2006), CCR Inc. MT-100 Payment Rights Master Trust (Peru, 02/08/2007), CCR Inc. MT-100 Payment Rights Master Trust (Peru, 02/08/2007), Dollar Diversified Payment Rights Finance Co. (Brazil, 06/03/08), Banco Bradesco SA (Brazil, 23/03/2009).

b) Comparable sovereign issues have been selected for each DPR issue on the basis of country of issue, maturity and date of issue.

Source: OECD Development Centre calculations based on Dealogic and Datastream databases.

StatLink http://dx.doi.org/10.1787/716252278345

Governments may therefore have a strong incentive to promote this kind of securitisation. For a number of low- and middle-income countries, highly dependent on remittances, DPR issues represent a cost-effective and reliable way for their institutions to access international capital markets. DPR issues may also generate beneficial side effects for the countries that undertake them, as they improve the flow of information about those countries' economic and political conditions (Ketkar and Ratha, 2009*a*).

Risks, of course, remain. Some part of future cash flows from remittances is committed to the payment of DPR debt service and as a result issuers must pay recipients of those remittances from their own reserves. A depreciation of the local currency against the dollar or simply their own poor performance (perhaps losses in another line of business) can undermine the ability of a financial institution to meet its obligations to remittance receivers. Standard & Poor's (2008) reflects these in its assessment of the events that can affect the rating given to a DPR issue. They identify two main factors: any change that may affect the performance of financial institutions[3]; and any changes in the cash flows that underlie the securitisations (so that a decline in workers' remittances might prompt a downgrade of an issue that relied on them).

Remittance receivers rely on the credit of the financial institution to see that they receive their funds; DPR holders on the continued flow of remittances

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A programme's debt-service coverage ratio (DSCR), the ratio of its cash flows to its scheduled principal and interest payments, is an important test of the risk associated with any sudden decline in DPR flows. Programmes with higher DSCRs are more able to withstand a sudden decline in DPR flows than those with lower DSCRs. It is fortunate in the current world economic crisis that the risk of fluctuations in remittance flows has indeed been mitigated through over-collateralisation in secured transactions[4].

Diaspora Bonds: A Coin with Two Sides

Where DPR issues seek to make use of existing remittance flows, the second financial instrument examined in this chapter, the diaspora bond, sets out to seek new money from the community of nationals resident abroad. These are securities issued by governments specifically structured and targeted for this group. Through them members of the diaspora can help home-country governments to raise capital in order to finance projects that may improve economic and social development. From the issuer's point of view the attractions are a potential reduction in external financing costs through a "patriotic discount," reductions in foreign-exchange risk premiums and, sometimes, lower regulatory and legal costs[5]. This kind of bond might be particularly attractive when access to traditional international markets is difficult – something that may be important in the context of the current economic crisis, which has severely restricted liquidity in international capital markets.

Governments may issue bonds specifically targeted at their own emigrant communities round the world, seeking to tap their connection with the home country

International experiments with diaspora bonds nonetheless remain few and far between. Israel (through the Development Corporation of Israel) and India (through the government-owned State Bank of India) are the most well-known[6]. Other examples include issues by Sri Lanka and South Africa. The Lebanese diaspora has also been active in investing in government bonds. (For all these see Ketkar and Ratha, 2009b.) No Latin American or Caribbean country figures on this short list. Is there potential for governments in the region to issue such bonds?

Several factors contribute to the potential demand for diaspora bonds. First, there is the financial capacity of the relevant diaspora to invest in capital markets. While data regarding incomes of specific Latin American diasporas in developed countries are limited or even non-existent, a proxy is provided by the occupations of migrants in OECD countries. Figure 5.2 compares the number as well as the percentage of managers and professionals – the potential purchasers of diaspora bonds – born in Latin American and Caribbean countries with the corresponding figures for other countries with significant emigration to OECD countries.

As Figure 5.2 demonstrates countries that have issued diaspora bonds tend to have migrant communities in OECD countries in which managers and professionals are especially well represented (Sri Lanka being the exception). Latin American and Caribbean diaspora, in contrast, have lower levels of managerial/professional employment. Only (in descending order) Aruba, Bermuda, Argentina, Venezuela and Panama have proportions similar to India, Israel, Lebanon and South Africa. However, looking at absolute numbers gives more hope. Many Latin American and Caribbean countries have absolute numbers of managers and professionals abroad similar to those observed among diaspora-bond issuers (with the notable exception, of course, of India which has more than 500 000 people working as managers and professionals in OECD countries). Specifically each of Mexico, Puerto Rico, Cuba, Jamaica, Colombia, Argentina, Brazil, Peru, the Dominican Republic, El Salvador and Venezuela enjoy a potential market for diaspora bonds in excess of 40 000 people[7].

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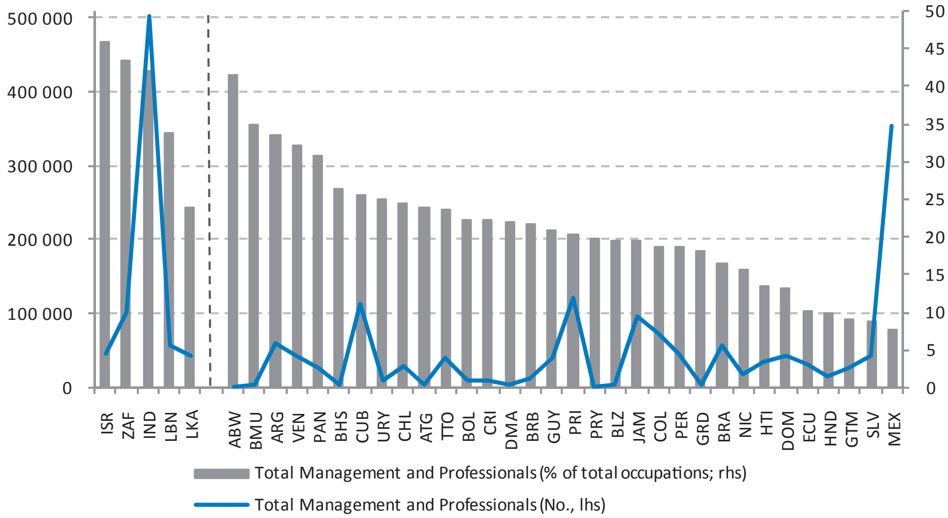
Obviously, the number of potential investors in diaspora bonds is not the sole criterion for the development of this market. Households' incomes clearly matter too but other factors are crucial. One is the potential propensity of diaspora members to invest in bonds issued by the home government. This is conditioned by feelings of patriotism and the level of support among diaspora members for the economic and social policies back home. These concepts are difficult to measure. For instance, it is difficult to track information on how popular policies established by home governments are with diasporas and an assumption that local polls can be a measure for diasporas' beliefs is often invalid.

Diaspora bonds are most likely to succeed where the overseas community is large, has savings to invest and is well-disposed to the home country...

Figure 5.2. Migrants in Managerial/Professional Roles, Latin America and Caribbean against Issuers of Diaspora Bonds
(circa 2000)



Notes: Universe is migrants resident in OECD countries.
Total management and professionals refers to "legislators, senior officials, managers and professionals" for OECD countries excluding Japan and United States. For Japan it refers to "Managers and officials" and "Professional and technical workers". For the United States it refers to items 001 to 395 of the Census Occupation Code (COC).

Source: OECD Development Centre calculations based on OECD (2008)

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Figure 5.3 examines two proxy variables that may influence the propensity of diasporas to invest in their home country: economic stability and control of corruption. Economic stability, particularly currency and price stability, is an important indicator for Latin Americans of economic policies given past periods of hyper-inflation and currency depreciation among countries in the region. Corruption is also likely to be a relevant fact for potential investors[8]. Good scores on these two measures are likely to encourage potential investors to believe that their money will be well used and for the purposes they anticipate (factors central to achieving a "patriotic discount" on a diaspora bond).

...economic stability and control of corruption are good proxies for this

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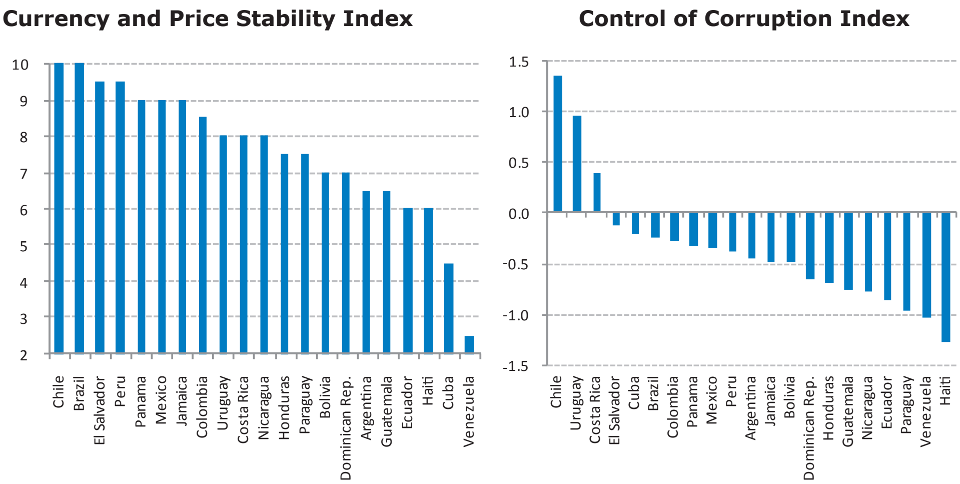
Figure 5.3. Economic Stability and Corruption



Notes:

a) The Currency and Price Stabilty Index is a subcomponent of the Bertelsmann Transformation Index (BTI). Its value ranges from 0 (low stability) to 10 (high stability).

b) Control of Corruption is measured on a scale from -2.5 (poor governance) to +2.5 (good governance).

Sources: OECD Development Centre calculations based on Bertelsmann Transformation Index (BTI, 2008) for the Currency and Price Stability Index and on Kaufmann *et al.* (2008) for the Control of Corruption Index.

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Combining a consideration of the potential market (from Figure 5.2) with the relative attractiveness of investment back home (from Figure 5.3), suggests that Brazil, Colombia, El Salvador, Mexico, Panama and Peru appear best positioned to place diaspora bonds.

HOW DO REMITTANCES AFFECT SENTIMENT IN THE CAPITAL MARKETS?

In addition to their microeconomic impact at the household level, remittances have grown into an important source of macro-finance and a pillar of macroeconomic stability. Such macroeconomic effects are clearly evident in Latin American economies, either where remittances are high in absolute terms (as is the case in Brazil, Colombia, Ecuador, the Dominican Republic, Guatemala and Mexico) or large relative to the size of the economy (as in El Salvador, Guyana, Haiti, Honduras and Jamaica). Chapter 2 shows how this latter factor is particularly important for Central American and Caribbean economies, but also the significant variations at the country level throughout the region.

Remittances are positive for the economies that receive them, both by virtue of their size and their stabilising nature

Material remittance flows appear directly in balance of payments data and through this they go on to affect exchange rates and so indirectly other macroeconomic variables including interest rates and inflation. In emerging and developing countries balance of payments data are a relatively high-profile indicator of government financial strength through the foreign exchange channel. Remittances then have many channels though which they can affect market perceptions of the macroeconomy[9].

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This is to look just at the scale of remittances. Their qualitative nature – which is quite different from flows from foreign investment or exports – is just as important. Remittance flows can be shock absorbers for the economy and so play a role in reducing the country's macroeconomic vulnerability. By reducing the probability of default in country-risk models they can mitigate perceived sovereign credit risk, and reduce the probability of current account reversals (Bugamelli and Paterno, 2005).

As with everything of course, strong remittance flows are not the proverbial free lunch. An increase in remittances will have a positive effect on the current account and can cause the real exchange rate to rise. Policy makers should be alert to this risk. This relative strength of the local currency may increase the incentive to issue – and so be dependent on – foreign-currency denominated debt. Remittance-induced exchange-rate appreciation can also threaten the so-called Dutch disease, reducing the export competitiveness of the economy and sucking in imports[10].

Many a Little Makes A Mickle: Mechanisms to Value Remittance Flows

A common way to pick up the effect of remittances on sovereign risk is to include them in the traditional solvency ratio (that is the ratio of debt to exports of goods and services) (Ratha, 2005; World Bank, 2006). Including remittances in the ratio's denominator captures the whole of current account income. Conversely, failing to account for remittance inflows (so measuring only other current-account flows such as earnings from exports) could provide a distorted picture of an economy's macroeconomic stability. Is such an inclusion justified?

Remittances are as much part of the assessment of a country's solvency as are its exports of good and services

Certainly both exports and remittances serve as a cushion against external shocks and reduce the risk of default on external debt. Since the solvency ratio measures the country's capacity to pay the entire total external debt (both private and public), it further seems qualitatively reasonable to include remittances in this ratio: thus capturing total debt on the one hand and total potential servicing flows on the other.

Figure 5.4 exhibits the evolution of the solvency ratio for selected Latin American and Caribbean countries over the period 1993-2006. In general, remittances have a higher impact on solvency in Central American and Caribbean countries (for example, the Dominican Republic and El Salvador) than in other countries of the region.

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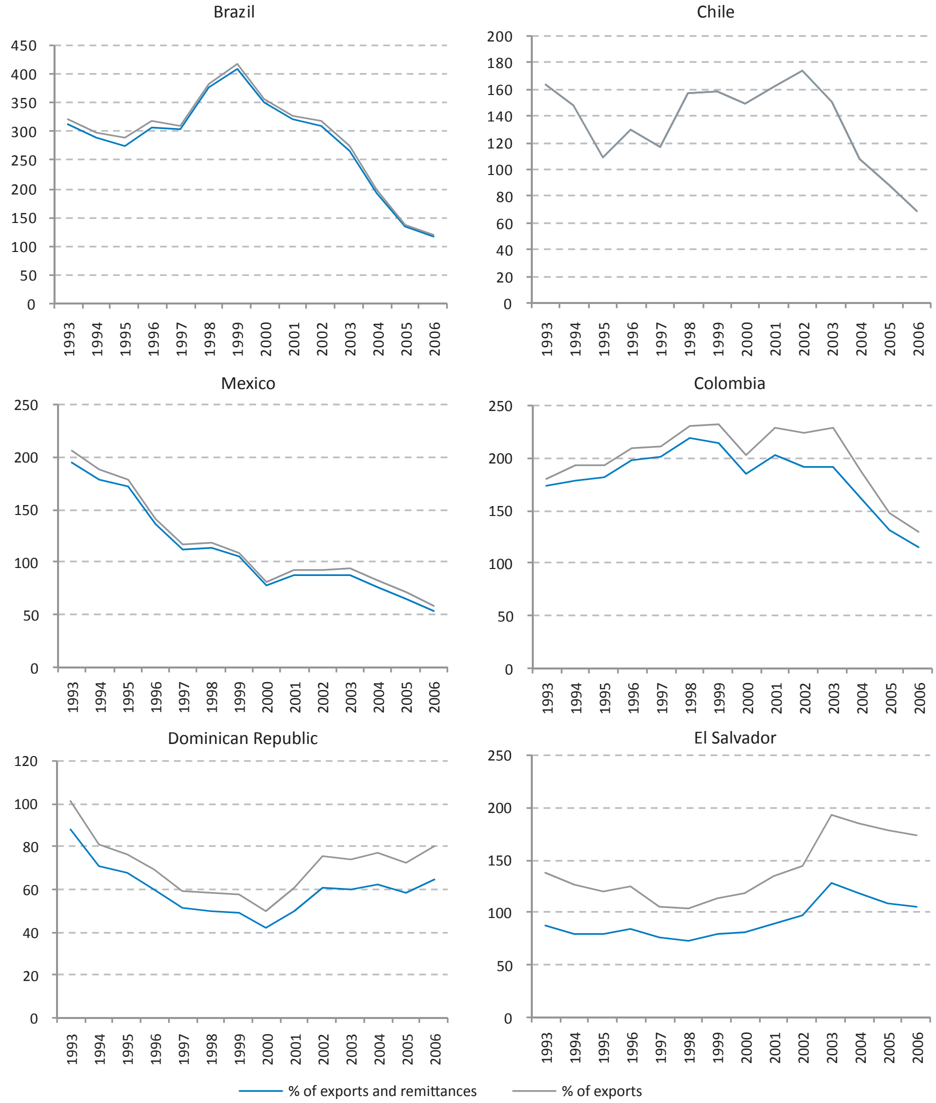
Figure 5.4. Solvency Ratios With and Without Remittances
(Selected Latin American and Caribbean countries)



Note: The Solvency Ratio With Remittances is defined as the percentage of external debt over exports and remittances

Source: Avendaño *et al.* (2009).

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Remittances act to reduce the overall volatility of external flows

Remittances have a counter-cyclical effect in most countries in Latin America, thus significantly reducing the volatility of growth (Fajnzylber and López 2007)[11]. Additionally, they can reduce the volatility of overall external flows (FDI flows, portfolio flows, ODA, bank loans, exports and remittances). Empirical studies show that they do so because of both their relative stability compared with other flows and their low correlation with those flows (Avendaño *et al.*, 2009). This characteristic may be particularly important for Latin America, where saving rates are low and dependence on external financing high[12].

This is at once apparent from Figure 5.5, which summarises the volatility of the major capital flows to Latin American and Caribbean countries over 1993-2007. The result is straightforward: the volatility of remittances has been much smaller than that of other external flows (portfolio flows, FDI, exports and ODA) indicating that it is a source of financial stability.

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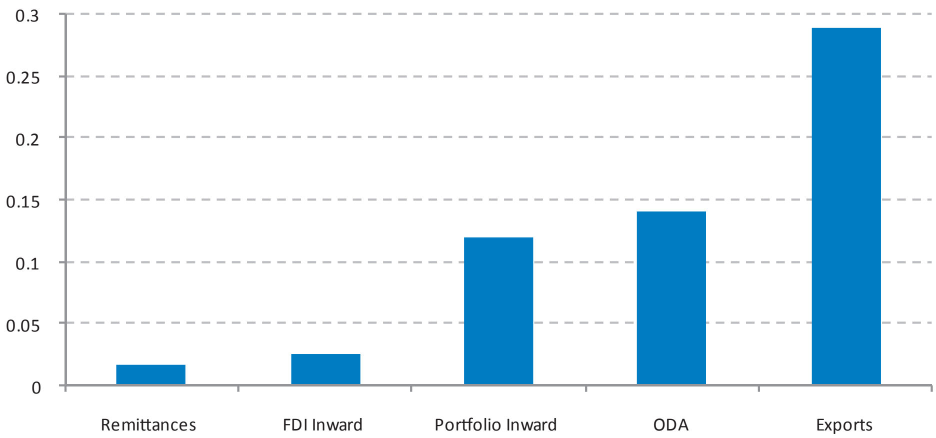
Figure 5.5. Volatility of External Flows

Latin American and Caribbean countries, Percentage of GDP (1993-2007)



Notes:

a) Volatility is calculated as the average of the variance of each flow as a proportion of GDP. Similar results are obtained for the volatility of Hodrick-Prescott filtered flows thus eliminating the effect of trends.

b) The countries included are: Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Dominican Republic, Ecuador, El Salvador, Guatemala, Haiti, Honduras, Jamaica, Mexico, Nicaragua, Panama, Paraguay, Peru, Uruguay and Venezuela.

Source: Avendaño *et al.* (2009).

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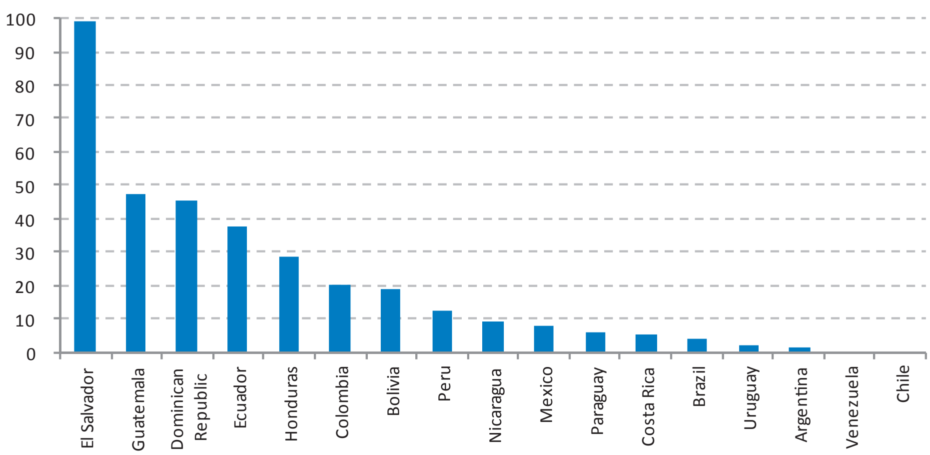
The effect of this lower volatility, and the counter-cyclicality noted above, is shown in Figure 5.6. The height of the bar for a given country represents the percentage change in volatility (defined as for Figure 5.5) calculated with and without workers' remittances over 1993-2007[13]. The higher the change the greater the implied role played by remittances in reducing the volatility of external flows (whether through their own low volatility or their low or negative correlation with the sum of other external flows).

Figure 5.6. Volatility of Inward External Flows With and Without Workers' Remittances

Percentage change on volatility excluding remittances (Average 1993-2007)



Note: The height of each bar represents the percentage change in annual variation of external resource inflows over the period 1993-2007 if workers' remittances are eliminated; a higher bar means that remittances reduce volatility of external flows to a greater extent.

Source: Avendaño *et al.* (2009).

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The variation between countries is considerable. In general the effect is most marked (among South and Central American countries at least) for those countries with high levels of remittances as a proportion of GDP. Remittances do have a material effect on the volatility of external flows for these countries. The next section examines if and how this influences market sentiment by looking at a key set of players in the arena of emerging markets: the rating agencies.

The View from the Credit Rating Agencies

For the credit rating agencies (CRAs) it has not been a good crisis. Academia as well as policy makers note that "the recent financial market turbulence has brought credit rating agencies under fire" and they are arguing for fundamental reform of their business model (Portes, 2008). Rating agencies are seen as faced with serious conflicts of interest given that their remuneration is drawn from rated issuers (see Mathis *et al.*, 2008, for a theoretical analysis). They are also in the hot seat because of their key role in the very international financial regulatory frameworks that are seen as having been found wanting[14]. Nevertheless CRAs continue to have a considerable and increasingly prominent role on international capital markets and understanding the way they assess country risk and exploring whether they take remittances into account is crucial to a full understanding of their impact on emerging-market issuers[15].

Despite criticism, the views of the rating agencies remain central to the availability and pricing of external sovereign debt

Indicators such as debt-to-export and debt-service-to-current-account ratios are routinely used by credit rating agencies (CRAs) in their assessments of creditworthiness. Research on the access of sovereign borrowers to international capital markets (see Ratha, 2005; and World Bank, 2006) suggests that perceptions of sovereign creditworthiness could be improved were remittance flows – quite properly – included in the calculation of these indicators. Is this done in practice?

Ratha *et al.* (2007) defined a standard ratings model and found that a number of unrated countries would be likely to have higher ratings than expected, notably on account of foreign currency inflows such as remittances. According to Ratha (2005), "country credit ratings by major international rating agencies often fail to account for remittances". This is at odds with what the major CRAs themselves say, at least when looking at countries where flows are material:

- Prior to the crisis, Fitch Ratings (2008) noted that remittance flows could positively impact ratings, for example in the case of El Salvador. These comments are consistent with Fitch's stated sovereign methodology which "takes into account the volatility and potential vulnerability of receipts, such as remittances, to domestic and external shocks" (Fitch Ratings, 2007).
- In its outlook for Mexico, Standard & Poor's (2005) stressed the importance of remittances in the balance of payments, and their indirect impact on other determinants of sovereign ratings, such as the public finances. More recently, in May 2009, when reducing El Salvador's credit rating to "BB" from "BB+", S&P stated that "the weak performance in 2009 is due to falling consumption, investments, and exports as a result of a significant pass-through from the global recession" and that "remittances from the United States fell by 8% in the first two months of the year"[16].
- Moody's, in February 2009 using the Philippines as an example, said that lower economic growth in 2009 could in part be attributable to a decline in remittances, which in that case account for more than 10% of domestic output and are a major driver of consumption[17].

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Despite these accumulating instances and the importance of understanding why and how ratings are arrived at, little research has systematically analysed the impact that remittances have on sovereign ratings assigned by CRAs[18]. Recall that exposure to remittances may be seen as a benefit (access to a relative stable external flow) or a risk (dependence on these flows which are largely outside the recipient country's control).

The models that CRAs use to assign ratings to countries are a trade secret and not publicly available. As such, external researchers cannot know with certainty what goes into the ratings they issue – and what does not. Consequently they have developed econometric models to simulate those used by CRAs. By building a rating model covering a long time span (1993-2006), and estimating ratings for a sample of 83 emerging countries, Avendaño *et al.* (2009) assessed the impact of remittances on the conclusions of the three main CRAs (Standard & Poor's, Moody's and Fitch). Their analysis covered the effect of the solvency ratio (external debt over exports and remittances) and the volatility of external flows on rating decisions. They asked: Do rating agencies really take remittances fully into account in their analyses? What is the potential effect of remittances when included in market variable estimations?

Results show that both the solvency ratio and the volatility of external flows are consistently negative and significant variables, whether remittances are included or not.

How and How Much? Assessing the Role of Remittances

CRAs certainly consider the effect of remittances in their assessments. The model tests the extent to which this is followed up in a quantitative analysis

To start to explore the central question of the extent to which remittances affect CRA analysis, Figure 5.7 compares three types of ratings: the observed rating, a predicted rating (estimated from a model which excludes remittances from the solvency ratio and the volatility of external flows) and a counterfactual rating (calculated from the estimators of the predicted model but including remittances in the two core explanatory variables)[19].

For countries with material levels of remittances relative to GDP (such as Ecuador, El Salvador, the Dominican Republic and Guatemala), there is a relative high difference between the predicted rating and the counterfactual rating, indicating that the inclusion of remittances would be beneficial for these countries – by close to one notch for El Salvador.

The remaining question of whether CRAs already include remittances in their own models is addressed by comparing the counterfactual rating and the observed rating. Here the major variances are not concentrated among those countries with high levels of remittances over GDP. Indeed, the greatest variations are found for countries, like Uruguay or Venezuela, which are outside this group. Moreover, for the set of countries with high levels of remittances, it is not clear that the observed rating is less favourable than the counterfactual rating (indicated by a positive sign in the figure). For El Salvador and Guatemala, observed ratings are more favourable than the counterfactual rating, meaning that S&P's actual rating is more favourable than that given by the statistical model including remittances. The reverse is true for Ecuador and the Dominican Republic.

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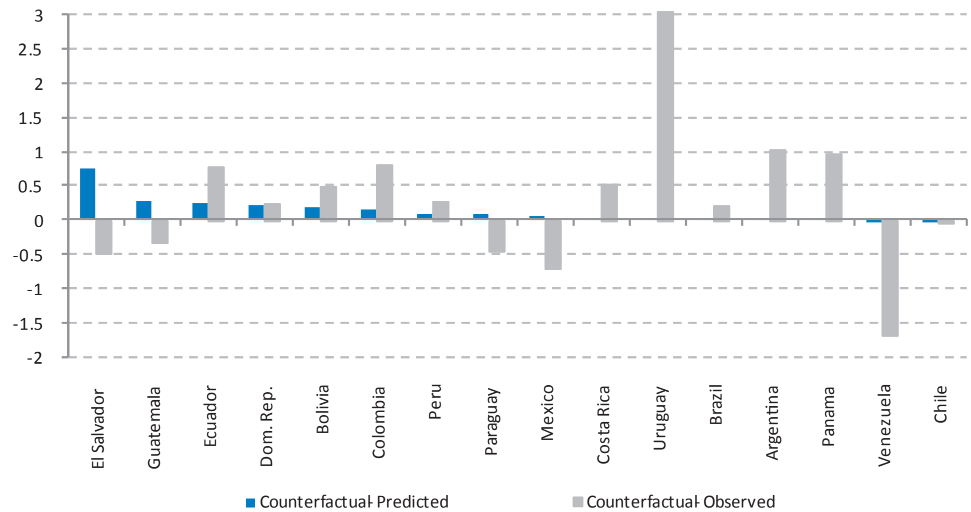
Figure 5.7. Difference between Observed, Predicted and Counterfactual Ratings in 2006



Notes:

a) A difference of one notch on the ratings scale (from BB to BB+ say) is scored as one and so on. A negative number represents a downgrade.

b) The data here are for Standard & Poor's . The Statistical Annex to this chapter presents the results for Fitch and Moody's.

Source: Avendaño *et al.* (2009).

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Modelling is a proxy for the more complex qualitative and quantitative analysis carried out by the CRAs

Now, CRAs do not use a single model to estimate ratings. Ratings are the result of a qualitative and quantitative analysis of credit risk and consequently a general econometric model to estimate ratings is only a second best. Furthermore ratings are given case by case. This is in line with previous research (including Roubini and Manasse, 2005) showing that there is no single model to rate countries nor do variables always have the same impact on sovereign ratings. In that context, the Avendaño study estimated a specific model for countries with relative high levels of remittances. This is presented in Table 5.1.

By using a set of control variables, the importance of a ratio of remittances over GDP higher than 5% is not significantly different from 0 for CRAs. High dependence on remittances does not necessarily mean an improvement in market perception.

However, the solvency ratio and the volatility of external flows (including remittances) are significant for most of the CRAs. Moreover, the interaction term between the remittances-to-GDP ratio and the volatility-of-flows variable is significant in explaining ratings, in the sense that the negative impact of the volatility of external flows is reduced. When estimating a second model for highly remittance-dependent economies, Avendaño *et al.* (2009) find that remittances have above all an indirect and positive impact on ratings through a premium (captured with the interactive dummy variables remittances over GDP and the volatility of external flows), with the impact being more pronounced in the case of volatility of external flows than solvency ratio.

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Table 5.1. Impact of Remittances Variables on Ratings Given by CRAs 1993-2006

	S&P	Moody's	Fitch
Threshold variable Remittances over GDP > 5%	+	-	+
Solvency ratio Debt over exports and remittances	-	-	-
Volatility of external flows Variance of external flows over GDP	-	-	-
Interactive of Solvency ratio Threshold x Solvency ratio	-	+	-
Interactive of Volatility of external flows Threshold x Volatility of external flows	+	+	+

Notes:
a) The threshold defines countries with high levels of remittances as those whose flows were above 5% of GDP.
b) Each box indicates the coefficient sign of the variable: + indicates that the variable has a positive impact on sovereign ratings; - a negative impact.
c) Shaded boxes identify variables that are statistically significant at 1%.

Source: OECD Development Centre calculations based on Avendaño *et al.* (2009).

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These results support the view that CRAs *do* take remittance flows into account in rating sovereign debt. However, this variable is significant for a limited set of countries: highly dependent on remittances, typically small in size and generally classified as low or middle income. An upward trend in remittances can improve ratings but the converse also applies. This may explain why in the current economic crisis six out of the seven rated countries with the highest remittance-to-GDP ratios in the region have been downgraded or seen a worsening of their rating outlook (from positive to stable, or from stable to negative)[20].

Finally it must be noted that the impact of including remittances on ratings remains weak when compared to variables such as debt service, the level of foreign-currency debt or the depth of local-currency financial markets.

CRA analysis does appear to reflect remittances. Their effect is significant for highly-dependent low- or middle-income countries. The effect remains weak however compared with other relevant variables

SHADOW RATINGS: RATING THE UNRATED

A rating issued by one of the major CRAs is a key influence on a sovereign borrower's access to capital markets. It is common practice to rate publicly traded bonds as a reassurance to investors and to open the market to those investors (such as pension funds) who for their own regulatory reasons require a rating on their investments[21]. Current controversy over the role of the CRAs aside, a rating may be more important today than in the past because other capital-market signals about credit risk may no longer hold (Flandreau *et al.*, 2009*a*).

Moreover, sovereign ratings generate externalities. Their issue of itself generates publicity about the borrower and may attract investor attention and therefore potentially capital. Sovereign ratings provide an anchor point – indeed a ceiling

– for investment decisions in a country's private bond and equity markets as well as in decisions about foreign direct investment. It would not be going too far to say that they influence – albeit sometimes indirectly – nearly all investment decisions by foreign investors in a given country, and are a tool familiar to those investors.

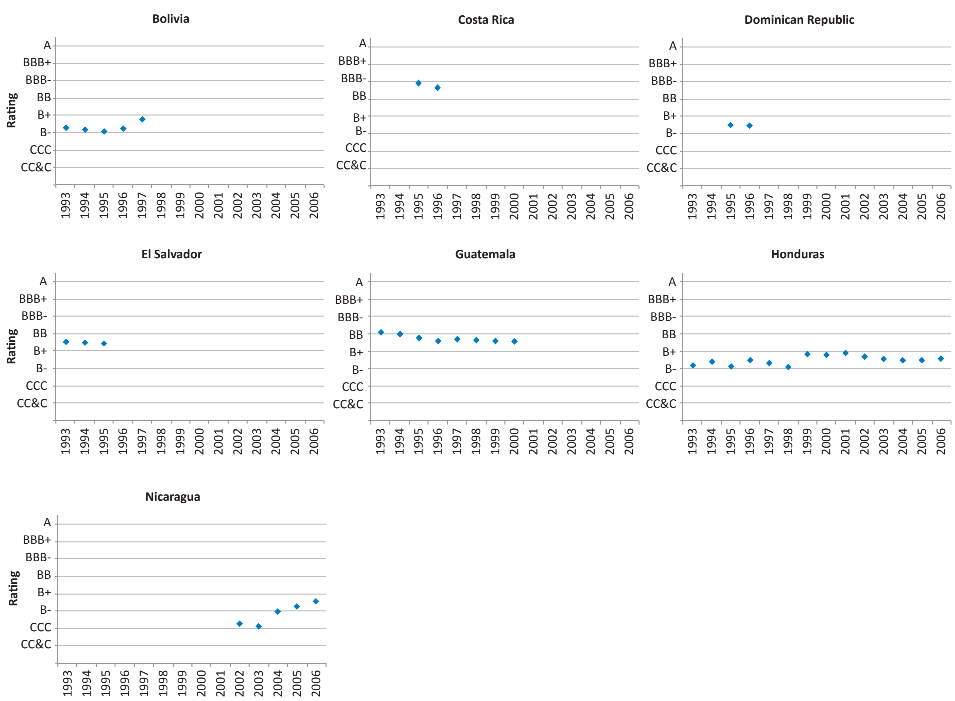
Despite the importance of ratings in conditioning access to all forms of credit, many developing countries remain unrated

Somewhat surprisingly then given these informational benefits many developing countries remain unrated. High fixed costs, lack of information and poor understanding of the incentives may be responsible for this. According to Ratha *et al.* (2007) "70 developing countries – mostly poor – and 12 high-income countries do not have a rating from a major rating agency. Of the 86 developing countries that have been rated, the rating was established in 2004 or earlier for 15 countries." Similar results are found for the coverage given by investment banks in their reports to developing and emerging countries (Nieto-Parra and Santiso, 2007)[22].

In the absence of a CRA rating it is natural to wonder what it would be. Avendaño *et al.* (2009) predict ratings for selected remittance-dependent Central American and Caribbean countries, some of which are not rated by any of the three main CRAs, using the models described earlier. Figure 5.8 exhibits these shadow ratings for selected Latin American countries. Historic shadow ratings are also provided since trends are almost as important as absolute values in their impact on portfolio allocation and investors' behaviour.

Figure 5.8. Shadow Ratings for Latin America and Caribbean
(unrated periods)

Panel A: Standard & Poor's



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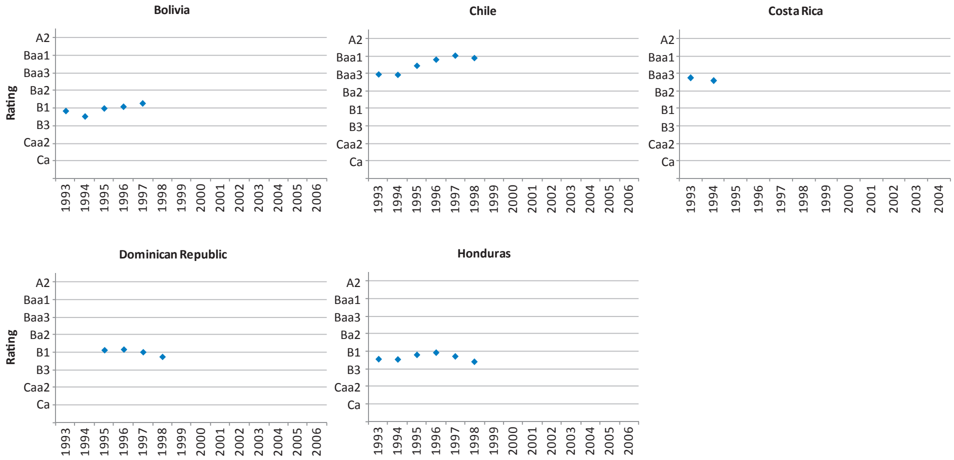
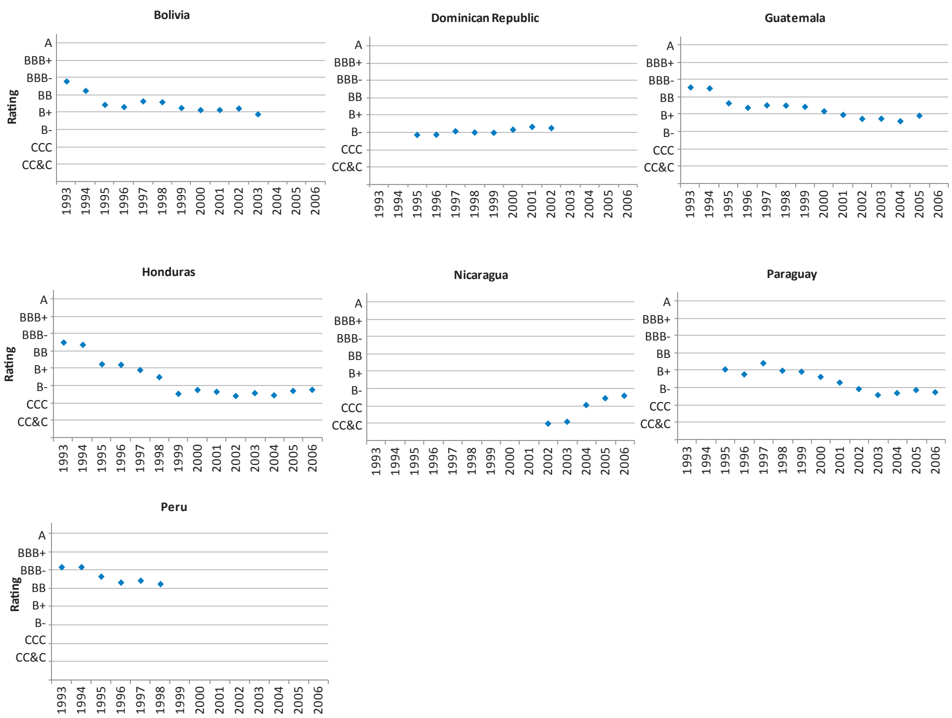
Panel B: Moodys



Panel C: Fitch



Source: Avendaño *et al.* (2009).

StatLink http://dx.doi.org/10.1787/716467340567

Shadow ratings for countries highly dependent on remittances (the Dominican Republic, Ecuador, El Salvador, Guatemala, Honduras and Nicaragua) were estimated using a specific model for this kind of country. As illustrations the Fitch shadow ratings for Honduras and Nicaragua are respectively B- and CCC+ while the Standard & Poor's shadow rating for both countries is B. An extensive comparison between shadow and observed ratings is provided in Avendaño *et al.* (2009).

These models enable the calculation of shadow ratings for otherwise unrated countries

Nieto-Parra and Santiso (2007) floated the idea of creating a partnership between a leading international organisation with expertise in development finance,

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A suitable PPP could promote the extension of coverage to otherwise unrated countries, thus increasing their market profile

donor agencies and a market maker in emerging markets as a way of boosting country coverage. Such public-private partnerships are not without precedent: for some years Standard & Poor's has provided rating coverage of some African sovereigns with support from the International Finance Corporation and United Nations Development Programme. In 2006 this led to ratings for 14 sovereigns. The *African Economic Outlook* produced by the OECD Development Centre and the African Development Bank with the support of the European Union also seeks to boost the economic and rating coverage of countries lacking attention from the capital markets. An extension of these efforts in the way suggested would be an important step towards reducing the market informational gap for some developing countries.

LESSONS AND IDEAS

Capital markets and remittances have multiple links, from the securities in which remittances play a crucial role to the ways in which remittances can affect sentiment in the international capital markets. The lessons for policy makers are many.

Diaspora bonds are worthy of consideration. This chapter has provided a toolkit to assess the chances of success for a given issuer. Chief amongst there are the financial capacity of the relevant diaspora(s) as well as their incentive to invest in government bonds from their country of origin.

Remittance flows are important to perceptions of sovereign borrowers in the capital markets. They directly improve key indicators like the solvency ratio and reduce the volatility of external flows. Consequently, market participants and in particular rating agencies now take remittance flows into account in assessing country risk.

The influence of remittances on ratings is particularly crucial for small, low and middle income Central American and Caribbean countries. It is also a double-edged sword. Over dependence (however defined) can be seen as a negative factor. Market education and careful presentation will be important in capturing the benefits, particularly in a global crisis when remittance flows come under pressure.

Finally, this chapter has provided shadow ratings for countries where relative remittances flows are high but commercial ratings not available. Shadow ratings themselves may prompt useful discussion with capital markets investors or international agencies. The information flows that result could be leveraged by means of a public-private partnership to promote formal ratings from the CRAs.

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NOTES

1. Consequently default remains rare and more importantly in terms of investor sentiment defaults and crises in emerging countries such as Argentina in 2001 and Brazil in 2002 did not lead to renegotiation or dispute with DPR investors.
2. Given that these securities are traded infrequently and have different characteristics from sovereign bonds it is more meaningful to compare them on the primary than on the secondary market.
3. In 2008, Fitch upgraded 17 different structured-financing programmes driven by sovereign upgrades. In Brazil bank-related future-flow programmes from Itaú, Unibanco, Santander and Visa Net all benefited from an improved sovereign environment (Fitch Ratings, 2009).
4. For investment grade DPR transactions, Standard & Poor's ranges DSCRs between 8 times and 14 times. This is the case in most DPR issues, particularly those of Latin American countries, considered to have high DSCRs (Standard & Poor's, 2008). As an example, in July 2001 Standard & Poor's assigned a rating of BBB- to Nikkei Remittance Trust's USD 250 million fixed-rate certificates, series 2001-1, due August 2006. This deal involved Banco do Brasil selling its future remittance receivables from Brazilian workers in Japan. The volatility and uncertainty of future flows of remittances were mitigated with a DSCR of 7.6 times.
5. Any "patriotic discount" secured represents the margin of economic returns that diaspora individuals are willing to forgo (perhaps through desire to contribute to the development of their home country). Specifically, its discount is measured as the difference between the rate of interest a country would pay to issue the bond on the international market and the rate of interest paid to sell the bond to the member of the diaspora (Johnson and Sedaca, 2004).
6. According to Ketkar and Ratha (2009*b*), Israel was the first country to issue this kind of bond, in 1951, followed by India in 1991. A major difference between these two bonds is the regulation to which they were subject. While the Israeli bonds are registered with the US Securities and Exchange Commission, the Indian bonds are subject to local laws (see Chander, 2001, for a discussion of regulation of the Indian diaspora bonds).
7. Needless to say, these numbers are a crude approximation of the size of the market for diaspora bonds. First, members of the diaspora who do not work as managers or professionals might nevertheless buy such bonds. Second, any diaspora includes not only migrants, but also all of their descendants who retain cultural and other ties to the country and this is without a doubt an important feature of the diasporas targeted by the Israeli and Indian governments. For both of these reasons the numbers reported here probably tend to under-estimate the number of potential buyers of diaspora bonds.
8. Latinobarómetro (2008) found that 69% of Latin Americans think that public employees are corrupt. A similar proportion has been reported in surveys since 2000. Moreover 54% of Latin Americans think there is more corruption in politics than in the rest of the society.
9. See Moody's (2008) for the importance of balance-of-payment considerations in determining ratings.
10. Amuedo-Dorantes and Pozo (2004) found that a doubling of workers' remittances resulted in real exchange rate appreciation of about 22% in Latin American and Caribbean countries and consequently they relate remittance flows to a reduction in the receiving country's competitiveness. However, Rajan and Subramanian (2005) did not find any empirical evidence for such a reduction. According to IMF (2005), the "Dutch disease" effects of remittances are less marked than for exchange rate appreciations linked to natural resource booms.

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11. However, migrant-derived income can become costly to emerging countries when resources are mismanaged. Remittances may reduce the government's incentive to maintain fiscal policy discipline (Chami *et al.*, 2008). They may create a moral hazard problem by reducing the political will to implement reforms allowing real exchange rate appreciation.

12. Migrants' remittances constitute a large source of foreign capital in many Latin American countries and are considered a stable source of financing compared with other financial flows (Ratha, 2004). Similar effects are seen over long periods of time: see Esteves and Khoudour-Casteras (2010) regarding the late 19th century.

13. Specifically, the variance of inward external flows is defined as follows:

$$Var\ external\_flows)_{\alpha,t} = \sum_{i=1}^{N} w_{i,t}^2 \cdot Var(X_{i,t}) + 2\sum_{i \neq j}^{N} w_{i,t} w_{j,t} Cov(X_{i,t}, X_{j,t})$$

where $Var(external\_flows)_{\alpha,t}$ corresponds to the variance of inward external flows of country α at time *t*, $w_{i,t}$ is the weight of the external flow *i* with respect to the total external flows in country α, $Var(X_{i,t})$ is the variance of the external flow *i* as a share of GDP between *t-5* and *t*, $Cov(X_{i,t}, X_{j,t})$ is the covariance between the external flows over GDP *i* and *j* and from *t-5* to *t*.

14. See Flandreau *et al. (*2009*b*) for a discussion of how the emergence of rating agencies as a pillar of financial regulation in the 1930s was due to the then absence of conflict of interest.

15. In this context, there is a large and useful literature studying the impact of ratings on market prices (Kaminsky and Schmukler, 2001) and bond spreads (Reisen and Von Maltzan, 1999; Sy, 2001; Ratha *et al*., 2007; Cavallo *et al*., 2008; Gaillard, 2009).

16. "S&P" lowers El Salvador rating to 'BB' from 'BB+'", Reuters, 12 May 2009 (online article).

17. "Moody's: Slowing remittances hurt RP", Manila Bulletin, 14 February 2009 (online article).

18. This is in sharp contrast to the extensive study of the effects of workers' remittances at the macro and the micro level (for a review of the literature see World Bank, 2006).

19. In particular they estimated ratings by using the solvency ratio, the volatility of external flows and a set of control variables, using the following model:

$$Rating_{i,t} = \beta_0 + \beta_1 control\_\mathrm{var}iables_{i,t} + \beta_2 TDX\_wr_{i,t} + \beta_3 Volat\_indicator\_wr_{i,t} + \tau_t + \nu_i + \varepsilon_{i,t}$$

where *TDX_wr* is the solvency ratio excluding remittance flows, *volat_indicator_wr* is the volatility indicator excluding remittance flows, τ_t is a year fixed effect and ν_i is the country-individual effect. They obtain the vector β as the fixed-effect estimator. Then, they use the observed solvency ratio (remittances included) as well as the volatility of external flows (remittances included) and calculate the counterfactual rating using these two variables and the β coefficients estimated above.

20. Since September 2008 the Dominican Republic, Ecuador, El Salvador, Guatemala, Honduras and Jamaica have been downgraded and/or seen their outlook lowered. The only country with stable ratings is Nicaragua.

21. Moreover, the Basel II regulatory framework could penalise unrated securities (BIS, 2005).

22. Country coverage by leading investment banks, emerging-market benchmarks including the EMBI (produced by JPMorgan for the bond markets) or global banks such as Citigroup, Deutsche, HSBC, JPMorgan or Morgan Stanley rarely covered more than 35 economies. The other 120 developing countries simply did not exist for global financial-market investors. Only ten countries enjoyed systematic coverage from the major financial institutions.

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STATISTICAL ANNEX

Table 5A.1. Observed, predicted and counterfactual ratings in 2006

Fitch			Moody's			Standard and Poor's		
		Counterfactual-			Counterfactual-			Counterfactual-
	Predicted	Observed		Predicted	Observed		Predicted	Observed
El Salvador	0.36002	-0.46191	El Salvador	0.49599	-0.75814	El Salvador	0.75845	-0.47801
Guatemala	0.15211	-3.63764	Nicaragua	0.28704	1.15952	Guatemala	0.28846	-0.32169
Ecuador	0.12520	-0.24559	Honduras	0.28190	-0.39468	Ecuador	0.24507	0.77884
Dom. Rep	0.11397	-0.19136	Guatemala	0.16645	-0.97724	Dom. Rep.	0.21119	0.24258
Bolivia	0.09989	-1.03815	Ecuador	0.14730	0.01511	Bolivia	0.18792	0.49443
Colombia	0.08054	1.28596	Dom. Rep.	0.11804	1.58312	Colombia	0.16740	0.80879
Peru	0.04802	-0.58759	Colombia	0.10788	-0.04414	Peru	0.08798	0.25887
Mexico	0.02654	-0.54456	Bolivia	0.10726	-0.28165	Paraguay	0.08274	-0.44526
Costa Rica	0.01711	0.48053	Peru	0.04837	0.31399	Mexico	0.05425	-0.70479
Uruguay	0.01645	2.46372	Mexico	0.03433	-1.58148	Costa Rica	0.03166	0.53555
Brazil	0.01450	-0.68554	Paraguay	0.02661	0.18622	Uruguay	0.03088	3.03986
Argentina	0.01249	5.23028	Brazil	0.01775	-0.34089	Brazil	0.02891	0.18954
Panama	0.00774	0.65071	Costa Rica	0.01766	0.37066	Argentina	0.02213	1.01766
Venezuela	0.00148	-0.09606	Uruguay	0.01756	3.80778	Panama	0.01271	0.94879
Chile	0.00001	-0.72834	Argentina	0.01358	1.28194	Venezuela	0.00227	-1.68417
			Panama	0.00582	0.19339	Chile	0.00003	-0.01361
			Venezuela	0.0009	0.39559			
			Chile	0.00001	-0.47072			

Note: Unity is equivalent to one notch.

Source: OECD Development Centre based on Avendaño *et al.* (2009)

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CHAPTER SIX

Managing Latin American Migration: A Case for Public Action?

This *Outlook* appears at a time of change for international migration, and migration from Latin America and the Caribbean in particular. The European Union has in recent years been taking its first steps toward a European immigration policy; the 2008 Return Directive for irregular migrants discussed in Chapter 1 is one facet of this emerging policy structure[1]. At the same time, individual EU member states have pursued aggressive, and sometimes controversial reforms, including the Spanish assisted-return programme for legal migrants assessed in Chapter 3. France has established quantitative targets for the share of economic immigrants among all immigrants, and for expulsions of irregular migrants (some 30 000 a year). The Obama administration in the United States announced in April 2009 that immigration reform, stalled since 2007, would be a policy priority for the new president's first year in office – despite competition from health care and energy reform and the need for measures to combat the economic crisis. As part of this, the administration signalled a commitment to make legal status possible for the unauthorised population (about which statistics were provided in Chapter 2)[2].

This flurry of political activity in the principal destination countries for Latin American and Caribbean migrants and the reaction to it within the region demonstrate at least two things. First, there is a widespread conviction that migration can be better managed. Second, political actors of all stripes and at all levels of political action are convinced that now is the time to act. There is unfortunately a third element: the absence, or apparent absence, of a consensus on what must be done. Not only do the interests of countries of destination and countries of origin sometimes differ, but different parties within each of those groups have different objectives and interests. Nonetheless some kind of reform is needed, and quickly, to ensure international people flows deliver better outcomes for people in countries of destination and countries of origin, and indeed for migrants themselves.

The crisis has raised the political profile of migration in both countries of origin and destination. This may offer an opportunity for co-ordinated reform

Part of the problem is that "global migration regime" – with which the potential migrant must contend – is in fact a patchwork of national rules, regulations and norms of enforcement, often differing vastly from one country to the next. Within this are, notably, the policy decisions taken in Latin American and Caribbean countries of emigration and of immigration (such as Argentina, Venezuela and Costa Rica). And, as our review of United States-Mexico migration relations below will show, the choice of "no policy" is itself a policy choice (Alba, 2009). We do not mean to imply by this observation that there is, or that there should be, a single set of rules for all countries, but simply that national rules work in interconnected ways.

The global economic crisis, particularly since the collapse in September 2008 of Lehman Brothers, has thrown immigration centre stage in many countries. The "urgency of now" invoked by President Obama may loom large for immigration reform precisely because of this crisis, but should not be allowed to obscure the fact that the underlying need for reform is independent of it.

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To see this it is important to distinguish phenomena linked to business cycles from longer-term trends. Demand for immigrant workers may be expected to decline with the crisis (a shorter-term phenomenon), while differences in the demographic profile of countries of immigration and emigration – and the spur they provide to international migration – will endure in the longer term. Of course, classifying phenomena as short-term or long-term is harder than it looks: as the Macro Overview of this *Outlook* showed, some of the social and economic outcomes we are observing now are cyclical, and some stem from longer-term transformations being wrought by this crisis. Nevertheless, it bears repeating that immigrants are disproportionately feeling the pain of the crisis in many countries. In Spain, for example, the – already high – general unemployment rate of 17.4% is in fact a compound of 15.2% for native-born workers and an alarming 28.4% for the foreign-born[3].

This chapter will look at how this reform might be undertaken and the role that policy makers in Latin America can play in this. The approach adopted is guided by a desire to foster improved development outcomes in Latin America and the Caribbean, while recognising that any such improvement must be accompanied by gains to countries outside the region in order to be politically feasible.

WHY ACT? THE CASE FOR A POSITIVE RESPONSE

The potential gains from freer migration are huge...

If the gains from international mobility are as great as this *Outlook* argues, should not policy makers merely stand aside and let migrants go where they wish? The economic gains from international labour mobility are certainly huge and the potential gains from further liberalisation are, if anything, larger still. An early study by Hamilton and Whalley (1984) estimated that eliminating all barriers to international people flows would *double* world GDP. Subsequent calculations have been slightly less dramatic, but even so, Hatton (2007) summarises the literature by saying that the gains from free people flows are about ten times as large as those from free trade. The foregoing chapters of this *Outlook* have argued that there are gains to all parties. Migrants realise extraordinary income gains relative to remaining at home. Countries of origin gain from remittance inflows and may benefit from increased earnings for low-skilled workers (even acknowledging concerns about brain drain). Countries of destination benefit from increased efficiency in labour markets and increased fiscal revenues, often offsetting a growing burden from an ageing population. To be sure, these gains are not equally shared – benefits flow notably to migrants, their families and new employers – and some groups run the risk of being losers from increased immigration (this is equally true in OECD as well as Latin American and Caribbean countries of destination). But these are challenges for policy design not reasons to forgo the rich potential gains.

A second rationale for public action is economic. International migration can create externalities – that is, costs or benefits which are imposed upon third parties, leading to inefficient allocation of resources. An example is the brain drain. Say a person finances her education in the country of her birth and then leaves to take a job in a second country; this does not necessarily mean there are externalities. But if her education was instead paid for (even in part) by resources provided by the tax payers of her birth country, then her emigration means that part of the return to that public investment is lost to them. Moreover, if there are positive externalities from having educated people in the economy – and much of the modern theory of economic growth assumes that there are – then the

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country to which our migrant moves is the beneficiary of positive externalities. Another example is the law-enforcement costs associated with patrolling borders to reduce illegal immigration: these costs are arguably negative externalities imposed upon countries of destination by migrants and their putative employers. A typical response to externalities would see public policy subsidise economic actions that provide positive externalities and tax actions that lead to negative ones. But of course, the mere presence of externalities does not mean that the correct policies will be easily implemented – and all the more so if the externalities cross borders. This is a point to which we will return below.

...and reform may also reduce some of the externalities associated with current regimes

Other inefficiencies might also be addressed by public action. For example, emigration can in principle benefit low-skilled workers in the country of origin by raising local wages or increasing opportunities for work. But these benefits may be lost through badly functioning labour markets, for example if the opportunities created are lost as a result of poor infrastructure preventing internal labour mobility. Public policy that facilitates domestic labour mobility could ensure that more people gain from migration.

As some of these examples suggest, it is not always the case that imperfectly functioning markets justify public action, but rather that imperfect policies need to be reformed. Irregular migrants "impose" enforcement costs on the United States or Spain in part because those countries do not provide legal access to their labour markets at levels commensurate with gaps between demand and supply in many of their domestic labour markets – arguably, what needs to be changed in such cases is the legal access to jobs rather than "taxing" migrants or employers.

Even where the net gains from migration are positive, there may be grounds for public action. Some of these transcend economic concerns: for example, better protection of migrants and safeguarding of human rights may be needed, even if migrants are better off in the narrow sense of earning higher incomes abroad.

What Should Reform Look Like?

Whether it is for human rights protection, to reduce economic inefficiencies or to fix policies that are not working, the aim of any meaningful reform of international mobility of people is a new regime of global migration governance. In this effort, it is useful to keep four general principles in mind.

First, it is not a matter of *whether* one wants to have a global governance regime for migration, but *which* one is to be chosen. At any point in time, the totality of rules and enforcement efforts undertaken to manage people and money flows constitute a governance system. As with the Mexican experience of the *política de no tener política* (the "no-policy policy" reviewed later in this chapter), the status quo is itself a system and furthermore inevitably serves the interests of some parties more than others. Again, this does not mean that all countries must have uniform national policies. The conflict among European Union member states regarding the admission of highly skilled workers – presumably one of the less controversial dimensions of migration policy – is an example that suggests that uniformity is not a realistic objective in this field. But accepting this does not mean ruling out concrete co-operation among groups of countries around particular aspects of migration governance.

Second, the nature of international migration means that responsible policy making must involve decision makers in more than one political jurisdiction. Our brief review of the management of people flows between Mexico and the United States below shows that this is in some sense a shared responsibility of the two

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Migration is transnational by definition; in consequence the most effective reforms will be transnational too

countries, and indeed both have largely implicitly recognised this during the last half century. But the likely gains from co-operation are substantially under-realised, and institutions and conventions leading to better outcomes have been notoriously absent. To take policy decisions that affect an Ecuadorian in Madrid, or a Paraguayan in Buenos Aires, or a Mexican thinking about opportunities in Los Angeles, one must engage policy makers in at least two countries. Paraguayan authorities, for example, can offer consular protection to their compatriot in Argentina, but the Argentinian authorities will govern the conditions of his stay abroad. Actions taken by the host-country authorities may have consequences for social protection or financial development of his village in Paraguay; labour-market policy decisions taken in Argentina may well have influenced his decision to seek his fortunes there, and in its turn his presence might have consequences for the use of resources provided by Argentinian tax payers.

For all these inter-related reasons, international migration is a shared responsibility among governments in countries of emigration and immigration. To recommend unilateral policies is increasingly politically risky: action taken by one government will have consequences on both sides of the border and may indeed lead to unintended consequences for the government that took the initial action. Moreover, all countries are increasingly countries of emigration, immigration, circular or return migration, and transit migration. The proportions may differ substantially, but many countries in Latin America and the Caribbean and in the OECD alike share common concerns related to immigration. The sizeable minority of international migration in Latin America and the Caribbean that is "South-South" in nature attests to this.

The idea of unilateral migration policy is misleading since actions will always reverberate in other countries. Furthermore non-discretionary flows, or increased irregular migration, may make them ineffective

Third, to an important extent, migration flows themselves are beyond the control of policy makers. While the research by Ortega and Peri (2009) cited in Chapter 1 clearly shows that tightening of immigration regimes reduces measured flows, this does not mean that policy makers can simply "turn off the tap". Indeed, the statistics presented in Chapter 2 on unauthorised migration to the United States since 2001 suggest that restricting legal movement simply pushed many migrants into irregular migration. One way to illustrate this point is by looking at the relative importance of what the OECD (2006) characterises as "nondiscretionary flows", the share of immigration over which policy makers essentially have no control. Leaving aside unauthorised migration, nondiscretionary flows include family reunification, refugees and asylum seekers, and those with a right to free movement (such as citizens of European Union member states moving throughout the EU area). Nondiscretionary flows are relatively low in the traditional settlement countries: 28% of permanent-type migration flows in Canada and New Zealand, 39% in Australia and the United States. Nevertheless, the non-discretionary fraction is quite high in many European countries: 83% in France, 94% in Switzerland, 95% in Sweden. Much of the difference in the share of non-discretionary migration between the "settlement" countries and the non-European countries noted here stems from the fact that the latter have much less discretionary labour migration overall. But the larger message is that the absolute levels of non-discretionary migration are substantial. Sealing the borders, or even fine tuning the quantity and characteristics of migration flows will thus be at best an imprecise and costly exercise for OECD and Latin American countries alike.

Fourth, the development dimension of international migration has until quite recently been absent from policy debates. Even today, the interests of the countries of origin including those in Latin America and the Caribbean are largely missing from current discussions of immigration reform in the United States and Europe. As an example the European Union's "Blue Card" initiative, launched in late 2007 to attract more high-skilled workers to the region, was the fruit of much co-operation and consultation among different European ministries and

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interest groups. Yet discussion of the measure's possible exacerbation of brain-drain pressures upon developing countries was notably lacking[4]. The review of Mexico's migration relationship with the United States shows that for most of the last 70 years authorities in both countries have not explicitly acknowledged the link – whether positive or negative – between people flows and development of the Mexican economy and consequently they have never sought to capitalise upon those links.

This migration-development link poses a challenge for many OECD countries that have explicitly set themselves ambitious targets to promote global development and reduce poverty worldwide. To meet these objectives, they must entertain the possibility of mobilising a broader range of policy instruments than foreign aid alone, including migration-related policies. Box 6.1 illustrates the complexity of policy coherence for development in the context of the manifold economic relationships between Spain and Ecuador[5].

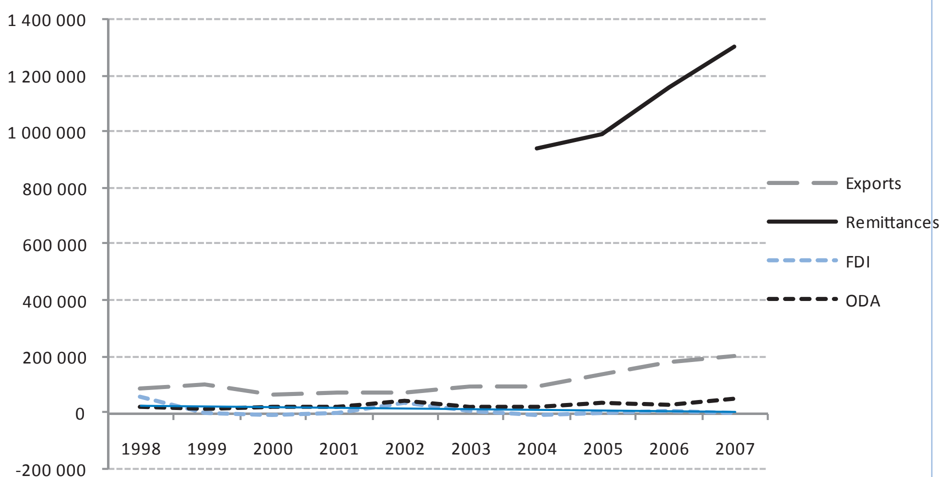
Migration policy must be seen as part of the broader development agenda, for which the OECD countries have set themselves ambitious targets

Box 6.1. Are Spain's Policies Coherent with Ecuador's Development?

The economies of Spain and Ecuador are linked in many ways, but the migration of Ecuadorians to Spain – and the money that they send home – is rapidly becoming the most important economic connection between the two countries. This poses important challenges for policy makers in both countries as they seek to promote growth and development in the South American country. Within the overall economic (financial and trade) relations between Spain and Ecuador there is a clear predominance of migrants' remittances sent from Spain to Ecuador. Although it is likely that the current economic and financial crisis will have decreased these flows in 2008 and 2009, data for 2004-07 show that remittances accounted for more than 80% of the economic exchanges between both countries.

This box first examines the role played by these remittances, and then puts this in the context of the overall economic ties between the two nations.

Figure 6.1. Economic Relations between Ecuador and Spain (EUR)



Source: OECD Development Centre research, Bank of Spain, MITYC (DataComex and DataInvex), MAEC and OECD (OECD.Stat).

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Though the information available to evaluate the impact of remittances on development in Ecuador is sparse, the Real Instituto Elcano and the Ecuadorian unit of the Latin American School of Social Sciences (FLACSO) obtained additional data on the migrant, the recipient of remittances and remittance flows. The analysis of the data shows no significant impact on poverty reduction and a moderate negative impact on inequality (Olivié *et al.*, 2009). These results – which it has to be noted have only a narrow relationship with migration, given that migrants are mainly drawn from non-poor households – imply that it is necessary to rethink co-development programmes where remittances are an issue. One possible conclusion is that the Spanish authorities could achieve more leverage by using education to improve access to remittance channels in Spain and to influence the use of remittances in the hands of their recipients. A relatively easy measure would be to work to reduce transmission costs.

The second-largest source of Ecuador's revenue from Spain is exports of goods and services, which accounts for the bulk of the remaining 20%. Though a decade ago trade was volatile, exports have increased steadily since, more than doubling in value terms. The most pronounced increases were immediately following 2005, when exports rose from a little over EUR 135 million to close to EUR 200 million in just two years. Commodities and primary products dominate. The most important single export is bananas – a good which typifies the way in which trade and development interact. The entry of bananas to the European market is the subject of special regimes which have been the subject of various disputes at the WTO. Ecuadorian bananas currently face a tariff of EUR 176 per tonne and negotiations even to reduce this are making slow progress (to a proposed EUR 114 per tonne, over as much as 11 years).

The third largest source of funds is ODA. With the single exception of 1998, this has exceeded net FDI every year. Its evolution is surprisingly erratic. In 1998, ODA was just over EUR 18 million, by 2002 it was more than EUR 45 million only to fall back over the next two years. Stronger figures in 2005 and 2007 (EUR 50 million, the highest annual figure) buttress a lower one in 2006. This erratic character is largely explained by the lumpy nature of the policy programmes that lie behind the funding, ODA loans and debt forgiveness in this case. Greater security of flows, and discretion in their use might improve their value to the recipient and allow for them to be leverage in (for example) supporting market assessments of the economic outlook.

Last – and perhaps unfortunately least – is FDI. Only in 1998 did this exceed ODA and disappointingly the absolute and relative trend is downward. In 1998, net FDI was more than EUR 60 million, but it decreased sharply the following year and did not recover until 2002, when nearly EUR 41 million of Spanish direct investment flowed into Ecuador. From 2003 there were further declines and recoveries ending with a net FDI flow of just over EUR 6 million in 2007. The bulk of these investments are concentrated in relatively few sectors. More than 71% of the FDI flows for the period 1998-2007 were concentrated in extractive industries, of which the majority related to the oil sector. Taking into account the primary single-production and export bias of the Ecuadorian economy, there would be advantages to the Spanish authorities promoting investments which favour diversification and a higher value-added, perhaps through the tax system in Spain.

Migration – in both directions, of course – has created deep links between Ecuador and Spain. These find expression in the financial flows between the two countries. The flows exist but there may be a place for policy making to respond more directly to the reasons for those flows and to the social and human links that support them.

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WHAT CAN COUNTRIES OF EMIGRATION DO? MEXICO'S EXPERIENCE

The history of US-Mexican migration provides a good summary of different policy approaches and their effects

Movement from Mexico to the United States is the single largest migration corridor in Latin America and the Caribbean, and has a comparatively long history which starts well before the massive post-World War II flows in which contemporary Mexican migration is rooted[6]. The Mexican experience, spread across people and time, therefore provides plenty of evidence that may illuminate issues less clearly seen in other migration corridors. We examine this long history by looking at its distinct periods, and thereby seek to draw an understanding of the migration-policy tool kit that Mexico has deployed during the last half century (Alba, 2009).

Mexico's migration falls into three chronological periods according to the policy response at the time:

1) **The *Bracero* Programme (1942-64): Jointly Managed Seasonal Flows**
The *Bracero* ("Day-labourer") programme brought Mexicans to the United States as seasonal workers, particularly in agriculture, initially to ease labour shortages during World War II. Whatever its imperfections the programme provided binding agreements between the two countries. The programme was eventually terminated but the flows of migrants continued unabated – in part because it had institutionalised the role of migrant Mexican workers in United States agriculture.

2) **"*La política de no tener política*" (1964-86): Tacitly Serving the Interests of Employers and Migrants**
During this period of "the policy of not having a policy", which lasted for as long as the formal *Bracero* programme, a tacit bilateral understanding was marked by little government intervention on either side; the economic interests of the migrants and employers were more or less passively served by this arrangement. During this time, Canada and Mexico began a high-profile but much smaller scale Seasonal Agricultural Workers Programme (SAWP), beginning in 1974. Between 10 000 and 15 000 Mexican workers participate in the SAWP annually, largely heading for the Canadian provinces of Ontario and Quebec.

3) **The IRCA Era (1986-2007): Combating Unauthorised Immigration**
The 1986 Immigration Reform and Control Act (IRCA) in the United States definitively put an end to the "no-policy" era in the United States, and forced Mexico to do the same. IRCA sought to reduce unauthorised Mexican immigration dramatically (by requiring employers to verify their employees' immigration status, and by increasing resources for border surveillance and control). At the same time, IRCA established channels for regularisation of existing undocumented migrants, leading to the regularisation of some 2.8 million individuals, 2.1 million of whom were Mexican. It also left open the possibility of allowing in additional farm workers, if needed. The subsequent 1996 Illegal Immigration Reform and Immigrant Responsibility Act (IIRIRA) substantially strengthened the law-enforcement dimensions of US immigration policy. This hardening of the immigration regime in the United States may have persuaded many migrants to opt for permanent rather than circular migration, as the likelihood of being able to cross the border again in the future became more uncertain for both legal and unauthorised migrants. During this phase, immigration from Central America across Mexico's southern border grew as a security and social policy issue in Mexico. Most of these immigrants came from Guatemala,

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either originating in refugee flows from the Central American country's civil war, or in seasonal labour flows to harvest coffee in the state of Chiapas (Freije, 2007).

A high-level rapprochement on migration issues between Presidents Fox and Bush early in 2001 was seen by the Mexican authorities as an opportunity to advance its agenda, but this brief interlude was abruptly brought to an end by the terrorist attacks on the United States in September 2001. Immigration policy priorities in the United States shifted from a focus on economic issues to security and anti-terrorism. When the Bush administration proposed a new immigration policy framework in 2004, it was dominated by security considerations and was explicitly opposed to any regularisation. The extensive policy debate surrounding this proposal nonetheless failed (in 2007) to lead to comprehensive immigration reform. From 2006 the Calderón administration in Mexico began to play down migration in its dealings with the United States, and some observers began to talk of a "*de-migratización*" of United States-Mexico relations.

What policy levers are available to governments in Latin America and the Caribbean to increase the net benefits from migration flows? Mexico's experience suggests there are essentially three[7].

Mexico's policies have encouraged the productive use of remittances…

Migration policies narrowly conceived include visa policies, consular activities and border controls, but also, increasingly, all manner of relations with communities of nationals living abroad. Relations with the Mexican diaspora in the United States have focused particularly on reducing the cost of remittances, and encouraging migrants to channel these money flows into community development projects. Box 6.2 reviews the success of the *Tres por uno* initiative – a programme, which, to be sure, is dwarfed by the magnitude of total remittances into the country.

Box 6.2. Mexico's "*Tres por uno*" Programme: Successes, but on a Small Scale

Mexico's *Programa 3x1 para Migrantes* ("3-for-1 Programme for Migrants") was established by the country's Social Development Secretariat (Sedesol) in 2005. Under the scheme, each of the three levels of government – federal, state, and municipal – matches any funds that migrants abroad contribute to community-development projects. The goal is to increase the coverage and quality of social programmes (health, housing, education, communications and cultural) and productive infrastructure, particularly in poorer regions or those with high emigration rates. At the same time, it aims to strengthen the links between migrants and their communities of origin. Specific investments are based on proposals from migrants' organisations, with projects approved by a government committee chaired by Sedesol.

The initiative is a development of similar projects implemented in the Mexican states of Zacatecas, Jalisco, Michoacán and Guanajuato in the 1980s and 1990s. In particular, it draws on the successful experience in Zacatecas, where migrant funds for community-development projects were matched one-for-one by the state. A dialogue between migrants, migrants´ organisations and the different levels of government yielded a programme with twin objectives: facilitate those projects that migrants wanted in their home towns, and generate a relationship of trust between the state government and migrants. (In 1992, under the Salinas administration, federal funding was added making the scheme two-for-one; the Fox administration brought in the present three-for-one arrangement in 2002, under the name *Iniciativa Ciudadana 3x1*; see Iskander, 2005.)

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It may be too early to evaluate the national 3-for-1 Programme, given that in most states it has only recently been implemented. However, some figures and qualitative discussions have recently become available. In particular, an external evaluation (Aparicio *et al.*, 2008) by the *Centro de Investigación y Docencia Económicas* (CIDE) shows several important results. According to this report, 3.3 million people benefited from the programme in 2006 and 4.6 million in 2007 (around 1.5 million on average since 2002 for the current programme and its predecessors; coverage rates cannot be calculated given that there is no definition of the pool of potential beneficiaries). Federal investment mobilised by the programme reached almost MXN 340 million in 2006-07 (EUR 17.8 million). According to Sedesol (2008) the total financial resources in 2009 may exceed MXN 2 billion (some EUR 105 million) of which MXN 535 million is federal government money, MXN 500 million from the municipal and state governments and the balance from migrants.

Expenditure is concentrated in the states of Zacatecas, Jalisco and Michoacán (54% of total federal resources disbursed under the programme). Nearly two-thirds of the resources are assigned to regions where levels of marginalisation are characterised as low or medium. However, highly marginalised municipalities received less than 24% of programme resources in 2007. This regional distribution explains in part why so little spending has been on basic social infrastructure such as electricity and water provision (less than 15%).

CIDE´s evaluation concludes that the 3-for-1 Programme is accomplishing its stated goals: strengthening the links of migrants with their home communities and increasing infrastructure investment in high-emigration areas (although no effectiveness analysis is available). The success of Zacatecas programme does seem to be scaling up.

Their main reservation stems from the regional redistribution objective: infrastructure investment in marginalised areas. This may simply not be achievable. The greatest need is in the areas least likely to receive funding because the poorest and most marginalised persons do not emigrate, or at least they emigrate less. CIDE shows than less than half of the municipalities with high and very high marginalisation (according to data from the *Consejo Nacional de Población,* Conapo) also have medium or high emigration rates. Even more striking is the conclusion of BBVA Bancomer (2009) that among the 93 municipalities with virtually zero emigration in Mexico fully 91 exhibit high or very high levels of marginalisation. By contrast, the highest emigration rates are found among middle-income regions. Given that the 3-for-1 Programme is demand-driven (relying on migrants' proposals), under-representation of the poorest municipalities and of basic infrastructure follows. CIDE suggest that, in order to overcome this in-built bias, quotas and/or stronger financial incentives be introduced for these regions.

...provided practical help for migrants...

A recent innovation under this heading is the creation of the *matrícula consular*, an identity card issued since 2002 by the Mexican state to migrant nationals regardless of their legal status in the United States. In the year of their introduction nearly a million *matrículas* were issued. Though primarily intended to extend consular protection to Mexicans abroad, it is well-known that these cards have become an accepted form of identification for some private and public institutions in the United States, allowing migrants – including unauthorised migrants – some access to banking and public services. Such measures certainly help with the effective integration of migrants into the life of their communities abroad[8].

Second, there are non-migration policies with effects on migration and development, for example, the development of *maquiladora* industries along Mexico's border with the United States. These plants, which assemble components imported from the United States in-bond and re-export the results back across the border, have had consequences for migration and development, although the nature of these is a matter of debate. On the one hand, the *maquiladoras* in

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principle have created jobs which may have absorbed candidates for emigration – more than 1 million workers since 2000. On the other hand, they have attracted workers from all over Mexico to the border states, from where they may have used *maquiladora* employment as a springboard for crossing into the United States; in this view, the *maquiladoras* increased emigration.

A second example is the signature of the North American Free-Trade Agreement (NAFTA) by Canada, Mexico and the United States. The leaders of the latter two countries explicitly linked this trade opening to a reduction in migration pressures, President Carlos Salinas of Mexico famously declaring, "We want to export goods, not people."[9] However sincere leaders might have been about trade replacing migration, in the event Mexican emigration to the United States probably accelerated following the adoption of NAFTA. From a level of between 325 000 and 360 000 a year during the latter half of the 1990s, yearly emigration may have surpassed 500 000 a year since 2000. In fact, the effect of NAFTA itself on migration flows has been negligible, according to statistical analyses[10].

...and promoted agreements at the international level

A third class of policies are international agreements or processes directly or indirectly related to migration, at the bilateral, regional and global levels. Mexico, for example, promoted and adopted the United Nations Convention on the Rights of All Migrant Workers and Members of Their Families in 1998. In 1996, it helped establish the Regional Conference on Migration[11] – the so-called Puebla Process – together with the United States, Canada, all of the Central American countries and the Dominican Republic, to support co-operation initiatives, the training of personnel, technical assistance, the establishment of guidelines for return and repatriation of migrants, and to fight trafficking and smuggling of migrants.

NEGOTIATING FREE MOVEMENT?

What are the prospects for a new regime for the global governance of international migration that better embodies a spirit of partnership? And what will different countries bring to the negotiating table?

By and large, many Latin American and Caribbean countries are likely to have migration policy agendas similar to that pursued by Mexico during the brief Bush-Fox thaw in migration negotiations: regularisation of unauthorised migrants; temporary-worker programmes; special immigration visas for their citizens; economic co-operation for the development of migrants' regions of origin. (Creation of safe conditions along the shared border was an additional objective of the Mexican agenda,but less relevant to most other countries.) Such an ambitious set of goals can only be achieved by the co-ordinated use of all three policy areas defined above: direct migration policies, indirect non-migration policies and international agreements.

Bilateral agreements have demonstrated successes and many have been agreed

The review of Mexico's experience earlier in this chapter underscored the importance of bilateral co-operation (think of the *Bracero* programme with the United States and the SAWP with Canada as well as Mexico's 2008 bilateral agreement with Spain). Mexico is not alone in entering into bilateral migration agreements, indeed a 2004 report by the OECD lists 176 of them. (A selection of Latin American examples from that report are listed in Table 6.A.1 in the appendix to this chapter; Table 6.A.2 lists other agreements which, like NAFTA for Mexico, are likely to influence the relationship between migration and development.) If Latin American and Caribbean governments are looking for policy levers, the sheer number of these agreements might suggest that they should be considered.

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But do these bilateral agreements make sense? Fernández-Huertas Moraga (2008), in a simple economic model, argues that unilateral migration policy is inefficient because it involves externalities. In brief, unilateral restrictions on entry impose a cost on the country of origin, by closing off earning opportunities to potential migrants and denying an escape valve for labour markets marked by low wages and underemployment. At the same time they tax the country of destination (through the incentive they create for more irregular migration) in the form of the costs of enforcing the policy. Bilateral agreements, in this view, allow the parties to internalise some of these externalities for example by establishing guidelines that provide for legal migration resulting, in principle at least, in lower enforcement costs.

Those readers familiar with earlier debates about the best model of governance for international trade in goods and services will see the resemblances here. What, that debate asked, is the optimal arrangement: unilateral liberalisation, bilateral free trade arrangements, regional free trade areas, or a world trade organisation? Economic historian Timothy Hatton (2007) asks why we do not have a world migration organisation; a question that has been echoed by Latin American leaders. Before going any further it has to be pointed out that the analogy between these debates is illustrative but clearly can only be taken so far. Labour flows involve human beings. And human beings have needs and create moral obligations in a way that goods do not. Furthermore much of the debate surrounding international migration in countries of destination – including in Latin America – is about aspects of migrants other than their status as economic agents. Examples include the costs associated with integration of migrants into the host country's society.

While trade negotiations offer interesting parallels for migration policy, two important distinctions must be recognised: reciprocity is lower and migration is driven by absolute rather than comparative advantage

So given the trade history and noting these differences between the flows of goods and people what are the implications for the ease or difficulty of securing international agreements on migration? Hatton is generally quite pessimistic about the prospects for the emergence of a world migration institution. He notes that the economics of trade in goods differs from that of movement of people in at least two important ways.

First, people flows do not offer much prospect for what is called "reciprocity" in trade negotiations, the notion that two countries can offer each other concessions of roughly equivalent value. Benefits always tend to be much greater for agents in migrants' countries of origin than those for countries of destination (while the political visibility of costs and benefits will tend to be the converse). Furthermore, if those gains are captured largely by migrants, their families, and their communities, and not spread to the wider economy at large, then even country-of-orgin governments will have little motivation to pursue international negotiations[12].

Second – and this underlies the first point – international migration, especially between poor and rich countries, is driven by absolute advantage, while trade in goods is driven by comparative advantage. That is, wage differences between El Salvador and the United States, or Morocco and Spain, are due to differences in total factor productivity between the countries, not to differences in factor endowments. If so, there is greater scope for productive co-operation among countries with less disparate standards of living. Perhaps the Puebla Process is a harbinger of greater intra-Latin American co-ordination in this respect.

Popular resistance to trade liberalisation might provide some clues about opposition to more liberal human mobility. The fact that the net gains from total liberalisation of people flows could theoretically be quite large raises the possibility of compensating those who stand to lose – making "side payments" in economic parlance. In practice these may be difficult to make. A clear example of potential side payments would be explicitly to reinforce social protection systems

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for lower skilled workers who may find themselves in competition with immigrant workers, but the institutional feasibility of this kind of reform would be difficult in many countries. On the side of countries of origin, compensation might involve transfers from industrialised countries to developing countries to offset the losses to the latter from the brain drain of highly skilled people; the magnitude of such transfers might well prove larger than current foreign aid flows.

In addition to the difficulty of compensating losers, there may be considerable uncertainty before the event about just who will be a loser. Indeed, this kind of "individual specific uncertainty" has been postulated as a potent explanatory factor behind resistance to reform more generally[13]. Low-skilled workers or earlier waves of immigrants may strenuously oppose further immigration, even if in fact *most* of them might gain, given that *some* of them will lose their jobs or suffer pay cuts without knowing ahead of time who those unlucky people will be.

And of course there may be non-economic considerations as well. Strong opposition to immigration may spring from fears that new languages, religious practices or social behaviour that migrants bring with them will dilute or transform national culture.

South-North migration in Latin America and the Caribbean is still far greater than South-South movement. The gains would therefore be lower, but feasibility may mean that South-South agreements represent a better starting point for governments in the region to begin striking bilateral and multilateral agreements.

FIVE CONCRETE ACTIONS DECISION MAKERS CAN UNDERTAKE

This *Outlook* ends on a practical note, drawing out five policy recommendations suggested by its analysis and informed by this chapter's discussion of the policy space available to governments. These suggestions engage the public as well as the private sector, in Latin America and the Caribbean as well as in the OECD countries.

Policy should recognise the needs of labour markets and the potential for supply

Create legal and flexible labour market access on a par with labour demand. In many countries, employers in many sectors aggressively seek more immigrant workers to fill gaps in the labour market, and even so cannot always find enough workers. Three examples from the United States amply illustrate this phenomenon. Firms in the information technology sector regularly lobby the Congress to expand the quota on H1-B visas under which highly skilled foreigners can work on a temporary basis in the country – Microsoft's Bill Gates testified to a Senate committee to this effect in 2007. In agriculture, farm owners lobbied hard to loosen restrictions on H2-A temporary farm worker visas in late 2007, as crops lay rotting unharvested in the fields[14]. In medicine, if current projections of the shortage of nurses in the United States are accurate, a clear opportunity will arise for nurses in Latin American and Caribbean countries with training to United States standards to fill labour-market gaps.

These examples suggest that in a world of closed borders there will be unfilled jobs in the short term and over the longer term significant structural changes in an economy (in the examples above, the high-tech and agricultural sectors of the United States could shrink in response to continued scarcity of labour or its cost – the very fears in fact recognised by the existence of the H1-B and H2-A visas)[15].

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In addition to unfilled jobs, though, the mismatch of labour supply and labour demand and the large earnings differentials between economies mean that many migrants will seek out these job opportunities without legal authorisation. The incentives for irregular migration – and the associated human cost – could be reduced were legal channels expanded.

Extend social protection to more Latin American migrants. Chapter 3 showed that Latin Americans lose pension and health coverage when they cross borders to a proportionally greater degree than migrants in other parts of the world.

Making pension rights portable is an important first step, and the relevant agreements are ready for ratification

Making pension rights fully portable – as they are already for some Latin American migrants – would increase the social wage earned by these migrants and reduce their vulnerability to risks in old age. The necessary steps are both quite clear and may be accomplished in the short term. First, implementing the United States/Mexico Totalisation Agreement (signed in 2004 but not yet ratified) would at once extend coverage to a much larger share of Latin American migrants, notably Mexicans. Second, Ibero-American countries should ratify as soon as possible the Ibero-American Social Security Convention agreed at their 2007 Summit in Chile. Together these would assure that the vast majority of Latin American migrants would keep their pension rights when moving abroad or returning home. In the longer term policy makers should aim to extend both agreements to cover the portability of health benefits.

Complementary work needs to be done to improve the quality of social-security coverage (not only pensions, but also health assistance) for migrants and non-migrants alike. Finally, a related problem, particularly acute in the United States, is that of irregular migrants contributing to social security schemes that they will never be able to access. As noted in Chapter 3, perhaps three-quarters of irregular migrants in the United States are "on the books" in this sense. This is an area where creating more opportunities for legal labour-market access for migrants can help increase their social-security coverage.

Even small reductions in the cost of remittances can yield substantial benefits for recipients

Reduce the cost of remittances. The cost of remittance transfers to Latin America has fallen dramatically in the last decade. This is the result of a combination of active public policy (for example in promoting agreements among banks to eliminate some charges and fees), and increased competition in the financial services sector. Neither the policy-driven nor the market-driven solution would have been sufficient of itself, but the result has been that Latin American and Caribbean migrants and their families now lose much less in fees and other charges than their counterparts in other parts of the developing world. But this does not mean that complacency would be justified: in a region that receives USD 80 billion in remittances in a year a further reduction of 1% in average transfer costs would shift USD 800 million from transfer companies to migrants' families. Encouraging low-cost or zero-cost forms of money transfer could achieve this kind of reduction. Mobile payments are an emerging example in the region of an alternative and cheap money transmission system. However, as Chapter 4 has shown, turning mobile payments into broader mobile banking depends on policy makers developing a clearer regulatory framework for these institutions, something which they have yet to do in most countries in the region.

Broaden the benefits from remittances. The analysis of the "interaction model" in Chapter 5 confirms that ratings agencies appear to take remittances into account when calculating the sovereign risk of emerging economies. This can translate into lower costs of public debt for governments in the region – a macroeconomic benefit from remittance inflows. However, the impact of including remittances on capital markets remains weak with respect to other fundamental variables that affect ratings.

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Chapter 5 provides shadow ratings for countries where relative remittances flows are high. A suitable public-private partnership could use a similar methodology to boost country coverage and to supply the market with useful information on and education about the potential ratings for some of these as-yet unrated countries.

Remittance policy should promote opportunities for senders and seek to educate the capital markets

Of course, there are other ways in which decision makers in Latin America and the Caribbean, public and private, might generate more such macroeconomic benefits from remittances, including the issue of diaspora bonds (as India and Israel have done in the past), or securitising remittance inflows; again, these possibilities have been discussed in greater detail in Chapter 5.

However, if Latin American countries are reaping some of the macroeconomic benefits of remittance flows, there remains significant work to be done to gain more at the microeconomic level.

Policy debate over "non-productive" use of remittances – consumption rather than investment – is a dead end. These are private transfers within or between families and it is up to those families to decide how they will be deployed. There is nevertheless a role for public action to *influence* those choices and to *widen the opportunities* for deploying those resources. The Mexican 3-for-1 programme is a good example, using incentives to get migrants to channel remittances into community investments.

In this vein, efforts to extend the reach of the formal financial sector – "bankarisation" – can provide benefits to migrants' families and to national economies at the same time. Receiving remittances is the first step along a road that with suitable public help can lead to increased financial literacy and ultimately incorporation in the formal financial economy. A step along this road could be the public provision (or promotion) of financial instruments such as stabilisation funds or pooled currency derivatives that could help stabilise the domestic purchasing power of remittances. Bankarisation would be a natural counterpart and so see currency-risk mitigation go hand-in-hand with formalisation and financial education.

Diasporas retain many family and cultural links to their home countries. As a result they may be a source of ideas, finance and skilled labour

Engage the Diaspora. The worldwide communities of migrants and their children born abroad constitute emerging transnational political forces that can be engaged both by countries of origin and by countries of destination[16]. Governments can work with migrants' organisations to pursue policy objectives jointly in the domains of labour markets, social protection, integration, development co-operation – and international migration. Diaspora communities and migrants' networks can be engaged to encourage skills transfer (the "brain sharing" of Chapter 3), whereby skilled expatriates can contribute to their development in their home country without definitively returning. Both have a role too in the strengthening of trade and investment networks.

Countries of destination can engage to improve the delivery of social services, facilitate integration and to improve labour-market access. They can also work as partners in international development efforts – an engagement that is especially relevant given the common interest of home and host countries in regional economic development and the opportunities for co-development. Such engagement fits well with the "ownership principle" – that developing countries set their own strategies for poverty reduction, institutional improvement and reduction of corruption – encapsulated in the 2005 Paris Declaration for Aid Effectiveness.

This raises the question of whether governments should seek to reach their diaspora through existing migrant networks or create one specifically for this purpose. There is no definitive answer; however, drawing on the reach and experience of existing networks is the model in the majority of cases today.

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Government's role then is to build upon endeavours led and owned by the diaspora groups through the mechanism of a public-private partnership[17]. Latin America already contains good examples of this in action. Mexico's 3-for-1 programme is one, also noteworthy are *ColombiaNosUne* and its *ColombianosNegocian* sister initiative, ECODAR (in Argentina), and *ChileGlobal*. Details of each can be found above and in Chapter 3. Through those networks the respective governments mobilise and benefit from the potential, knowledge, contacts and capacities of their co-nationals abroad in order to attract business opportunities, transfer of knowledge and know-how. This "virtual return" goes some way towards solving the problem of the brain drain.

Unfortunately, this positive engagement by countries of migration is not yet being matched by their receiving counterparts. Joint action would leverage still further existing arrangements with the diaspora and – of potentially lasting importance – create a genuine focus for and strengthening of working contacts between the two national authorities. Moreover, in pursuing their development-policy goals recipient countries are not taking advantage of the knowledge, suggestions and access that fuller engagement with their immigrant communities could provide (de Haas, 2006).

The links at the human level that diasporas provide can be a springboard to closer international co-operation

The transnational business networks outlined in Chapter 3 can form part of this. Governments in destination countries could support the existing efforts of countries of origin, both governments working together to promote economic development through diaspora-led trade and investment links, as well as mitigating brain drain. Specifically, development agencies and foreign-trade authorities could deliver this support: by offering capacity building assistance; through economic incentives to transnational migrant entrepreneurs working with their country of origin (whether this engagement takes the form of employees in the country of origin, trade with origin country, the development of new markets, or knowledge transfer); by actively promoting engagement between national entrepreneurs seeking new markets and transnational migrant entrepreneurs; and, last but not least, by providing funding, technological assistance, and logistical support to those business networks that have a strong developmental potential.

More generally, receiving countries should seek to move to an immigration policy that reflects the actual demands created by their own economies and the national actors within it. Provisions that made it easier for migrants to come and go would not only be humane but would also remove the sense that many migrants – whether regular or irregular – have that once inside the "fortress" they must at all costs stay put.

Migration – in both directions – is something that indissolubly links the OCED countries with Latin America and the Caribbean, through history and for the future. The gains from a realistic approach to the pressures that migrants feel and to the economic forces that create them could bring huge benefits to migrants, the societies they live in, and those they leave. Were one to apply only financial criteria then – as we have seen – it is safe to conclude that these potential gains outweigh those from free movement of capital or goods. Yet it is these latter two, and above all trade, that seems to dominate international relations, perhaps particularly so in the case of Latin America and the Caribbean. But there is more to migration than just numbers. It has its human side too and there are benefits here that cannot be so easily quantified, in terms of human rights, human development and family life. These matter for human development which takes us to another theme: that migration should be seen in the context of the broader development policy for both countries of origin and destination, rather than as a separate and – often paradoxically – domestic issue.

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As this year's *Outlook* has demonstrated there is no shortage of tools available to the policy maker. These start from "easy wins" that can be implemented unilaterally by governments in one nation. They grow by drawing in migrant networks and bilateral partners. All these are worthwhile, but the biggest prizes lie in the sphere of broad international co-operation. We all live in one world, united as never before by trade, finance, transport and communications. Patterns of migration across the globe increasingly reflect this. Sooner or later policy will have to follow.

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NOTES

1. The recent European experience is summarised in Dayton-Johnson *et al.* (2007), Ch. 2.

2. Julia Preston, "Obama to Push Immigration Bill as One Priority", *New York Times*, 8 April 2009, p. A1.

3. Statistics from the Spanish Instituto Nacional de Estadística (INE), April 2009. While these rates of unemployment are high by the standards of recent decades and the source of much political concern, Spanish unemployment more regularly attained these levels 20 or more years ago.

4. An exception was the United Kingdom, where earlier debates surrounding recruitment of health workers from developing countries to staff the National Health Service had arguably sensitised public opinion to brain drain issues. The NHS, in fact, established ethical recruitment guidelines that forbade efforts to attract workers from a number of developing countries (Findlay, 2006).

5. OECD (2007) analyses this problem of policy coherence for development, with a focus on international migration from developing countries to OECD countries.

6. Many of the areas to which Mexican migrants go in the United States were part of Mexico until the February 1848 Treaty of Guadalupe Hidalgo put an end to the Mexican-American War and granted the victor more than half of Mexico's territory; thus the presence of Mexican-born people in the US Southwest predates the entry of those areas into the United States.

7. See Dayton-Johnson *et al.* (2008) for more on this classification.

8. In their survey of migration-management policies among Mediterranean emigration countries, Tovias and Tovias (2009) make the same argument for measures such as the Moroccan state's provision of religious and Arabic-language instruction to Moroccan diaspora communities in France and Spain.

9. Drawing on the economic theory of factor-price equalisation, this view held that Mexico would profit from increased regional trade by specialising in the production of goods that used low-skilled labour relatively intensively, thus absorbing would-be emigrants into new manufactured-exports sectors.

10. See Boucher *et al.* (2007) and Richter and Taylor (2008) for more details.

11. See www.rcmvs.org or www.iom.int/jahia/Jahia/policy-research/puebla-process.

12. However, some Latin American political leaders have argued that restrictions on people flows could be met with restrictions on capital flows, an equivalence which makes clear there is an area of reciprocity which covers the flow of the factors that are abundant in developed countries: capital. If the question is broadened to embrace all factor mobility, then there is an arena for reciprocity. Why this is not the case is an open question.

13. This kind of resistance to reform is modelled in Fernández and Rodrik (1991); see also Ciccone (2001).

14. Nicole Gaouette, "US working to let in more immigrants", *Los Angeles Times*, 7 October 2007.

15. See Facchini *et al.* (2007).

16. See Dayton-Johnson *et al.* (2007, Ch. 6) for a discussion of the engagement of migrants' networks in the European context; Dayton-Johnson and Xenogiani (2007) argue that migrants' networks can be encouraged by policy makers in sending and receiving countries to loosen constraining policy tradeoffs.

17. See de Haas (2006).

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ANNEX

Table 6.A.1. Principal Latin American and Caribbean Bilateral Migration Agreements Signed with OECD Member Countries

Sending Country	Receiving Country	Programme(s)
Argentina	France	Traineeship
Belize	United Kingdom	Working holidaymaker
Colombia	Spain	Seasonal Employment, Guest Worker
Dominican Republic	Spain	Seasonal Employment, Traineeship
Ecuador	Spain	Seasonal Employment, Guest Worker
Jamaica	Canada	Seasonal Employment (SAWP)
Mexico	Canada	NAFTA[a], Seasonal Employment (SAWP)
Mexico	United States	NAFTA
Mexico	Spain	Seasonal Employment
Trinidad and Tobago	Canada	Seasonal Employment (SAWP)

Note: a) NAFTA includes an element of labour mobility between members under the Trade NAFTA (TN) status for certain professional occupations.

Source: OECD (2004).

Table 6.A.2. Other Agreements Which May Impact Migration Flows

Countries Involved	Agreement (year)
Costa Rica, Dominican Republic, El Salvador, Guatemala, Honduras, Nicaragua, United States	DR-CAFTA (2004)
Canada, Costa Rica	C-CR FTA
Canada, Mexico, United States	NAFTA (1994)
Panama, United States	P-USA FTA (pending)
Antigua, Barbuda, Bahamas, Barbados, Belize, Dominica, Grenada, Guyana, Haiti, Jamaica, Montserrat, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Suriname, Trinidad and Tobago	Caribbean Community (CARICOM) (1973)
Argentina, Bolivia, Brazil, Colombia, Chile, Cuba, Ecuador, Mexico, Paraguay, Peru, Uruguay and Venezuela	Asociación Latinoamericana de Integración (ALADI) (1980)
Argentina, Brazil, Paraguay and Uruguay	Mercado Común del Sur (MERCOSUR) (1991)
Bolivia, Colombia, Ecuador and Peru	Andean Community of Nations (1969)
Colombia, Mexico and Venezuela (no longer a member)[a]	G3 FTA (1995)
Bolivia, Dominica, Cuba, Honduras, Nicaragua and Venezuela[b]	Alternativa Bolivariana para América Latina y El Caribe (ALBA)
Argentina, Bolivia, Brazil, Chile, Colombia, Ecuador, Guyana, Paraguay, Peru, Suriname, Uruguay, Venezuela	Union of South American Nations (UNASUR)[c] (2008)
Canada, Colombia	CC FTA (2008)
US, Colombia, Ecuador, Peru[d]	US-Andean countries FTA (pending)
EU, Bolivia, Colombia, Ecuador and Peru	EU-CAN FTA (pending)
EU, Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua and Panama	EU-Central America FTA (pending, projected 2010)
EU, MERCOSUR	EU-MERCOSUR FTA (pending)

Notes: a) Ecuador, Panama and Peru have held negotiations to join the G3-FTA; *b)* Ecuador has begun the process of joining ALBA; *c)* UNASUR will potentially absorb the Andean Community and MERCOSUR; *d)* Bolivia has begun preliminary FTA negotiations with the United States.

Source: OECD (2004).

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PART THREE

Country Notes

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Argentina

Argentina has a long history of immigration, yet global forces and recent economic, political and social instability have gradually transformed it into a simultaneous sender, recipient and transit pole.

Figure 1. Stock of Migrants and Level of Education of Argentinian Emigrants to OECD and Latin American Countries

Stock of immigrants in Argentina
(Persons aged 15 or over, 2001)

305 557	Paraguay
215 295	Italy
214 338	Bolivia
207 380	Chile
132 865	Spain
382 087	Others
1 457 522	**Total**

Stock of Argentinian emigrants in OECD and Latin American countries
(Persons aged 15 or over, circa 2000)

120 777	United States
92 680	Spain
48 755	Italy
45 877	Paraguay
35 057	Chile
118 250	Others
461 396	**Total**

Proportion of Argentinian emigrants with completed secondary or higher education
(Persons aged 25 or over, circa 2000)

62% - 100%
46% - 62%
0% - 46%

Workers' Remittances
(USD million, 2007)

Inflows	541 (0.2% GDP)
Outflows	334 (0.1% GDP)

Note: This figure reports the stock of migrants recorded in national censuses and workers' remittances in balance-of-payments data. It will therefore not reflect unrecorded formal or informal flows, which may be material.

Source: For details on definitions and sources, please refer to the Statistical Annex.

Argentina is a net immigration country, attracting the largest number of migrants in the region (5.6% of the total population). Most immigrants come from neighbouring countries and, to a lesser extent, Italy and Spain.

Since the late 1990s Argentinians have begun to emigrate in larger numbers, principally to the United States and Europe. Emigrants represent 1.8% of the total population.

Argentinian emigration is generally of people with a medium or high educational level. More than 62% of Argentinian emigrants in the United States have secondary or higher education.

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Migration History and Policy Developments

Historically, Argentina has been a magnet for foreign workers, attracting the largest number of immigrants in the region (around 1.5 million people). European immigrants, principally from Italy and Spain, form the core of this historic migration, which was underpinned by the entry and integration measures provided by the Avellaneda Law (Act Nº 817 of 1876). The bulk of European migrants arrived in Argentina between 1890 and 1950, and their relative share of the population is in a steady decline.

According to the 2001 Census, the largest group of more recent immigrants come from neighbouring countries, mainly Paraguay, Bolivia, Chile, Uruguay and Peru. These migrants face a very different policy setting. Since 1960 entry standards have became steadily more restrictive. In 1981 the Videla Law (Act Nº 22.439) specified a long list of factors disqualifying candidates for immigration and denied labour and education rights to those who did not have formal migrant status.

Most recently Argentina has moved again toward a more open conception of immigration. The Mercosur Free Movement and Residence Agreement (2002) and the new Migration Law (Act Nº 25.871 of 2003) embody this shift. The Law incorporates two new features: a human rights perspective and a regional approach. The Law recognises the right of people to migrate and guarantees education, health and social assistance rights to all immigrants (including those in an irregular situation). From a regional perspective, the Law explicitly recognises the role of migration from neighbouring countries and implements the Mercosur-derived free movement of people. In addition, the "Patria Grande" National Programme for the Regularisation of Immigration Documents was established in 2004 to regularise the immigration status of immigrants from Mercosur and associated states, providing a path to legal residence in the country.

In the late 1990s, new flows of Argentinian emigrants appeared, primarily directed toward the United States and Spain. These flows are dominated by highly skilled middle-class people. These new flows accelerated with the contraction of Argentina's labour market and the rise in unemployment in the wake of the economic crisis of 2001. The 2003 Migration Law also addresses the situation of Argentinians abroad, facilitating voluntary return and seeking to strengthen ties between Argentinians abroad and their home country. The R@ices programme seeks to bolster the nation's scientific and technological capabilities by linking local researchers with Argentinians living abroad, aiming both to discourage migration and encourage the return of Argentinian researchers currently abroad.

Labour Market

Labour-market participation rates of Latin American immigrants tend to be higher than those of Argentinians, evidence that immigration from neighbouring countries is generally economic in nature.

Figure 2 shows the occupational distribution of employed males and females, both migrant and native-born. The occupational profiles of the two groups are distinct. This segmentation suggests that immigrant workers are complementary to the native-born workforce, occupying positions that natives reject. In particular, immigrants are concentrated in construction (for men) and domestic service (for women).

Migrants' employment also reflects differences in educational attainment between these two groups. With the exception of Peruvians, immigrant workers from OECD countries and Latin America are less likely to have completed secondary school than native Argentinians.

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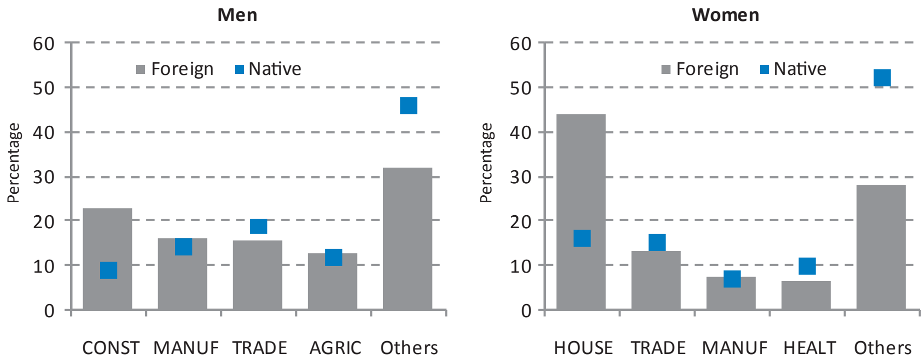
Figure 2. Distribution of Workers in Argentina by Activity and Origin
(Latin American and Argentinian workers aged 15 or over, 2001)



Note: Sectors of activity are recorded according to the International Standard Industrial Classification, Rev. 3. The following abbreviations are used AGRIC: Agriculture and fisheries; CONST: Construction; HEALT: Health and social work; HOUSE: Employment in private households; MANUF: Manufacturing; and TRADE: Wholesale and retail trade.

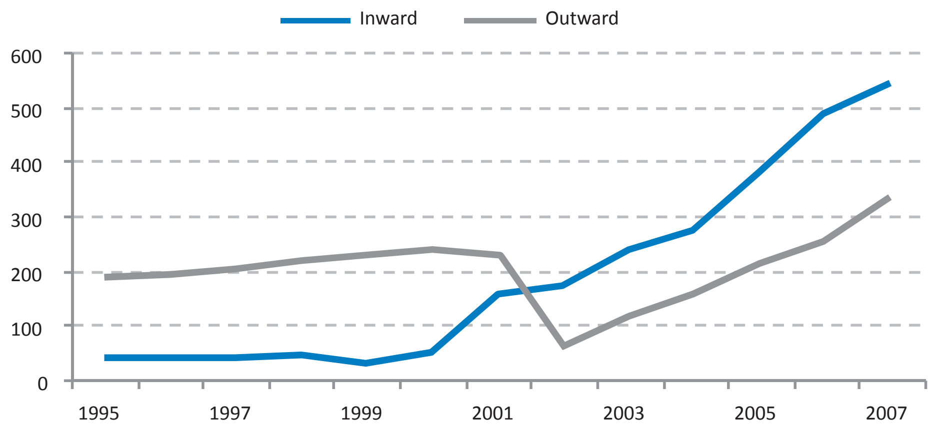
Source: OECD Development Centre calculations, based on the 2001 National Census of Argentina (processed with ECLAC Redatam+SP on-line).

StatLink http://dx.doi.org/10.1787/716544610278

Relationship with the Country of Origin and Integration in the Host Country

Remittance inflows and outflows account for 0.2% and 0.1% of Argentina GDP in 2007, respectively; these magnitudes are low relative to the regional average (6.6% of GDP). Figure 3 shows that remittance inflows surpassed outflows for the first time in 2001. This reflects two factors linked to the deterioration of economic conditions in Argentina during the last decade. First, the rapid increase of Argentinian emigrants to OECD countries (mainly Spain and the United States) driving inward remittances, and second, the general rise in unemployment and the impact this has on the capacity of foreign workers in Argentina to make outward remittances.

Figure 3. Remittance Flows in Argentina
(USD million)



Note: Remittances are measured using the estimates of workers' remittances in the balance-of-payments current transfers account.

Source: IMF, Balance-of-Payments database.

StatLink http://dx.doi.org/10.1787/716653001523

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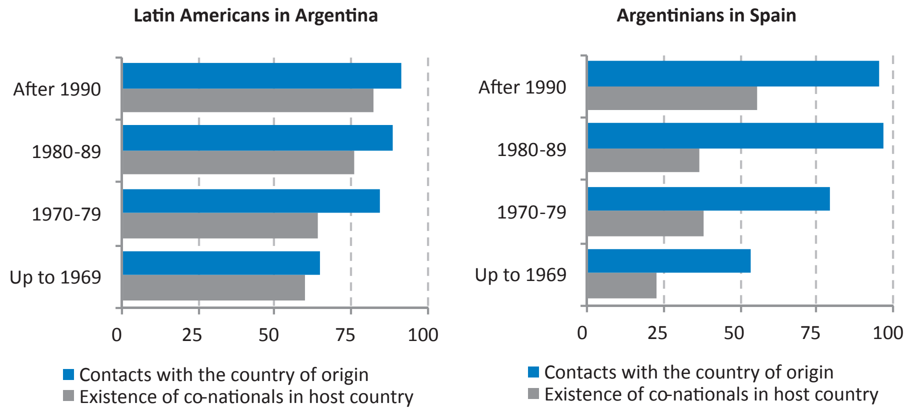
Diaspora communities often influence the decision to migrate, and the choice of destination. This is confirmed for Argentinian emigrants in Spain and Latin American immigrants in Argentina. Migration surveys in Argentina and Spain show that 67% and 51% of immigrants, respectively, say that their decision was influenced by a co-national who had already migrated.

Figure 4. Existence of Links in the Host and Origin Country by Year of Arrival (Percentage)



Source: Indec Argentina, Complementary Survey on International Migration and INE Spain, National Survey of Immigrants.

StatLink http://dx.doi.org/10.1787/716700653631

Another interesting aspect of migrants' life is the relationship they maintain with their country of origin. Migration surveys highlight the high degree of contact that immigrants maintain with their relatives and/or friends. In Argentina and Spain, respectively, 80% and 93% of immigrants keep these links alive, percentages which are indirectly related to the length of stay in the host country.

In order to benefit from the strong networks that exist with migrants abroad, the Argentinian government established the programme Provincia 25. This seeks to ensure the exercise of political rights of Argentinians abroad, promote their integration and strengthen the links between them and the Argentinian state.

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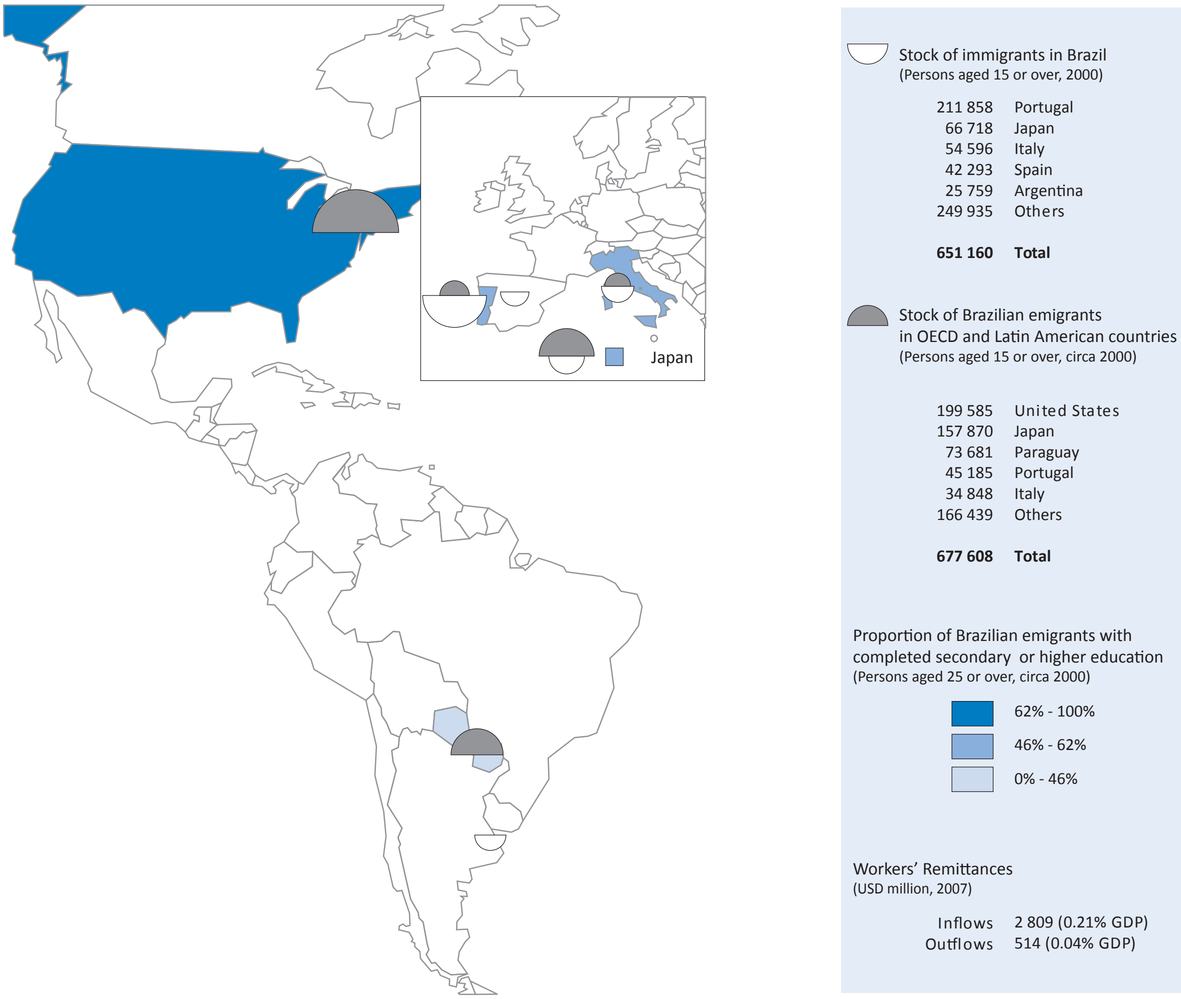
Brazil

At various moments in history, Brazil has welcomed different waves of immigrants. Nevertheless, over recent decades Brazilians from all walks of life have started to emigrate to other countries in search of economic opportunities.

Figure 1. Stock of Migrants and Level of Education of Brazilian Emigrants to OECD and Latin American Countries



Note: This Figure reports the stock of migrants recorded in national censuses and workers' remittances in balance-of-payments data. It will therefore not reflect unrecorded formal or informal flows, which may be material.

Source: For details on definitions and sources, please refer to the Statistical Annex.

Extensive emigration of Brazilians is a relatively recent phenomenon. Emigration to the United States, Japan, and Portugal started in the second half of the 1980s and is still rising.

The Brazilian population has been influenced by distinct waves of immigrants, from European countries particularly Portugal, Italy and Spain, as well as from Japan and its Latin American neighbours.

There is a high degree of variation in educational attainment among Brazilian emigrants. Educational levels of Brazilians now in Paraguay are typically low, they are medium in European countries and Japan, and high among those in the United States.

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Migration History and Policy Developments

Historically Brazil has been a country of destination, influenced by successive waves of immigrants. Some early initiatives as Decree No. 80 (1824) and governmental programmes providing grants for the travel costs of immigrants promoted the growth of communities of European migrants. The abolition of slavery in 1888 led the economy to experience a labour shortage, particularly felt in the coffee plantations. The legal response was Decree No. 528 (1890) which regulated the entrance of immigrants to Brazil, favouring European flows. Brazil's main countries of origin at the end of the 19th century were Portugal, Italy, Spain and Germany.

In the early years of the 20th century immigration continued to be intense, and Japanese migration started. However, the 1929 economic crisis was sharply felt, particularly, in the Brazilian coffee industry and the consequent unemployment led to the introduction of tighter restrictions on immigration. Decree No. 19 482 (1930) suspended all immigration for one year and the Quotas Law established in the Constitution of 1934 and reinforced in 1937 limited annual immigration from any individual country to 2% of the average level over the previous 50 years. The period extending from the end of World War II to the end of the 1970s saw significant economic growth. Immigration policies again became more flexible, but still privileged European inflows (regulated by Decree No. 7 967 of 1945). At the same time, under the government of Getulio Vargas (1930-45 and 1951-54), migrants were encouraged to assimilate into Brazilian culture with the objective of building a single Brazilian identity.

At present, Brazil is an attractive destination for Latin Americans from various socio-economic and educational backgrounds, particularly following the creation of Mercosur in 1991. Immigration in Brazil is currently regulated by Law No. 6 815 (1980) and Decree No. 86 715 (1981), which establish the National Immigration Council as the agency responsible for implementing migration policy and issuing visas and work permits. More recent measures have prioritised entry permits for those who have attended at least secondary education.

The last three decades have seen Brazil move from being a country of destination to one of origin. The economic crises in the 1980s and 1990s were factors in this. The most recent census counted more than 670 000 Brazilians living abroad, but official figures from the Ministry of Foreign Affairs estimate the total number at more than 2 million in 2008. Their main destinations are the United States, Japan and Paraguay, and to a lesser extent the countries of the European Union. In response the Brazilian government has taken some steps towards strengthening its links with communities abroad. The network *Brasileiros no Mundo* aims to improve the conditions of Brazilians abroad through a dialogue with the government in Brazil.

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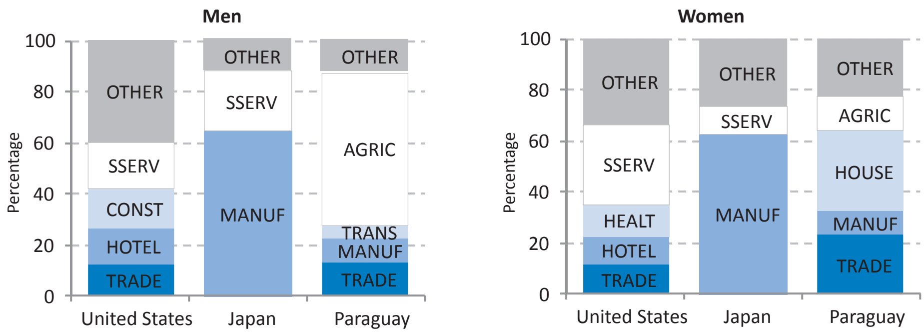
Labour Market

Brazilian emigration flows are best analysed as a series of specific subsystems, according to the country of destination and the socio-historical context.

Figure 2 shows the occupational profile of employed Brazilians in three main destinations: United States, Japan and Paraguay. There are clear differences between the three. While the bulk of immigrants in Japan and Paraguay are concentrated in few activities, Brazilians in the United States cover a broader spectrum of sectors.

Figure 2. Distribution of Brazilian Emigrants by Activity in Three Main Destinations
(Circa 2000, percentage of total Brazilian emigrants in employment)



Note: Sectors of activity are recorded according to the International Standard Industrial Classification, Rev. 3. The following abbreviations are used AGRIC: Agriculture and fisheries; CONST: Construction; HEALT: Health and social work; HOTEL: Hotels and restaurants; HOUSE: Employment in private households; MANUF: Manufacturing; SSERV: Other community, social and personal service activities; and TRADE: Wholesale and retail trade. TRANS: Transport, storage and communication.

Source: OECD Development Centre calculations, based on OECD (2008), Database on Immigrants in OECD countries for the United States, the Japanese Statistics Bureau for Japan and the 2000 round of national censuses for Latin America (processed with ECLAC Redatam+SP on-line).

StatLink http://dx.doi.org/10.1787/716740672601

Brazilian migration to Paraguay started in the 1960s. These immigrants (known as Brasiguayos) are normally landowners in the border regions of Paraguay. Among males, agriculture is the main activity, while domestic service and trade are particularly relevant for women.

The emigration of Brazilians to Japan is closely linked to the earlier flows in the opposite direction and comprises mostly descendants of those former immigrants. Brazilian workers in Japan (known as Dekasseguis) enter the country legally through Japanese employment agencies based in Brazil or by using their personal networks (CGEE, 2008). The majority are employed in manufacturing: 64% across both sexes, of which 88% are production workers.

In contrast to Brazilians in Paraguay and Japan, migrants in the United States show a mixed profile. The presence of Brazilians is notable in sectors such as personal services, health, hotels and restaurants, construction and trade. The higher educational level observed for Brazilians in the United States compared to other destinations is consistent with their increasing presence in professional occupations (nearly 29% of Brazilians in the country). More than 81% of emigrants to the United States have completed secondary or higher education, and 39% have university or equivalent technical studies.

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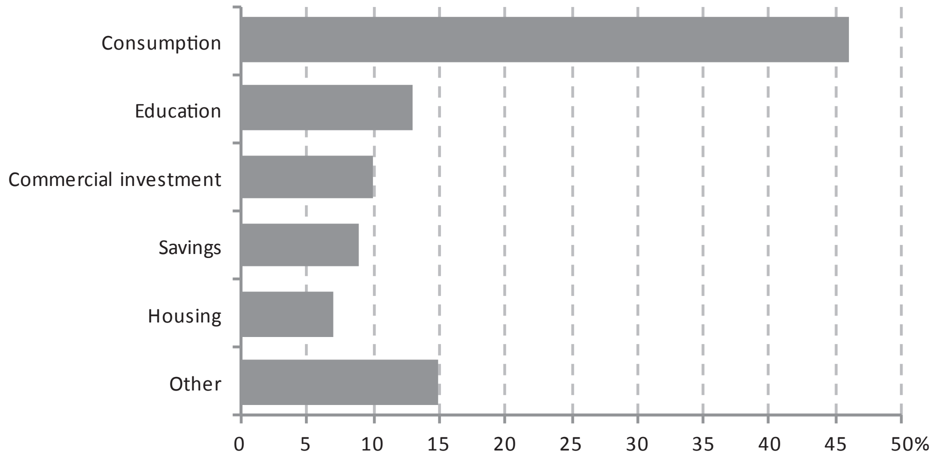
Relationship with the Country of Origin and Integration in the Host Country

Although remittances represent only 0.21% of GDP, Brazil is an important remittance-receiving country in absolute terms. Remittance inflows in 2007 surpassed USD 2.8 billion. Remittance outflows were less than 0.04% of GDP.

Figure 3. Principal Use of Remittances in Brazil, 2004



Source: IDB/MIF (2004*a*).

StatLink http://dx.doi.org/10.1787/716806527852

In 2004, the IDB conducted a survey to study the profile of the recipients of remittances in Brazil (IDB/MIF, 2004*a*). It concluded that the recipients of remittances in Brazil were predominantly families belonging to low and medium income groups and with relatively low educational level (35 and 44% of respondents had attained only primary or secondary education, respectively).

The survey also indicated how migrants' families use the remittances they receive (Figure 3). Nearly half, 46%, of resources were spent on consumption. Lesser but also significant amounts were destined to education (13%) and commercial investment (10%).

A joint initiative of SEBRAE (the Brazilian Micro and Small Business Support Service), the IDB and ABD (the Brazilian Dekassegui Association) promotes the investment of remittances in productive activities. The Dekassegui Entrepreneur Programme seeks to develop the entrepreneurial capacity of Brazilians in Japan (or returning from Japan), by providing educational and technical support for business start-ups.

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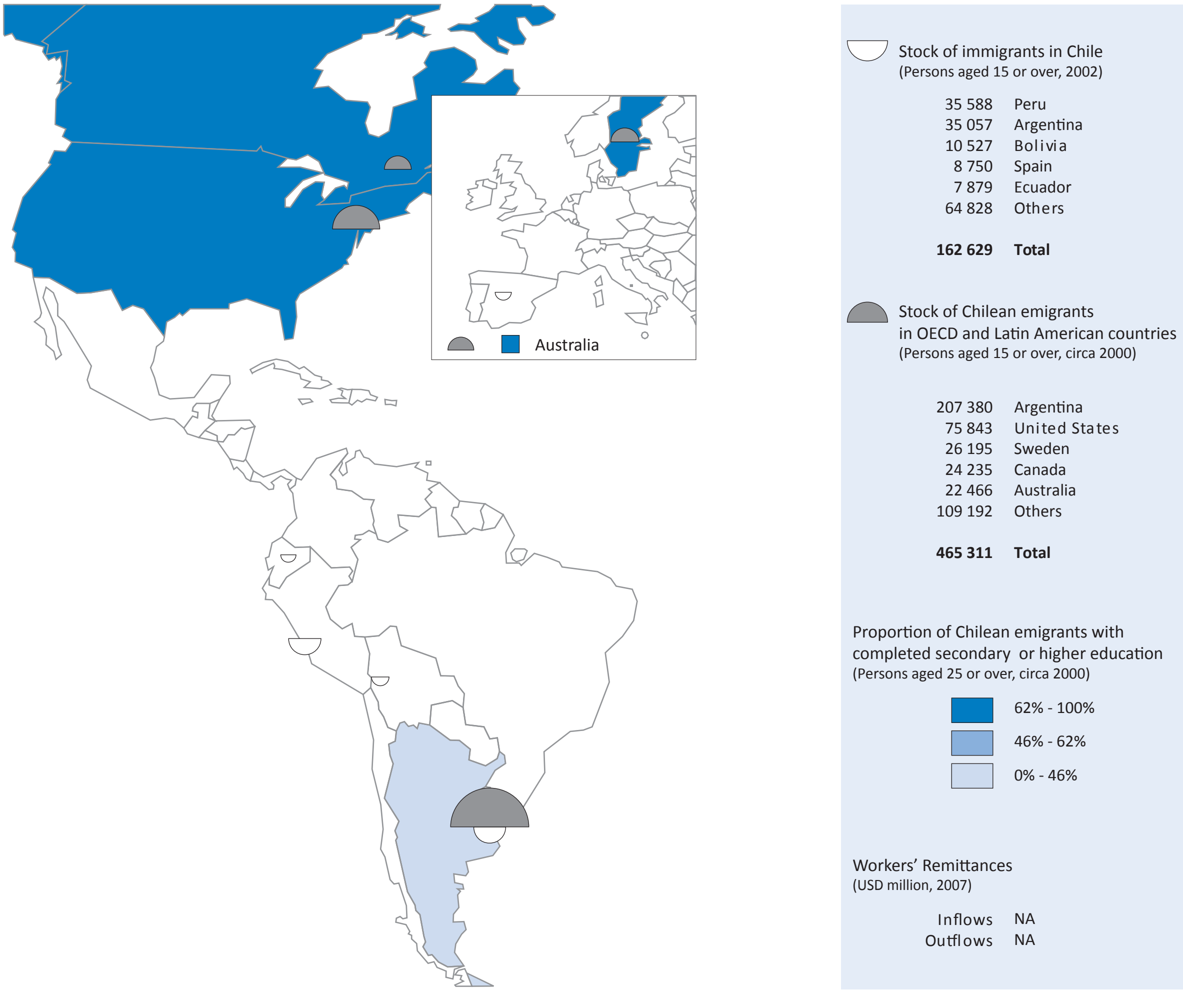
Chile

Increasing political and economic stability, in conjunction with the deteriorating economic and political situation of other countries in the region, has made Chile an attractive destination for Latin American migrants.

Figure 1. Stock of Migrants and Level of Education of Chilean Emigrants to OECD and Latin American Countries



Note: This figure reports the stock of migrants recorded in national censuses and workers' remittances in balance-of-payments data. It will therefore not reflect unrecorded formal or informal flows, which may be material.

Source: For details on definitions and sources, please refer to the Statistical Annex.

Throughout Chile's history immigration has been low relative to other Latin American nations. Nevertheless, 2002 saw Chile register the greatest inflow of immigrants in its history, with over 160 000 arriving in the course of the year. The most notable recent change is the increasing presence of Latin American immigrants, especially from Peru and Argentina.

Although the immigration panorama has changed since the late 1990s, Chile is a net emigration country. The stock of Chilean emigrants represents 4.1% of the total population, with Argentina as the main destination country.

The percentage of emigrants with primary education or less is 47%. This figure is influenced by the relatively low levels of education of emigrants to Argentina. In contrast, more than two-thirds of Chileans in the United States, Canada and Sweden have completed at least secondary education.

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Migration History and Policy Developments

For most of Chile's history immigration flows have not been significant. Over the 138-year period 1865-2002 on average only 2% of the total population were foreign born (Martínez, 2003). What immigration there was came from groups affected by Europe's economic plight at the end of the 19th century or by the two World Wars. European migration was directly encouraged by the state in order to populate and develop the local economies in uninhabited southern areas (Selective Immigration Law of 1845).

The increasing economic strength of Chile in recent years, in conjunction with the deteriorating economic and political situation in other countries in Latin America, has made the country an attractive alternative for regional migrants. According to the 2002 census, the largest regional group of immigrants are from Latin American countries, mainly Peru and Argentina. These new migration flows are recent and have a clear economic rationale. More than half of these immigrants arrived after 1996 and nearly 72% cite economic and labour difficulties in their countries of origin as a reason behind their decision to migrate (Chilean Ministry of the Interior, 2008).

Although immigration remains relatively small (the latest census found 1.4% of the total population were foreign born), its increasing profile is prompting political interest in the country's migration policy. The governments of the Concertación (1990 to present) have been active in formulating migration initiatives, including reforms to the framework Foreigners Law (Decree Law No. 1.094 of 1975), amnesties for irregular migrants, administrative modernisation of the Immigration Department and efforts to develop a regulatory framework that encourages integration of immigrants into the host society.

Another element of Chile's migration policy is the maintenance of relations with the more than 460 000 Chilean-born living abroad. (The government, in fact, recognises a total of close to 860 000 Chileans abroad, a number which, following the constitutional reform of 2005, includes the children of Chileans born abroad). Following the restoration of democracy, the early 1990s saw policies designed to promote the return of Chileans who had left the country for political reasons. In contrast, the main reason given by more recent migrants is to study (52%) (Chilean Ministry of Foreign Affairs, 2005). In 2005 the Ministry of Foreign Affairs compiled a register of Chileans living abroad, data from which are used to develop public policies oriented to overseas Chileans.

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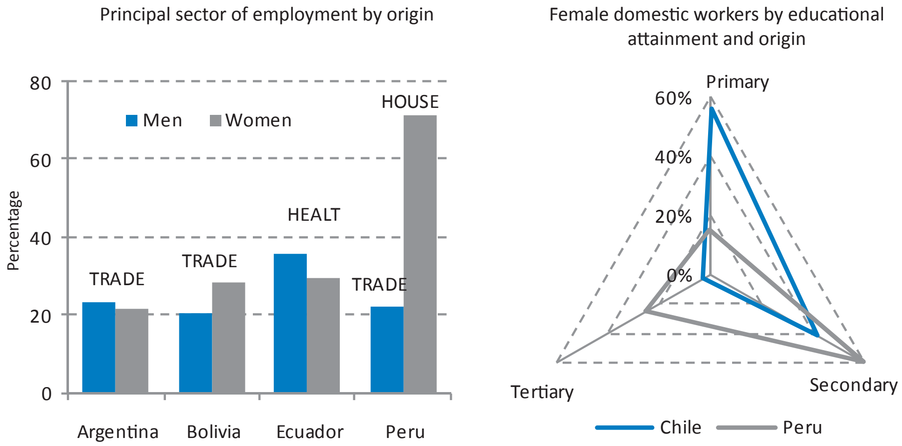
Labour Market

The issue of work permits increased exponentially over 1996-2007, overwhelmingly to workers from neighbouring Latin American countries who have a job offer in Chile. Work permits can be job specific, with a duration tied to the labour contract, or open, valid for one year or two and potentially leading to a permanent residence visa.

Figure 2. Principal Sector of Activity of Migrants and Educational Attainment by Origin
(Workers aged 15 or over, 2002)



Note: Sectors of activity are recorded according to the International Standard Industrial Classification, Rev. 3. The following abbreviations are used HEALT: Health and social work; HOUSE: Employment in private households; and TRADE: Wholesale and retail trade.

Source: OECD Development Centre calculations, based on the 2002 National Census of Chile (processed with ECLAC Redatam+SP on-line).

StatLink http://dx.doi.org/10.1787/716837331816

The lefthand panel of Figure 2, which shows the principal sector of employment in Chile of migrants by country of origin, reveals a clear pattern. Peruvian migrants are heavily concentrated in domestic service (71.5% of women) and trade (22.2% of men), while Ecuadorians are found in health and social work (32.6%). This degree of concentration is not found among Argentinians and Bolivians, for whom the principal occupation is trade (at 22.4 and 23.8%, respectively).

The righthand panel of Figure 2 compares the level of education of Peruvian and Chilean domestic workers. The Peruvian workers are generally more qualified than their native counterparts. This may be part of their attraction to employers.

Continuing integration of these immigrants may be one of Chile’s chief migration challenges. Domestic service, at least, does seem to be a good source of employment and opportunity. A study on Immigration, Gender Equity and Public Safety conducted by the Chilean Ministry of the Interior found that the incomes of immigrant domestic workers were sufficient to cover basic needs (91%), allow for savings (52%) and the sending of remittances (70%).

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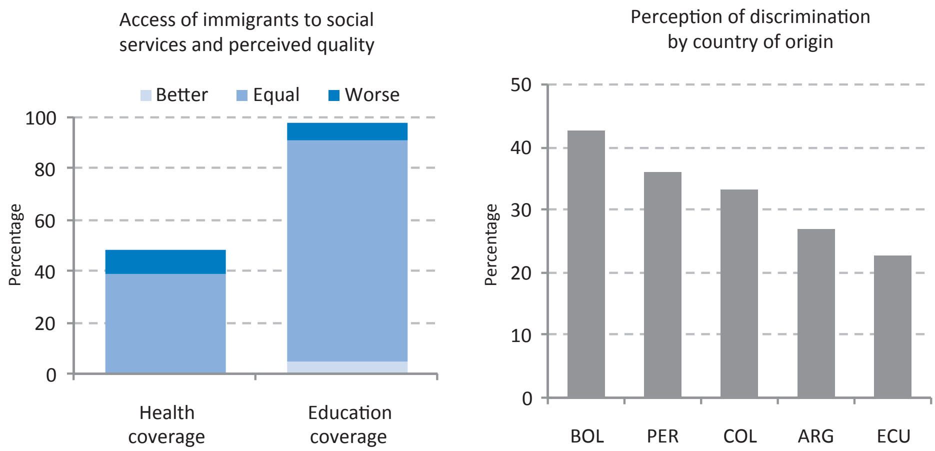
Relationship with the Country of Origin and Integration in the Host Country

A central element of Chile's current National Immigration Policy is promoting the successful integration of immigrants into Chilean society. Chile has held amnesties for irregular migrants, opening the way to their inclusion in the formal economy and in particular its health and pension systems. Existing labour legislation extends to migrants, and migrants' children have access to education regardless of immigration status of their parents.

Figure 3. Integration of Immigrants in Chile, 2008



Source: Chilean Ministry of the Interior (2008).

StatLink http://dx.doi.org/10.1787/716857433304

The Immigration, Gender Equity and Public Safety study demonstrates significant success in access to education and health. The lefthand panel of Figure 3 shows that almost all respondents reporting dependent children of school age declared that they attended school regularly. Additionally, 49% of migrants indicated that they were covered by health insurance. Moreover, they had positive perceptions of quality compared to social services received in their home country.

Challenges nonetheless remain in the areas of housing and perceptions of discrimination. The immigrant population expresses difficulties accessing housing (61%), particularly in the case of irregular immigrants. Overall, one in three immigrants in Chile felt they had experienced discrimination while in the country. Peruvians and Bolivians reported higher rates of discrimination than the average.

Emigrant Chileans maintain strong links with their country of origin. A survey of migrants by the Chilean Ministry of Foreign Affairs highlighted their high degree of contact with family (90%) and the frequency of return visits (74% made at least occasional return trips). The study found that 39% of respondents said they intended to return to Chile to resettle in the foreseeable future. This is borne out by the 2002 national census which recorded the return – mainly from Argentina and Europe – of almost 39 000 Chileans formerly living abroad (resident abroad in 1997 and now resident in Chile, aged 15 years or over).

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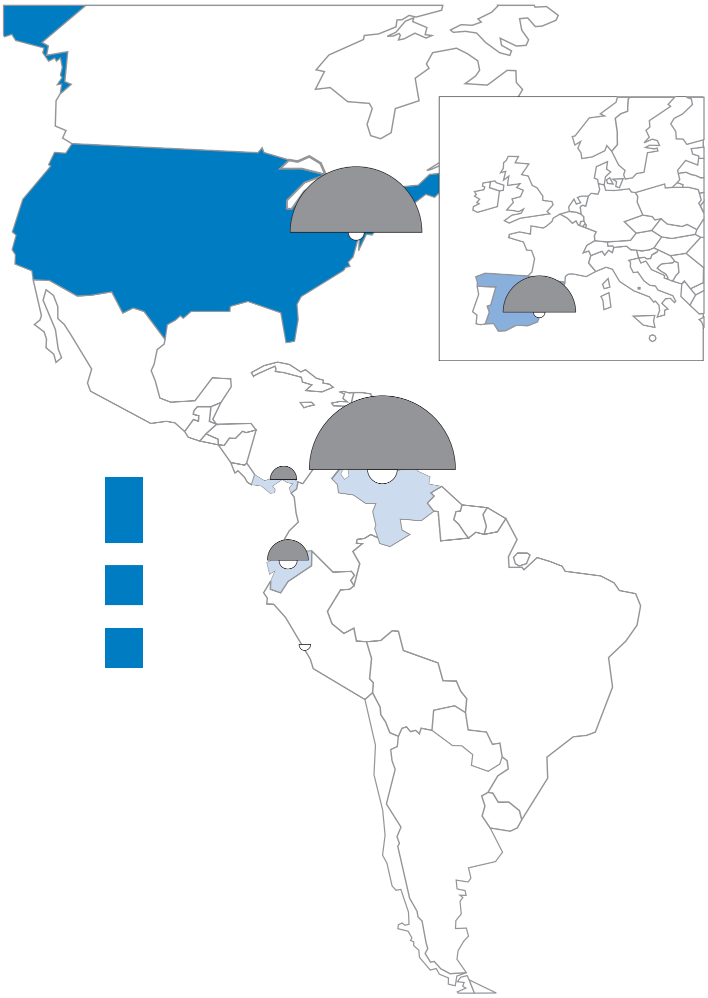
Colombia

Migratory outflows have increased substantially in recent years in Colombia. Economic and political factors have fuelled both voluntary and forced migration.

Figure 1. Stock of Migrants and Level of Education of Colombian Emigrants to OECD and Latin American Countries



Stock of immigrants in Colombia
(Persons aged 15 or over, 2001)

23 939	Venezuela
9 332	Ecuador
6 785	United States
3 687	Peru
3 565	Spain
29 120	Others
76 428	**Total**

Stock of Colombian emigrants in OECD and Latin American countries
(Persons aged 15 or over, circa 2000)

581 060	Venezuela
472 027	United States
143 500	Spain
45 346	Ecuador
19 118	Panama
99 935	Others
1 360 986	**Total**

Proportion of Colombian emigrants with completed secondary or higher education
(Persons aged 25 or over, circa 2000)

62% - 100%
46% - 62%
0% - 46%

Workers' Remittances
(USD million, 2007)

Inflows	4 493 (2.2% GDP)
Outflows	66 (0.03% GDP)

Note: This Figure reports the stock of migrants recorded in national censuses and workers' remittances in balance-of-payments data. It will therefore not reflect unrecorded formal or informal flows, which may be material.

Source: For details on definitions and sources, please refer to the Statistical Annex.

Colombian society has experienced large-scale emigration flows over recent decades. Some 4.7% of Colombians now live abroad. Venezuela and the United States are the main countries of destination, followed by Spain, Ecuador and Panama.

Past and present immigration levels in Colombia are relatively low in comparison to other Latin American countries and immigrants make up only 0.3% of the country's population.

Colombian migrants in the United States have a higher level of education than is observed for other destinations. Some 72% of immigrants in the United States have completed secondary or higher education, while for those living in Venezuela and Spain the proportion is 22 and 47%, respectively.

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Migration History and Policy Developments

Throughout most of Colombia's history immigration and emigration flows have been low compared to other Latin American countries. Nevertheless, economic factors and internal conflicts have driven extensive emigration of Colombians during recent decades. According to the latest round of the national census around 4.7% of the population live abroad (over 1.3 million people), most of whom are in Venezuela and the United States. Figures from the national statistics office put the figure higher, estimating that as a many as 3 million Colombians are resident in another country.

This is mostly but not completely the result of emigration in recent years. The first significant wave of Colombian emigration took place from the late 1960s. Colombians emigrated principally to Venezuela and the United States, taking advantage of the oil boom in the neighbouring country or the opportunities provided by the US Immigration Act of 1965. Later, from the mid-1980s, the economic slowdown and rise in unemployment in Colombia encouraged outgoing migratory flows. In this period, migration patterns reflected the labour programmes for low-skilled migrants in the United Kingdom and the permanent permits available through the US Immigration Reform and Control Act of 1986.

By the late 1990s, macroeconomic difficulties had undermined popular confidence in Colombia's prospects. In 1999 Colombia's economy shrank by 4.2% in its first economic recession in more than 50 years. Simultaneously the internal security situation deteriorated as guerrilla and paramilitary groups strengthened. Civilians were increasingly caught up in the conflict, forcing much of the population to flee from rural homes to urban areas or to leave the country.

Despite the significant improvement in the macroeconomic scenario, the progressive reduction in crime and violence and more restrictive immigration policies in North America and Europe, Colombian emigration has not decreased during the last decade. It is estimated that some 46 000 Colombians emigrated to OECD countries every year between 1996 and 2006 (OECD, 2008). As one response the Colombian government has engaged in active policies to maintain links with the communities abroad. One example is ColombiaNosUne, an initiative aimed at identifying and providing assistance to Colombian emigrants and supporting entrepreneurial networks.

Immigration has been correspondingly low over this period, and has never in the modern period been a major phenomenon in Colombia. Government inducements aimed at encouraging European immigration were provided from the early 20th century onwards, but they remained largely unimplemented partly as a result of Colombia's internal conflicts, such as the undeclared civil war known as La Violencia (1948-60).

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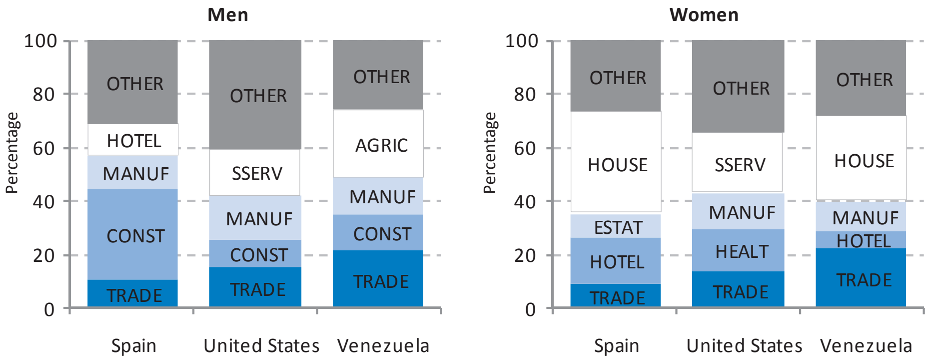
Labour Market

Labour-market participation rates of Colombians abroad tend to be higher than those of natives, providing evidence of their economic motivation to migrate.

Figure 2. Distribution of Colombian Emigrants by Activity in Three Main Destinations (circa 2000, percentage of total workers)



Note: Sectors of activity are recorded according to the International Standard Industrial Classification, Rev. 3. The following abbreviations are used AGRIC: Agriculture and fisheries; ESTAT: Real estate, renting and business activities; CONST: Construction; HEALT: Health and social work; HOTEL: Hotels and restaurants; HOUSE: Employment in private households; MANUF: Manufacturing; SSERV: Other community, social and personal service activities; and TRADE: Wholesale and retail trade.

Source: OECD Development Centre calculations, based on OECD (2008), Database on Immigrants in OECD Countries and the 2000 round of national censuses for Latin America (processed with ECLAC Redatam+SP on-line).

StatLink http://dx.doi.org/10.1787/717046631764

Figure 2 shows the occupational profile of employed Colombians in three main destination countries: Spain, the United States and Venezuela. While the bulk of immigrants in Spain and Venezuela are concentrated in few low-skilled activities, Colombians in the United States are employed in a broader spectrum of sectors.

Among males, construction and agriculture are respectively the main activities for Colombians in Spain and Venezuela and in these countries domestic service is the main source of employment for Colombian women. This contrasts with the experience of migrants in the United States, where Colombians are present in more skilled sectors such as personal services, health, manufacture and trade.

These differences in occupational profile are consistent with the levels of educational attainment in these groups. One of the features of Colombian emigration to the United States is its high level of education. More than 72% of migrants to this country have completed secondary or higher education, and of these 28% have completed university or technical studies. By comparison the corresponding figures in Spain were 47 and 19%.

In order to improve the labour insertion of emigrants, the Colombian government has implemented technical training programmes for its citizens abroad. One example is that for Colombians resident in Spain, which offers courses jointly certified by the Colombian National Apprenticeship Service (SENA) and the Spanish educational system. Additionally, SENA has concluded several bilateral agreements with local NGOs to support migrants who have temporary work contracts in Spain.

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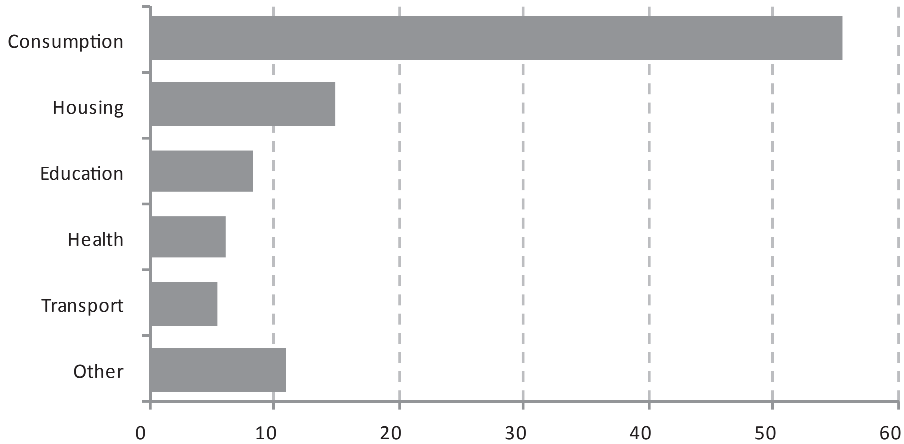
Relationship with the Country of Origin and Integration in the Host Country

Remittance inflows are increasingly important to the Colombian economy. In 2007 remittances represented 2.2% of Colombian GDP, almost three times the proportion in 2000. Remittance outflows, reflecting low levels of immigration, account for less than 0.1% of GDP.

Figure 3. Principal Uses of Remittances in Colombia, 2004
(Percentage of total current expenditures)



Source: DANE, Survey of Households in the Central Western Metropolitan Area (2004).

StatLink http://dx.doi.org/10.1787/717061424241

The 2004 Survey of Households in the Central Western Metropolitan Area (AMCO) indicated that 18% of households received international monetary transfers, of which 56% were in the middle socio-economic groups. Remittances were an important source of income for households in AMCO: they received on average monthly transfers of USD 173, equivalent to 10% of average household income in Colombia.

As shown in Figure 3, the principal use of these resources was to fund consumption (55%), especially of food and basic services. Remittances were also an important source for the acquisition of durable assets. Around 10% of the recipient households put remittances towards house purchase and 40% had invested in housing improvement in the last five years. *Mi casa con remesas*, a joint initiative between the private sector and the IDB, accounts for much of this phenomenon. This initiative facilitates house purchase in Colombia for households that regularly receive international transfers. Additionally, the Colombian Ministry of Foreign Affairs in conjunction with the construction sector organises housing fairs in the principal countries of destination to promote house purchase to Colombians abroad.

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Costa Rica

Costa Rica's political stability and relatively high standard of living have made the country an attractive destination in Central America and given it the highest percentage of immigrants in the region.

Figure 1. Stock of Migrants and Level of Education of Costa Rican Emigrants to OECD and Latin American Countries

Stock of immigrants in Costa Rica
(Persons aged 15 or over, 2000)

184 887	Nicaragua
8 386	Panama
8 282	El Salvador
6 933	United States
4 959	Colombia
31 882	Others
245 329	**Total**

Stock of Costa Rican emigrants in OECD and Latin American countries
(Persons aged 15 or over, circa 2000)

68 068	United States
3 746	Panama
3 006	Nicaragua
2 160	Canada
1 804	Mexico
8 433	Others
87 217	**Total**

Proportion of Costa Rican emigrants with completed secondary or higher education
(Persons aged 25 or over, circa 2000)

62% - 100%
46% - 62%
0% - 46%

Workers' Remittances
(USD million, 2007)

Inflows	596 (2.3% GDP)
Outflows	258 (1% GDP)

Note: This Figure reports the stock of migrants recorded in national censuses and workers' remittances in balance-of-payments data. It will therefore not reflect unrecorded formal or informal flows, which may be material.

Source: For details on definitions and sources, please refer to the Statistical Annex.

Costa Rica has a complex migration profile, including continuous inward, outward and transitory migratory flows. Inward migration is mainly from Nicaragua and neighbouring countries. The latest national census in Costa Rica (2000) counted over 200 000 immigrants, making up 9.5% of the total population.

Although primarily still a country of destination, since the late 1990s Costa Rica has increasingly experienced emigration notably to the United States. At the time of the census around 87 000 Costa Ricans lived abroad.

Costa Rican emigrants in the United States are in general highly skilled, some 70% of them having completed secondary education or more.

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Migration History and Policy Developments

Immigration flows are not new in the history of Costa Rica. From the late 19th century the development of banana plantations became a major factor drawing in foreign labour, mainly from Nicaragua and Jamaica. From 1892 to 1973 the foreign-born proportion of the population remained between 2 and 6% (Flacso, 2002).

Inward flows from Central America dramatically increased between 1984 and 2000. Costa Rica's political stability and relatively high standard of living made the country an attractive destination for migrants from elsewhere in Central America, a region affected by natural disasters, internal conflicts and structural economic imbalances. At the time of the latest national census in 2000 a total of nearly 185 000 Nicaraguans were resident in Costa Rica together with significant numbers from Panama and El Salvador (joined by significant numbers from Colombia).

Over this period Costa Rica has reformed its legal framework for immigration a number of times. In 1986 it introduced a Migration and Aliens Law (Ley No. 7.033 de Migración y Extranjería). This restricted legal immigration, though was followed in 1992, 1994 and 1999 (in response to Hurricane Mitch) by amnesties, implemented by decree, to regularise the position of undocumented migrants.

Household surveys since 2000 have shown immigration flows tending to stabilise and the proportion of migrants in the population stable or falling (though the relative weight of Colombians is growing). This reflects both lower demand as a result of the improving political and economic situation elsewhere in Central America and Costa Rica's tighter immigration polices since the introduction in 2005 of a new legal framework (Ley No. 8.487 de Migración y Extranjería). One of the most controversial features of this is the strength of measures to control undocumented immigration (including rejections and deportations) and the establishment of criminal penalties for unauthorised immigrants.

In 2007, the Executive presented a draft to reform some of these more controversial measures. The proposed new law (draft 16.594), which was approved by the legislature in August 2009, has a more open model of migration. It incorporates a human-rights perspective, creates new avenues for the regularisation of undocumented immigrants and promotes the integration of migrants through access to social services.

Since the late 1990s, Costa Rica has seen material emigration, notably to the United States. The 2000 census estimated that around 87 000 Costa Ricans lived abroad and during 2000-08 over 2 000 Costa Ricans entered the United States every year. The bulk of these flows are highly skilled people and are economically motivated. According to a survey by the Central Bank of Costa Rica (2008), 52% of Costa Rican migrants said they were motivated by employment opportunities or mentioned economic instability as a reason to migrate.

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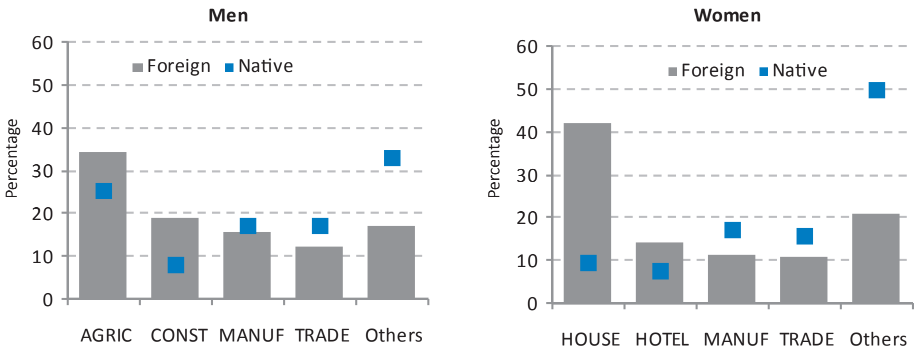
Labour Market

Many Nicaraguans migrate to Costa Rica in search of better conditions. A survey conducted by the Central Bank of Costa Rica (2008) found that migrants gave as their main reason lack of employment (39%) or political and economic instability (20%) in their country of origin.

Figure 2. Sector of Activity by Origin
(Nicaraguan and Costa Rican workers aged 15 or over, 2000)



Note: Sectors of activity are recorded according to the International Standard Industrial Classification, Rev. 3. The following abbreviations are used AGRIC: Agriculture and fisheries; CONST: Construction; HOTEL: Hotels and restaurants; HOUSE: Employment in private households; MANUF: Manufacturing; and TRADE: Wholesale and retail trade.

Source: OECD Development Centre calculations, based on the 2000 Costa Rican National Census (processed with ECLAC Redatam+SP on-line).

StatLink http://dx.doi.org/10.1787/717074441620

Figure 2 reviews the dominant economic sectors of employment for Nicaraguan and Costa Rican workers. It is noteworthy that the Nicaraguan workforce is concentrated in unskilled occupations particularly among women. Two activities (domestic service, and hotels and restaurants) account for about 56% of the female workforce. In the case of men, agriculture and construction constitute more than 54% of the workforce. This sectoral composition and the lower levels of educational attainment among Nicaraguan migrants compared with the native-born population may go some way to explaining the income differences observed between Nicaraguan and Costa Rican workers in some studies (Flacso, 2002; Gindling, 2009).

Further integration of these immigrants may be one of the challenges to address. Between them the governments of Costa Rica and Nicaragua have joined efforts to develop mechanisms to protect immigrant workers, and signed bilateral agreements in 1995 and 2002 regarding documentation and labour guarantees for Nicaraguan workers recruited by companies in Costa Rica.

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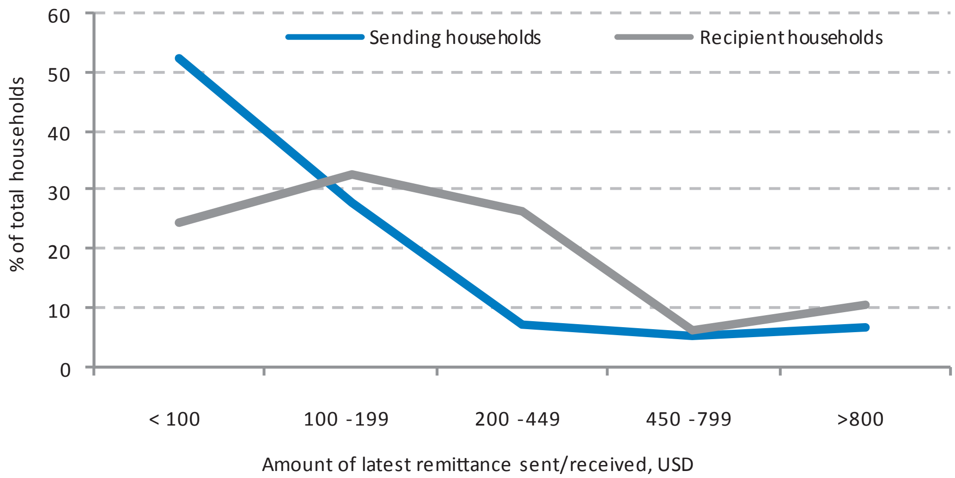
Relationship with the Country of Origin and Integration in the Host Country

Costa Rica's inward and outward migration are both reflected in its remittance flows. In 2007, inward remittances accounted for 2.3% of GDP and outward remittances 1%.

Figure 3. Distribution of Remittances in Costa Rica by Household Category
(2007)



Note: Since the basic data are in the form of frequency tables, an interpolation method has been employed.

Source: Multiple Purpose Household Survey (2007).

StatLink http://dx.doi.org/10.1787/717086744557

According to estimates from the 2007 Multiple Purpose Household Survey (EHPM), 22% of all immigrant households in Costa Rica sent remittances to their home country while 35% of Costa Rican households with a member abroad received international transfers.

The data also highlights the privileged economic situation of Costa Ricans abroad compared to immigrants in Costa Rica. While remittances sent by immigrant households in Costa Rica average USD 176 per month, the average transfers from abroad received by a Costa Rican family average USD 311 per month. Moreover, as Figure 3 indicates, the distribution of remittances for sending households is skewed to lower amounts: more than 50% of sending households in Costa Rica sent less than USD 100 to their home country, while amongst recipient households only 24% received USD 100 or less.

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Dominican Republic

Historically, the Dominican Republic has always been a destination for Haitian migrants. In the last three decades a growing number of Dominicans have migrated abroad, primarily to the United States.

Figure 1. Stock of Migrants and Level of Education of Dominican Emigrants to OECD and Latin American Countries

Stock of immigrants in Dominican Republic
(Persons aged 15 or over, 2002)

56 583	Haiti
3 091	Venezuela
2 227	Spain
1 973	Cuba
1 920	Puerto Rico
16 528	Others
82 322	**Total**

Stock of Dominican emigrants in OECD and Latin American countries
(Persons aged 15 or over, circa 2000)

633 267	United States
36 800	Spain
13 060	Venezuela
12 892	Italy
5 109	Panama
15 458	Others
716 586	**Total**

Proportion of Dominican emigrants with completed secondary or higher education
(Persons aged 25 or over, circa 2000)

- 62% - 100%
- 46% - 62%
- 0% - 46%

Workers' Remittances
(USD million, 2008)

Inflows	3 033 (8.3% GDP)
Outflows	NA

Note: This figure reports the stock of migrants recorded in national censuses and workers' remittances in balance-of-payments data. It will therefore not reflect unrecorded formal or informal flows, which may be material.

Source: For details on definitions and sources, please refer to the Statistical Annex.

- **The Dominican Republic** is a net emigration country, with approximately 13% of its population currently living abroad. Since the late 1980s Dominicans began to emigrate in larger numbers, principally to the United States and European countries such as Spain and Italy.
- **Immigration** from Haiti has been significant historically. Workers from Haiti were initially attracted by labour shortages and relatively higher wages in sugar plantations.
- **The Dominican** population in the United States shows a medium educational profile. Around 50% of Dominican immigrants in the United States have completed secondary education.

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Migration History and Policy Developments

Historically, the Dominican Republic has been a country of destination. Starting in the second half of the 19th century, cane-cutters were recruited to work in Dominican sugar plantations, mainly from English-speaking Caribbean countries and Haiti. Labour immigration from Haiti was actively encouraged during the United States' occupation of the Dominican Republic (1916-24), as a consequence of the expansion in the sugar industry under American rule.

Regulation of immigration flows from Haiti followed increasing tension surrounding the definition of the border between the two countries beginning in 1937. Due to labour shortages and growing interest of the government in the sugar plantations, a series of bilateral agreements (*convenios*) were signed between Haiti and the Dominican Republic, allowing the entrance of Haitians for specified periods. Gradually, permanent Haitian settlements around sugar plantations (known as *bateyes*) were also established.

During the 1960s, political and economic turmoil led to an increase in Dominican emigration, notably towards the United States. During this period, Dominican migrants moved through a variety of channels, benefiting from the easing of visas and immigration restrictions in the US Immigration Act of 1965 and support for asylum seekers and refugees. A large portion of this migration was also unauthorised.

The last three decades have seen the Dominican Republic move decisively to being a country of origin. Dominican emigration accelerated from 1980 in response to economic crises. The 1980s also witnessed a reduction in the importance of sugar production in the Dominican economy, encouraging many Haitian immigrants to move to other sectors including construction, trade, manufacture and domestic service.

Despite the sustained growth and political stability exhibited by the Dominican economy during the last decade, emigration has not decreased. In the latest census round, it was estimated that 716 586 Dominicans lived abroad (13% of the population), of whom around 633 000 were in the United States. A more recent estimate (2008) in the American Community Survey put this figure at more than 1.3 million (including Dominicans born in the United States). In addition to the continental United States, Dominicans have also established sizeable communities in Spain, Italy and Puerto Rico.

The Dominican government has implemented initiatives to strengthen its links with the diaspora, among them the Constitutional amendment recognising dual nationality (1994), the extension of the right to vote to overseas Dominicans (1997) and the proposed Constitutional draft establishing seats for Senators and Deputies representing Dominicans abroad. Within the country, the precarious conditions faced by Haitians have been also a subject of increasing political awareness, leading the governments of both countries to sign a declaration against clandestine recruitment and illegal migration in 2000. Moreover, the 2004 General Migration Law (Act No. 285) and the ongoing National Regularisation Plan also focus on the regulation of undocumented immigrants in the country.

Labour Market

Dominican migrants and native-born workers in OECD countries have similar patterns of labour-force participation rates. For instance, 68.1% of Dominicans in the United States are employed or actively seeking work, very close to the corresponding 65.4% figure for US workers.

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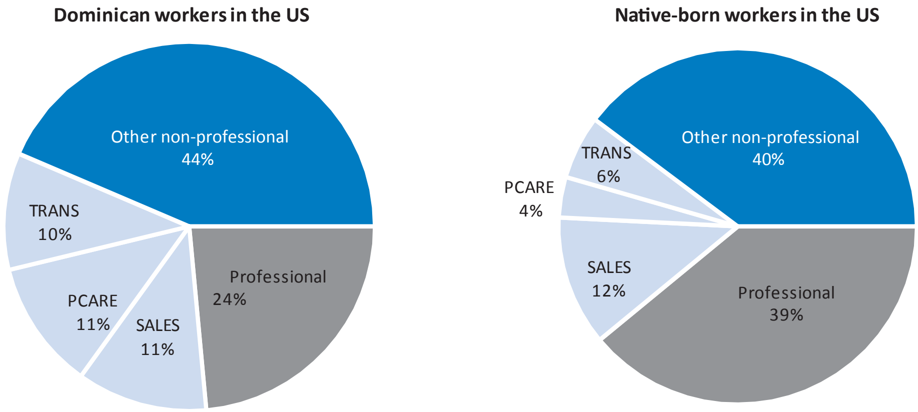
Figure 2. Distribution of Workers by Occupational Categories
(Percentages, 2009)



Note: The professional category comprises professionals and technicians, items from 001 to 395 of the Census Occupation Code (COC). Other abbreviations used are PCARE: Personal care and service; SALES: Sales and TRANS: Transportation and material moving.

Source: OECD Development Centre calculations, based on the US Current Population Survey.

StatLink http://dx.doi.org/10.1787/717114631018

Despite this evidence of effective labour market integration, there are still challenges to be met. Dominican immigrants show a higher concentration in low-skilled positions than their native-born counterparts. Figure 2 shows the distribution of Dominicans and native-born workers in the United States according to occupational categories. More than 76% of Dominicans are in non-professional positions compared with only 61% for native-born workers. In particular, immigrants show a higher concentration in sales, personal care and transportation occupations.

This labour market composition and the lower levels of educational attainment among Dominican migrants compared with the native-born population may help to explain the income differences observed between Dominican and US workers in some studies (Hernández and Rivera-Batiz, 2003).

Despite the fact that most Dominican immigrants work in low-skilled positions, an increasing number of high-skilled migrants can be found in the United States. The 2008 American Community Survey estimates that there are around 90 000 Dominicans with bachelor or professional degrees.

Relationship with the Country of Origin and Integration in the Host Country

From the 1990s onwards the Dominican Republic experienced significant growth in remittance inflows, reflecting the growth of Dominican emigration. Remittances increased from USD 0.8 billion in 1995 to USD 3.1 billion in 2008 (representing 5.0 and 6.8% of Dominican GDP, respectively). However, since 2007 the growth in remittance flows has been gradually slowing, and even declined in the first quarter of 2009.

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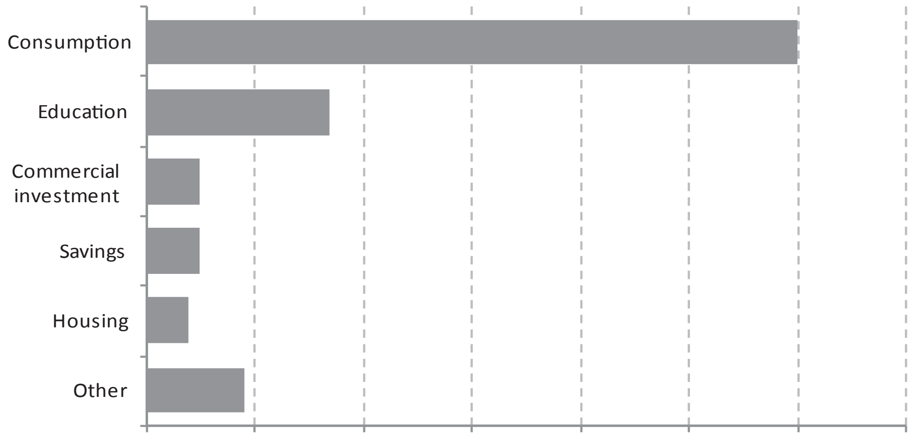
Figure 3. Principal Use of Remittances in the Dominican Republic, 2004

(Percentage of total current expenditures)



Source: IDB/MIF (2004*b*).

StatLink http://dx.doi.org/10.1787/717115440606

The 2007 National Survey of Households (ENHOGAR) indicated that remittances are an important source of income, with approximately 17% of total Dominican families receiving some form of international monetary transfers. The monthly average transfer was USD 100, equivalent to 16% of the typical household income.

In 2004, the IDB conducted a survey to study how migrants' families use the remittances they receive in the Dominican Republic (IDB/MIF, 2004*b*). As shown in Figure 3, remittances are spent mostly on consumption items (60%). Lesser but also significant amounts were destined to education (17%) and commercial investment (5%).

Bankarisation of money transfers in the Dominican Republic is significantly small. According to ENHOGAR data, 92% of total recipient households use licensed money transfer companies to receive the money, while only 1% do so through commercial banks. Remittances in the Dominican Republic are currently regulated by the Financial and Monetary Law No. 183 (2002), which controls the operation of foreign exchange and money transfer companies.

Following nearly three decades of large-scale emigration to the United States, transnational ties – including but not limited to remittances – have solidified an identity among the Dominicans. The political, cultural and social dimensions of these linkages are reflected in the establishment of US branches of the main Dominican political parties, the participation of Dominicans in political positions in the United States, the increasing participation of the overseas community in Dominican elections and the existence of civic and social associations abroad.

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MEXICO

Mexico

Although Mexico has historically welcomed people of different origins, more recently millions of Mexicans have left their homes to go to other nations, primarily the United States.

Figure 1. Stock of Migrants and Level of Education of Mexican Emigrants to OECD and Latin American Countries

Stock of immigrants in Mexico
(Persons aged 15 or over, 2000)

107 840	United States
21 578	Guatemala
20 263	Spain
6 266	Cuba
5 886	Argentina
79 629	Others
241 462	**Total**

Stock of Mexican emigrants in OECD and Latin American countries
(Persons aged 15 or over, circa 2000)

8 250 885	United States
37 470	Canada
16 580	Spain
5 205	France
4 480	United Kingdom
41 852	Others
8 356 472	**Total**

Proportion of Mexican emigrants with completed secondary or higher education
(Persons aged 25 or over, circa 2000)

- 62% - 100%
- 46% - 62%
- 0% - 46%

Workers' Remittances
(USD million, 2008)

Inflows	25 137 (2.3% GDP)
Outflows	NA

Note: This Figure reports the stock of migrants recorded in national censuses and workers' remittances in balance-of-payments data. It will therefore not reflect unrecorded formal or informal flows, which may be material.

Source: For details on definitions and sources, please refer to the Statistical Annex.

Mexico has a complex migration dynamic, including origin, transit, and destination flows; nevertheless, Mexican outflows now dominate. According to the latest census round, there were more than 8.3 million Mexicans living abroad, of whom 99% were in the United States.

Although current immigration levels in Mexico are relatively low and the foreign-born represent only 0.4% of the country's population, the southern border with Guatemala has become a key crossing point for Central American migrants, most of them in transit towards the United States.

The Mexican population in the United States shows a low educational profile: around 70% of Mexicans in the country have not completed secondary education.

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Migration History and Policy Developments

Mexico embodies several dimensions of the migration process, being at once a country of origin, transit and destination. Yet, these flows are now dominated by the emigration of Mexicans to the United States. In the latest census round it was estimated that around 13% of Mexicans lived abroad, of whom around 8.3 million were in the United States. A more recent estimate (20087) in the American Community Survey put this figure at more than 11.4 million.

Current migratory patterns have their origins in the first half of the 20th century. During this period, Mexican workers migrated to meet labour shortages in the United States. This need became particularly acute during World War II, with much of the native workforce away on duty. In 1942 the Mexican Farm Labor Program (informally known as the Bracero programme) was created to formalise the temporary employment of workers from Mexico in the United States, mainly in the agriculture sector and railway construction. Over the 22-year period of its life, the programme saw the entry of some 4.5 million workers from Mexico on temporary contracts.

The official end of the Bracero programme in 1964 did not bring a stop to Mexican emigration to the United States. On the contrary, there was a gradual increase in flows, but with two important changes. First many more migrants were now undocumented and, second, flows tended to be more permanent. To respond to this new reality, the US Immigration Reform and Control Act (IRCA) of 1986 attempted to restrict unauthorised migration. It granted amnesty to certain immigrants already in the country, but established sanctions for employers that knowingly recruited undocumented workers.

The pattern of emigration to the United States responds to a combination of structural factors, such as wage and economic disparities, the complementary nature of labour markets and demographics, and a context of increasing economic integration and interdependence between the two countries. Despite currently more restrictive migratory policies, migration continues to be a major focus of political concern. The Mexican government has implemented a series of programmes and institutional reforms to strengthen governance and promote the integration of Mexicans into the host society. These include the creation of the National Council for Mexican Communities Abroad (CNCME) and the Institute of Mexicans Abroad (IME).

In recent decades Mexico has become an important migration transit country: migrants coming from Central America to the United States (mainly from Guatemala) approach by land through Mexico. The Mexican government's response has concentrated on administrative strengthening of its migration control structures and streamlining and reinforcing return procedures for irregular migrants. Bi-national commissions have been established with Central American countries and agreements for orderly return have been signed with Guatemala, Honduras and El Salvador. At the same time, Mexico also plays a leading role in most regional initiatives on migration, particularly the Regional Conference on Migration.

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Labour Market

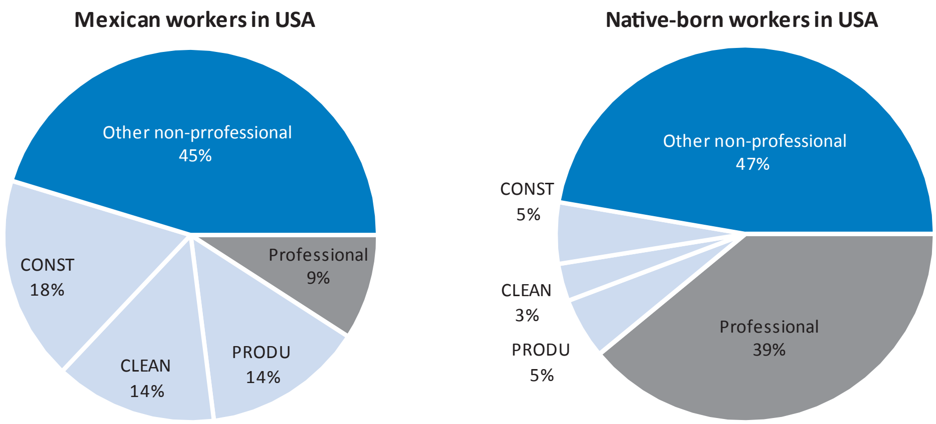
The 2008 American Community Survey confirms the importance of the Mexican labour force in the United States. On its figures there are around 7.1 million Mexicans working in the country, equivalent to 4.5% of the total US labour force.

Most Mexican emigration to the United States is motivated by economics. According to the 2006 Mexican National Survey of Population Dynamics, 76% of migrants were primarily seeking improved employment opportunities. This is reflected in the high activity rates of Mexicans, which are at levels similar to the native-born population.

Their employment pattern, however, differs from the native-born, despite the increasing diversity of the Mexican population in the United States. More than 90% of Mexican migrants occupy low-skilled positions compared with 61% for native-born workers (Figure 2). In particular, Mexicans show a significant concentration in cleaning, construction and production. Among other factors, differences in educational levels and lack of documentation may go some way towards explaining the reduced access of Mexicans to high-skilled jobs in the US market.

This is not to say that highly qualified Mexicans do not go to the United States. On the contrary, they are there in increasing numbers. The 2008 American Community Survey estimated that close to 470 000 Mexicans with bachelor or professional degrees were present in the country.

Figure 2. Distribution of Workers by Occupational Categories
(Percentage, 2009)



Note: The professional category comprises professionals and technicians, items from 001 to 395 of the Census Occupation Code (COC). Other abbreviations used are CLEAN: Building and grounds cleaning and maintenance; CONST: Construction and extraction; and PRODU: Production

Source: OECD Development Centre calculations, based on the US Current Population Survey.

StatLink http://dx.doi.org/10.1787/717132008464

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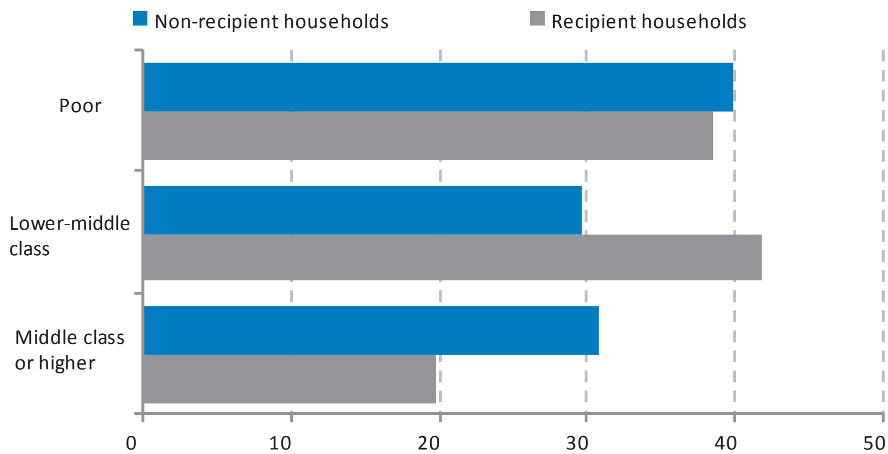
Relationship with the Country of Origin and Integration in the Host Country

From the 1990s onwards Mexico registered significant growth in remittance inflows, mainly from the United States. According to data from the Bank of Mexico, remittances increased from USD 3.7 billion in 1995 to USD 25.1 billion in 2008 (representing 1.3 and 2.3% of Mexican GDP, respectively).

Remittances are a significant currency flow for the Mexican economy, figuring as one of the main items in the balance of payments. In 2008 these transfers were 15% higher than Foreign Direct Investment. However, since 2006 growth in remittances flows has been slowing gradually. The economic crisis has seen them decline in 2008 and the first quarter of 2009.

Transfers of remittances play an important role too in supporting recipient families. The 2006 National Survey of Household Income and Expenditure (ENIGH) found that the monthly average transfer was USD 258 and made up 34% of family income. Around 1.8 million households, 7% of the total, received some form of international monetary transfers.

Figure 3. Distribution of Households by Socio-Economic Group and Receipt of Remittances (Percentage of remittance class, 2005)



Source: Secretaría General del Consejo Nacional de Población (2008).

StatLink http://dx.doi.org/10.1787/717132360467

Although remittances improve quality of life for recipient households, they do not contribute as much as they might in reducing poverty levels. As shown in Figure 3, the group that benefits most from remittances is the lower-middle class group, which accounts for 42% of recipient households but only 30% of non-recipients. In contrast, the proportion of households below the poverty line receiving remittances, at close to 40%, is similar to those not receiving them.

An interesting policy initiative that has spread in recent years is the "3-for-1" programme. With the aim of encouraging remittance-senders to invest in socially useful and productive projects, this Mexican government initiative sees the federal, state and municipal governments match the funding that communities abroad invest in social projects in vulnerable areas in Mexico. Additional programmes such as *Quién es quién en el envío de dinero* (1998), *Directo a México* (2004) and *Calculadora de Remesas* (2006) have helped channel remittances through the formal financial system and reduce their cost.

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Peru

Political stability and economic growth in Peru in the last decade are leading to a change in migration patterns, contributing to a reduction in the level of emigration.

Figure 1. Stock of Migrants and Level of Education of Peruvian Emigrants to OECD and Latin American Countries

Stock of immigrants in Peru
(Persons aged 15 or over, 2007)

5 889	United States
4 611	Argentina
4 373	Colombia
4 234	Chile
4 091	Bolivia
37 070	Others
60 268	**Total**

Stock of Peruvian emigrants in OECD and Latin American countries
(Persons aged 15 or over, circa 2000)

261 922	United States
79 757	Argentina
47 900	Spain
35 588	Chile
32 720	Venezuela
140 291	Others
598 178	**Total**

Proportion of Peruvian emigrants with completed secondary or higher education
(Persons aged 25 or over, circa 2000)

- 62% - 100%
- 46% - 62%
- 0% - 46%

Workers' Remittances
(USD million, 2007)

Inflows	2 131 (2% GDP)
Outflows	NA

Note: This Figure reports the stock of migrants recorded in national censuses and workers' remittances in balance-of-payments data. It will therefore not reflect unrecorded formal or informal flows, which may be material.

Source: For details on definitions and sources, please refer to the Statistical Annex.

Peru has historically been a country of destination, but this has changed in recent decades. Peru now experiences net emigration. Most Peruvians abroad live in the United States, Argentina or Spain.

This emigration has been driven by economic factors and the improvement of domestic economic conditions has reduced the trend in recent years.

One striking feature of Peruvian emigration is its high skill profile. More than 80% of Peruvian migrants in the United States (the main destination for Peruvians) have completed secondary or higher education.

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Migration History and Policy Developments

Historically Peru has been a country of destination, beginning with the establishment of Chinese, Italian and Japanese communities in the 19th and 20th centuries. The abolition of slavery in 1854 left the Peruvian economy with a labour shortage, especially in the sugar and cotton plantations and in mining. The first waves of Chinese and Italian flows were encouraged by the Peruvian government, under the Chinese Law (1849) and through the "European Immigration Society" (1872-76). During the first half of the 20th century the Asiatic community was consolidated by the arrival of migrants directly involved in trade and commercial activities.

The last three decades have seen Peru move decisively to being a country of origin. Peruvian emigration increased from 1980 in response to the hyperinflation and recession that gripped the economy and the internal armed conflict in the country. The 2000 round of population censuses found nearly 600 000 Peruvians living abroad (3.1% of the population), but figures from the Peruvian Ministry of Foreign Affairs put this number at more than 1.8 million. The principal destination was the United States, followed by Spain and, when local economic conditions were good, neighbouring countries such as Venezuela, Argentina and, later, Chile. In spite of the improvement in the economic situation Peruvian emigration continued to increase strongly in 2000-06. During this period it is estimated that annually over 30 000 Peruvians emigrated to OECD countries.

Since 2001 the Peruvian government has implemented a series of institutional reforms to strengthen governance and promote and develop links with the diaspora. These include the creation of the Sub-secretariat of Peruvian Communities Abroad and an electoral reform extending the obligation to vote to Peruvians resident abroad. In 2004 the Law of Migration Incentives was passed to promote the return of Peruvians who have lived abroad for over five years and intend to engage in professional and/or business activities in Peru. This forms part of a clearly defined migration policy based on the strengthening of assistance and links with emigrants.

Peru has now enjoyed a decade of consistent economic growth and political stability. This new macroeconomic environment together with the resolution of the internal conflict has tended to stabilise emigration flows over the last two years. Reductions in poverty (from 49 to 36% between 2004 and 2008) and improvements in living and working conditions have played a role in reducing the international migration of Peruvians, whose principal expressed motivation was lack of economic opportunities: some 54% of respondents in a survey (ILO, 2006), cited economic problems as the main reason why they left.

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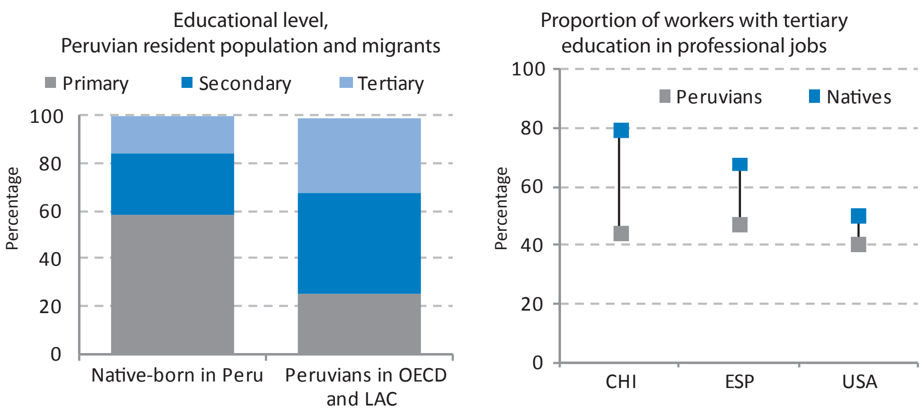
Labour Market

Peruvian migrants tend to be relatively highly skilled. As shown in the lefthand panel of Figure 2, 31% of Peruvian emigrants in 2000 had tertiary education while the equivalent figure for the general Peruvian population was 16%.

How these skilled workers fare in their countries of destination is therefore of interest. On the whole highly educated Peruvian immigrants are less likely to obtain skilled jobs than the native-born. The righthand panel of Figure 2 compares the proportion of Peruvian migrants with tertiary education who occupied skilled positions with equivalent figures for the native-born in three main destination countries: United States, Spain and Chile. Overall only 44% of Peruvian emigrants with a university or technical degree are employed in skilled positions, and in each case this is less than for natives. Although the absolute level is similar in each country, there are substantial differences in the size of the gap. Compared with the opportunities available to the native-born population, the likelihood of the migrants obtaining skilled jobs is lower in Chile than in Spain or the United States.

Figure 2. Peruvian Emigrants: Educational Level and Insertion in Labour Markets



Note: The professional category comprises professionals and technicians, corresponding to items 001 to 395 of the Census Occupation Code (COC) in United States, and groups 1 to 3 of the International Standard Classification of Occupations (ISCO-88) in Chile and Spain.

Source: OECD Development Centre calculations, based on OECD (2008), Database on Immigrants in OECD Countries and the 2000 round of national censuses for Latin America (Processed with ECLAC Redatam+SP on-line).

StatLink http://dx.doi.org/10.1787/717215602315

This unequal access suggests a need for further research. It is certainly the case that many Peruvian migrants are irregular (some 54% in 2004 according to estimates from the Peruvian Ministry of Foreign Affairs) and this will reduce their ability to seek formal skilled posts. In addition, the potentially lower value placed on qualifications obtained in their country of origin may be having an effect.

In this regard, bilateral agreements have been an important pillar of the Peruvian migratory policy. These agreements cover not only information exchange and the regulation of migration flows, but also matters intended to improve the working conditions of migrants including access to social security systems. Peru has signed migration agreements with Italy and Spain in the European Union and Argentina, Bolivia, Chile and Mexico in Latin America.

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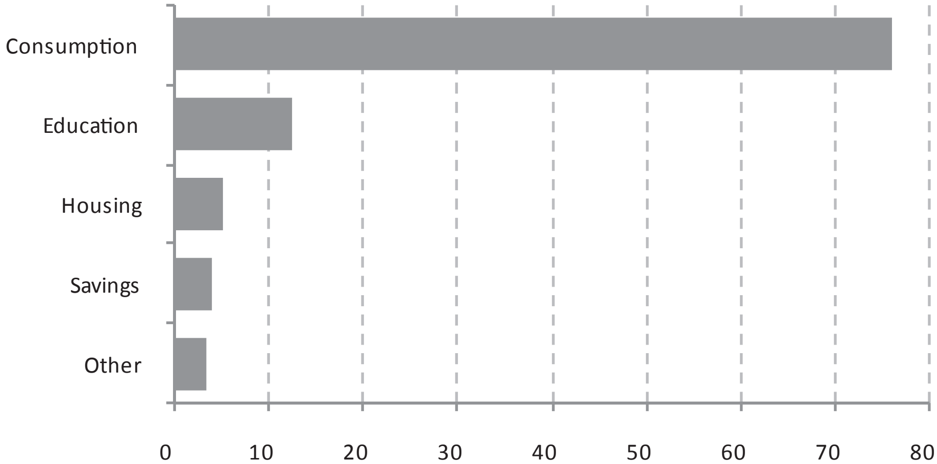
Relationship with the Country of Origin and Integration in the Host Country

Remittances to Peru have increased considerably, reflecting the growth of Peruvian emigration. In 2007, remittance inflows represented 2% of Peru's GDP (USD 3.7 billion).

Figure 3. Principal Use of Remittances in Peru, 2006
(Percentage of total current expenditures)



Source: ENCO, National Continuous Survey (2006).

StatLink http://dx.doi.org/10.1787/717231464504

According to the 2006 National Continuous Survey (ENCO) 249 700 households (3.8% of total households) receive international monetary transfers. Of these around 60% belong to the middle socio-economic groups.

Households receive on average monthly transfers of USD 156, equivalent to 72% of average labour income in Peru. This additional income for Peruvian households directly raises living conditions and, compared with the national average, recipient households also perform better in terms of educational level and access to basic services and housing (ILO/INEI, 2008).

As shown in Figure 3, Peruvian families use the bulk of the funds received (76%) for basic needs (food, utilities and other). Relatively small amounts are destined to education or housing expenditures (12 and 5% of receipts respectively). To stimulate greater investment in housing the Peruvian government has established the MIVIVIENDA fund. This provides guarantees to encourage house purchase in Peru. An agreement signed in 2007 between the Peruvian Ministry of Foreign Affairs and the financial sector also seeks to influence the use of remittances. This facilitates the granting of credit to develop micro enterprises in Peru through remittance-guarantees.

Following nearly three decades of continuous large-scale emigration, there are substantial communities of Peruvians abroad. A central element of the current National Immigration Policy is ensuring the successful integration of these Peruvian emigrants in their host societies.

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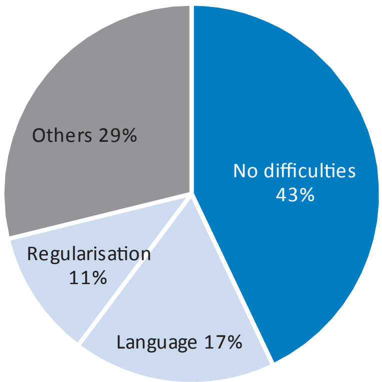
Figure 4. Difficulties Reported by Peruvians in Host Countries, 2006



Source: ILO (2006).

StatLink http://dx.doi.org/10.1787/717243165352

A survey "Linking Peruvians Abroad" (Revinculación de Peruanos en el Exterior), jointly conducted by the ILO and the Peruvian Ministry of Foreign Affairs (2006), explored this question. A surprisingly high number of respondents (43%) reported that they had encountered no difficulties in their integration (Figure 4).

However, there are still challenges to be met. The two main difficulties faced by Peruvians abroad are related to language barriers and their immigration status (reported by 17 and 11%, respectively). The latter is consistent with the way in which Peruvians emigrate. The same study found that 58% of respondents had entered their country of destination on a tourist visa.

For many Peruvian emigrants returning home is an aspiration they keep alive. Of the sample in the Revinculación study 47% said they intended to return to Peru at some point in the future. There is evidence that the current improved economic and security outlook, together with government initiatives explicitly aimed at encouraging voluntary return, are having an effect. The 2007 national census recorded 43 468 returned migrants, notably from the United States and Argentina.

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STATISTICAL ANNEX

The Country Notes aim to summarise briefly the main migration features of selected Latin American countries. Each is arranged in four sections:

- A map depicting the stock of emigrants and immigrants for each country by country of destination or origin, the education level of these migrants compared to the OECD and Latin American averages, and the relevant remittance inflows and outflows where this information is available.
- Migration history and policy developments, describing briefly the migration patterns experienced by each country and the effects of the migration policies at home and abroad on these.
- Labour market, presenting relevant information on labour-market insertion in host countries.
- Relationship with the country of origin and integration in the host country covering topics such as remittances, contacts with the country of origin and integration, depending on data availability for each country studied.

Methodological Note

In the preparation of the country notes, special attention was paid to data collection on migrant stocks. This has required processing of national census micro-data for a significant number of Latin American and Caribbean countries that are not members of the OECD. The model is the OECD DIOC database, a fundamental reference for OECD member countries backed by a consistent methodology. Extending the OECD DIOC methodology to Latin American and Caribbean countries will permit more transparent comparison of migrant stocks among Latin American economies, and between OECD and Latin American economies. Data on stocks of migrants in Latin American and Caribbean countries in this *Outlook* are taken from this new database. Those for OECD countries are from DIOC.

Sources and coverage:

Data contained in the country notes were extracted from:

- The 2000 round of national censuses of Latin American and Caribbean countries.
- The Database on Immigrants in OECD Countries (DIOC).
- Other sources of information in Latin American countries and OECD countries of destination such as labour, household and immigration surveys and the IMF Balance of Payments database for remittances.

The 2000 round of national censuses in Latin American countries were used to calculate the stocks of migrants in Latin American and Caribbean countries and some of their characteristics, including educational level, age, sex, sector of activity and occupation, among others. This project converted census micro-data into a format consistent with prior OECD work, using three different processing channels depending on data availability. Some census data were processed online with ECLAC Redatam+SP, others were derived from the IPUMS-International website and the remainder were processed directly from the original source. The countries covered were: Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Dominican Republic, Ecuador, El Salvador, Honduras, Mexico, Nicaragua, Panama, Paraguay, Peru and Venezuela (for further details on sources see Table 1 at the end of this note). Only eight countries (Argentina, Brazil, Chile, Colombia, Costa Rica, Dominican Republic, Mexico and Peru) are included in the country notes section of this publication. Other country notes will be provided online.

DIOC is the outcome of a multi-year project of the Directorate for Employment, Labour and Social Affairs (Non-member Economies and International Migration Division), which was carried out in collaboration with the national statistical offices of OECD member countries. It collects comprehensive and comparative data on immigrants living in OECD countries, covering a broad range of demographic and labour market characteristics of these populations. The information offered is on a stock basis,

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reflective of its main sources of data: population censuses and registers, complemented by labour force surveys.

Other sources have been used with the objective of better describing the migration reality of each country. These have included labour-force surveys, immigration surveys and the IMF Balance of Payments database, supplemented by other national surveys where appropriate and available.

Classifications and variables:

An extensive harmonisation exercise was carried out to reconcile the Latin American and Caribbean census data and the DIOC database. The new database covers the following variables: country of birth, educational attainment, sex, age, employment status, and (for employed individuals) occupation and sector of activity. Following DIOC conventions, these variables are defined as follows:

Migrants: Migrants are foreign-born individuals regardless of their nationality. For comparability with the DIOC database, only individuals aged 15 or older were taken into account.

Education: The International Standard Classification of Education (ISCED; cf. UNESCO 1997) was used as a baseline, but groups have been aggregated as follows: primary level (ISCED 0/1/2), secondary level (ISCED 3/4) and tertiary level (ISCED 5/6).

Sector: Sectors of activity were recorded according to the International Standard Industrial Classification, Rev. 3.

Occupations: Occupations were classified using the International Standard Classification of Occupations (ISCO-88).

Remittance inflows and outflows: Remittances have been measured using the estimates of Workers' Remittances in the Balance of Payments Current Transfers Account. The source for both remittance inflows and outflows is the Balance of Payments Statistics database of the International Monetary Fund (IMF).

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Table 1. Metadata on Stocks of Foreign-born Population in Selected Latin American and Caribbean Countries

Country	National Census
Argentina	Censo Nacional de Población, Hogares y Viviendas (2001). Complete sample. Processed with ECLAC Redatam+SP online.
Bolivia	Censo Nacional de Población y Vivienda (2001). Weighted sample. 10% sample of the 2001 Bolivian Census (collated online in IPUMS).
Brazil	Censo Demográfico (2000). Weighted sample. 5% sample of the 2000 Brazilian Census (collated online in IPUMS).
Chile	XVII Censo Nacional de Población y VI de Vivienda (2002). Complete sample. Processed with ECLAC Redatam+SP online.
Colombia	Censo General (2005). Complete sample. Processed with ECLAC Redatam+SP online.
Costa Rica	IX Censo de Población y V de Vivienda (2000). Complete sample. Processed with ECLAC Redatam+SP online
Dominican Republic	VIII Censo de Población y Vivienda (2002). Complete sample. Processed with ECLAC Redatam+SP online.
Ecuador	VI Censo de Población y V de Vivienda (2001). Complete sample.
El Salvador	VI Censo Nacional de Población y V de Vivienda (2007). Complete sample.
Honduras	XVI Censo de Población y V de Vivienda (2001). Complete sample. Processed with ECLAC Redatam+SP online.
Mexico	OECD (2008).
Nicaragua	VIII Censo de Población y IV de Vivienda (2005). Complete sample. Processed with ECLAC Redatam+SP online.
Panama	X Censo Nacional de Población y VI de Vivienda (2000). Complete sample. Processed with ECLAC Redatam+SP online.
Paraguay	Censo Nacional de Población y Viviendas (2002). Complete sample. Processed with ECLAC Redatam+SP online.
Peru	XI Censo de Población y VI de Vivienda (2007). Complete sample.
Venezuela	XIII Censo General de Población y Vivienda (2001). Weighted sample. 10% sample of the 2001 Venezuelan Census (collated online in IPUMS).

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Latin American Economic Outlook 2010

Contrary to prevailing wisdom, Latin American countries that opened their markets to international competition during the last decade have not been more vulnerable to the global economic downturn. The OECD *Latin American Economic Outlook 2010* provides a fresh analysis of economic trends in the region with a particular focus on the role that international migration and remittances play in shaping the current context.

"This excellent report correctly emphasises the less known and studied aspects of the complex and heterogeneous phenomenon of migration, allowing a broader vision of the topic." *Francisco Alba, Centre for Economic and Demographic Studies, Colegio de Mexico*

"Among the most interesting surprises of the global crisis is that so far its impact on Latin America has been less than anticipated. This OECD report offers a clear analysis of the factors that explain this phenomenon." *Moisés Naím, Editor in Chief,* Foreign Policy

"The OECD Development Centre has earned a privileged place in studies on Latin American economic development. This new report convincingly shows that migration has very positive effects in both sending and receiving countries and highlights the importance of migrants' social protection." *José Antonio Ocampo, Columbia University and former UN Under-Secretary General for Economic and Social Affairs*

"From this excellent report we can conclude that the recovery of social indicators will lag behind economic recovery. As a consequence, migration will continue, despite the fall in remittances and the difficulties created by the crisis in countries of destination." *Francisco Rojas Aravena, Secretary-General, Latin American Faculty of Social Sciences*

"This essential study shows that countries open to the international economy with serious fiscal and monetary policies were better prepared to confront this crisis. The report also explains, with realistic analysis, why migration policies belong on the international agenda." *Ricardo Lagos, former President of Chile*

"This report is a must-read, as it provides one of the most interesting sets of data I have seen on migration flows in Latin America and their economic impact on the region." *Andrés Oppenheimer, Syndicated Columnist,* The Miami Herald

"This report breaks new ground in highlighting the relationship between migration and finance. It underlines the key role of migration and remittances in the recovery from the crisis and, in the long term, in job creation and development." *Dilip Ratha, Manager, Migration and Remittances Team, World Bank*

"This volume suggests that migration can help the development process provided that some interventions are adopted both in the sender and recipient countries." *Mauricio Cárdenas, Senior Fellow and Director of the Latin America Initiative, Brookings Institution*

"Policy makers, academics and others interested in Latin American will find here a serious and relevant contribution to advancing their own work." *Santiago Levy, Vice President for Sectors and Knowledge, Inter-American Development Bank*

"This edition provides valuable insights on the role of contemporary migration flows in Latin America: the contribution of remittances; the urgent need to develop innovative financial markets suited for people on the move; and the evolving framework of public policies addressing migration flows." *Rafael Fernández de Castro Medina, President Felipe Calderón's Foreign Policy Advisor*

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