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Migrants' Money Is Imperfect Cure For Poor Nations

Earnings Sent Home From U.S. Fuel Increased Spending But Not Much Investment

By Bob Davis

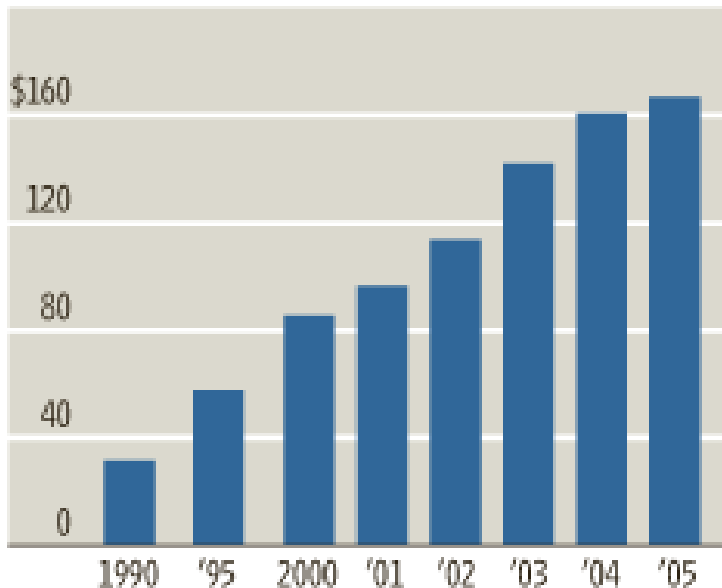
Nov. 1, 2006 12:01 am ET

CIUDAD BARRIOS, El Salvador -- This lively mountain town survives on money sent from its sons and daughters living in the U.S. On days payments arrive, lines at the local credit union can reach 150 deep. The crowds then hail motorcycle taxis and head for the town's open-air market to stock up on food and clothing, or browse tiny appliance stores stuffed with blaring televisions and stereos.

It's the sort of scene that many development economists believe could transform some of the world's most impoverished regions, by putting cash directly in the pockets of the poor. With tens of millions of migrants around the globe sending remittances home, the flood of money has grown immense -- \$167 billion last year, according to the World Bank.

Rising Balances

Worker remittances sent to developing nations, in billions of dollars:



Note: The bank doesn't provide year-by-year numbers before 2000. The numbers partly reflect better data collection.

Source: World Bank

But Ciudad Barrios also demonstrates why reliance on remittances may turn out to be the latest development fad that fails to live up to its hype. The downside: a cycle of continued poverty, as dependence on remittances turns the town into a kind of ward of the U.S. Those with entrepreneurial ambition head north, emptying out the town of its talent. Only a tiny fraction of the money they send home is invested in industry or agriculture that could produce jobs. And with the breadwinners away, organized thugs pounce on a place where money pours in from outside. All of that leaves little opportunity for the next generation except to follow their predecessors north, if they can.

"As soon as people go home and see what their salaries are [there], they come back to the U.S. again," says Israel Hernández, 38 years old, who left Ciudad Barrios in 1998 and has been cleaning houses in Washington, D.C. He has sent enough cash home to his grandmother for her to buy a house. She misses him, she says, but urges him to stay up north.

For countries to reduce poverty on a sustained basis and to create a middle class, they need to grow rapidly over years. Though remittances fuel some spending, there isn't much evidence they have added to sustained growth. Instead, the infusions of outside

cash often distort the local economy and may diminish the long-term prospects for gains.

The flood of money from abroad can raise the value of local currencies, making it harder for exporters to compete because the effective price of their goods goes up. Meanwhile, about 85% of the money goes to pay the daily bills of the people left behind, with little left over for savings and investment. Migrants eventually return to retire in their home nations, not to help build their economies.

"Remittances are a band-aid on fundamental development problems," says Dean Yang, a public-policy professor at the University of Michigan. "Labor export and remittances won't turn El Salvador, the Philippines and other poor countries into the next development tigers." Even the World Bank, which has pushed the development potential of remittances, is having second thoughts. In a report on Latin America released yesterday, the bank says that remittances are "neither 'manna from heaven,' nor a substitute for sound development policies."

Remittances have received increasingly widespread attention in recent years as a way to boost aid without spending government money, as other formulas for growth have failed to produce widespread gains. In the 1970s and early 1980s, many nations tried closing their borders to protect their local industries from competition, which boosted growth for a while but led to high prices and monopoly control. Then they tried the opposite approach, free trade and market liberalization, with limited effect so far except in Asia. Meanwhile, foreign aid has been too small and inefficient to make much of a difference, while private investment has been targeted at a limited number of countries and industries.

Remittances do directly help many poor families feed themselves and educate their children. Money sent home from abroad accounts for about 60% of the income of the poorest households in Guatemala, and has helped reduce the number of people living in poverty by 11 percentage points in Uganda and six percentage points in Bangladesh, according to World Bank studies.

Nevertheless, a look at El Salvador shows the ways in which the cash also can hinder impoverished nations. The nation of seven million has revamped its economy since the civil war ended in 1992 in a so-far elusive effort to spur rapid growth. El Salvador abolished price controls, privatized industries, slashed tariffs that were as high as 290% and adopted the dollar as its currency in 2001 to limit inflation. Earlier this year, it joined a regional free-trade bloc with the U.S.

Salvadorans started to flee the country in great numbers in the 1980s as the civil war there intensified. Now one in six Salvadorans -- 1.5 million people -- live abroad, many of them illegally in the U.S. They send home nearly \$3 billion annually, equal to about 16% of the country's gross domestic product.

Ciudad Barrios, a remote town 100 miles east of San Salvador, ping-ponged between guerrilla and government control during the civil war. José Edgardo Díaz Cordero worked in the town's hospital pharmacy in 1990 when guerrillas demanded that he give them medicines to treat their wounded. Then, he says, he

received an anonymous message from a right-wing death squad accusing him of being a guerrilla ally and warning him to leave the country.

Mr. D&az made his way to the Washington, D.C., area where many others from his town had settled, attracted by a booming construction industry. He started sending home several hundred dollars a month to his wife to care for their five children. He has been home just once, for about a year in 1995, but wages were too low to make a go of it, says Mr. D&az, who is now 54. He returned to the U.S. and was later joined by two sons who became his partners in a flooring business. Another burst of Ciudad Barrios natives, who worked in the region's coffee fields, headed for the U.S. starting in 2000 when coffee prices plummeted.

Francisco Membreño, once a Ciudad Barrios coffee farmer, left his pregnant wife in 2000, worried that he wouldn't be able to support his newborn. He hasn't ever been back to meet their son, Ronald, who's now 6 years old. Mr. Membreño works two jobs cleaning offices in Washington, D.C., making \$575 on a good week, and sharing an apartment with another Salvadoran.

Each month he sends home about \$300 to his wife, Ernestina Argueta, who moved with Ronald to her parents' sweltering concrete house lit by a single light bulb. The money goes for food and medicine mostly, says Ms. Argueta, with a little left over to save to expand a tiny plot of land her husband purchased and hopes someday to cultivate. Though her elderly mother dreams of a new sewing machine, Ms. Argueta says, "For now, we're not buying anything, until he comes back."

About one-third of the 40,000 residents of Ciudad Barrios and surrounding hamlets receive remittances, estimates Claudia Rodr guez-Alas, an American University researcher who has studied the town. Salvadorans abroad typically share apartments, keep each other current on job openings and lend relatives at home the \$5,000 or so necessary to pay "coyotes" to guide them illicitly across Mexico to the U.S.

In Ciudad Barrios, monthly remittances average about \$157 a household, according to Ms. Rodr guez-Alas. That's slightly more than the government calculates is

enough to feed a family of four. But it often doesn't pull families above the official poverty line of \$275 a month. Essentially, remittances are sufficient to push families out of extreme poverty, but not much higher.

The extra cash does have beneficial effects. It gives even the most destitute families the means to pay for food at the town's markets, and is extra disposable income for those who work. Salvadoran families that receive remittances are more likely to keep their children in school than other families, according to a study by two economists, Alejandra Cox of California State University, Long Beach, and Manuelita Ureta of Texas A&M.

Better-off Salvadorans abroad often send two checks a month -- one for their family's daily expenses, and another to save up to buy small homes with luxuries such as glass windows, electricity in every room, steel gratings on the doors and windows, and tile floors.

A small consumption boom fed by the checks has doubled the number of businesses registered with the Ciudad Barrios City Hall to 220 since 2000, and even helped prompt the opening of a "cyber cafe." Around the town's central square are five financial institutions that handle remittances, including Western Union, which also advertises on highway overpasses on the way to town.

One hardware store, Agro Ferreteria Rivera, has carved out an unusual niche: The couple that owns the store travels monthly to Maryland to take orders for homes sketched out by migrants, who wire payments to their families. A separate appliance store takes orders by cellphone from abroad, while a city council member sells solar panels for homes built in fields that lack electricity hook-ups. Some of the new homeowners also get their fences electrified for extra security.

The gains in consumption financed from abroad could fuel the economy. But paradoxically, the easy money from remittances leads to a fall, rather than a rise, in domestic savings as a percentage of gross domestic product. The investment rate as a percentage of GDP stagnates as well.

The result: The country makes little progress. Between 1999 and 2005, remittances doubled to \$2.8 billion, but the country limped along at an annual growth rate of just 2.4% -- far too low for a poor country to advance much. The tide of money from abroad boosted the value of its currency compared with that of its neighbors by nearly 50% between 1992 and 2001, which damaged exports. El Salvador has since adopted the dollar as its currency, but competition from China has intensified and other Central American nations have kept their currencies undervalued, so Salvadoran exporters haven't recovered.

Soaring remittances have boosted real-estate prices to levels that locals without outside help can't afford, while reducing the incentive of remittance recipients to work at home -- since wages are a pittance compared with what their relatives make in the U.S. In Ciudad Barrios, the coffee-growing cooperative recruits Nicaraguans and Hondurans to work the fields, because they can't find enough Salvadorans to fill jobs that pay between \$5.50 and \$8 a day.

Elsewhere, the same pattern occurs. Examining Mexican labor data, economists Catalina Amuedo-Dorantes of San Diego State University and Susan Pozo of Western Michigan University say that a boost in remittances prompts men to cut back their hours at salaried jobs and fill in with informal work.

Groups of Salvadorans abroad do form associations to help finance municipal improvements back home. In Chinameca, a town near Ciudad Barrios, for instance,

migrants have helped to pay for the town's water tower and for the roof on a local church. But the efforts have fallen well far short of the need.

Economists say that El Salvador and other remittance-receiving nations must figure out ways to route money from abroad into domestic investments. The Salvadoran government, for instance, wants to create investment vehicles for Salvadorans abroad to bankroll domestic projects or industries.

In that vein, Salvadoran developers are holding fairs around the U.S. to try to make it easier for migrants to buy real estate. A Washington, D.C., financial company, Microfinance International Corp., is starting to offer Salvadorans transnational loans, which they can use to make investments in El Salvador and make payments in the U.S. -- and avoid having to pay fees on money wired home. Since many Salvadorans don't use banks or credit cards, the company's customers can use their remittance history to prove their creditworthiness.

In Ciudad Barrios, Lorena Romero, the acting manager of a local credit union, says only a tiny percentage of remittance receivers take out business loans. Even those often use the proceeds to pay coyotes to take them to the U.S. instead of opening businesses locally. Another credit union called AMC, which does business throughout eastern El Salvador in conjunction with Microfinance International, says just 1% of its remittance customers take out loans for businesses.

Wilson Salmer n, AMC's general manager, says many migrants don't invest in El Salvador because they're afraid their families will become targets of gang violence. One of the reasons that many nations have come to depend so heavily on remittances -- Haiti, Bosnia, Serbia, Honduras, Nicaragua -- is because people were frightened away by war, and their nations are still torn by violence.

In Ciudad Barrios, many remittance recipients try to avoid calling attention to themselves. Some pick up their cash in neighboring towns where they aren't known. Others pace their purchases of appliances, so their neighbors don't notice. The latest gang tactic is to call remittance receivers on their cellphones and extort cash instead of doing it in person. Some in Ciudad Barrios won't answer calls from numbers they don't know.

The fear damps local investment, too. Mr. Salmer n says his credit managers are afraid to travel into the countryside where gang influence is strong. A number of migrants say they wouldn't start a business in Ciudad Barrios for fear they'll draw unwanted attention. "You'll be robbed," says Dora Ruiz, a cook at a Washington, D.C.,

McDonald's restaurant, who wires \$200 a month to care for her four children who live with her sister-in-law. "People will come in through the windows if need be."

At Ciudad Barrios' sole high school, students recognize one important benefit of remittances: They aren't forced to drop out of school to work, as their parents were. The senior class this year is triple the size of a decade ago, says the school's assistant principal, Lex Marvin. But some now leave early to join parents abroad, and few see much opportunity in El Salvador after graduation. José Ines Aguilar Osorio is a shy, slender senior whose father works as a mason in the U.S. "If I don't find work here," he says, "I'm leaving."

—*John Lyons in Mexico City contributed to this article.*

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