DIÁLOGO A FONDO
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Impact of Remittances on Household Decisions in Guatemala

Constitution Square in Guatemala City, Guatemala: where many families rely on remittances for income support (photo: diegograndi/iStock)

By Esther Pérez Ruiz

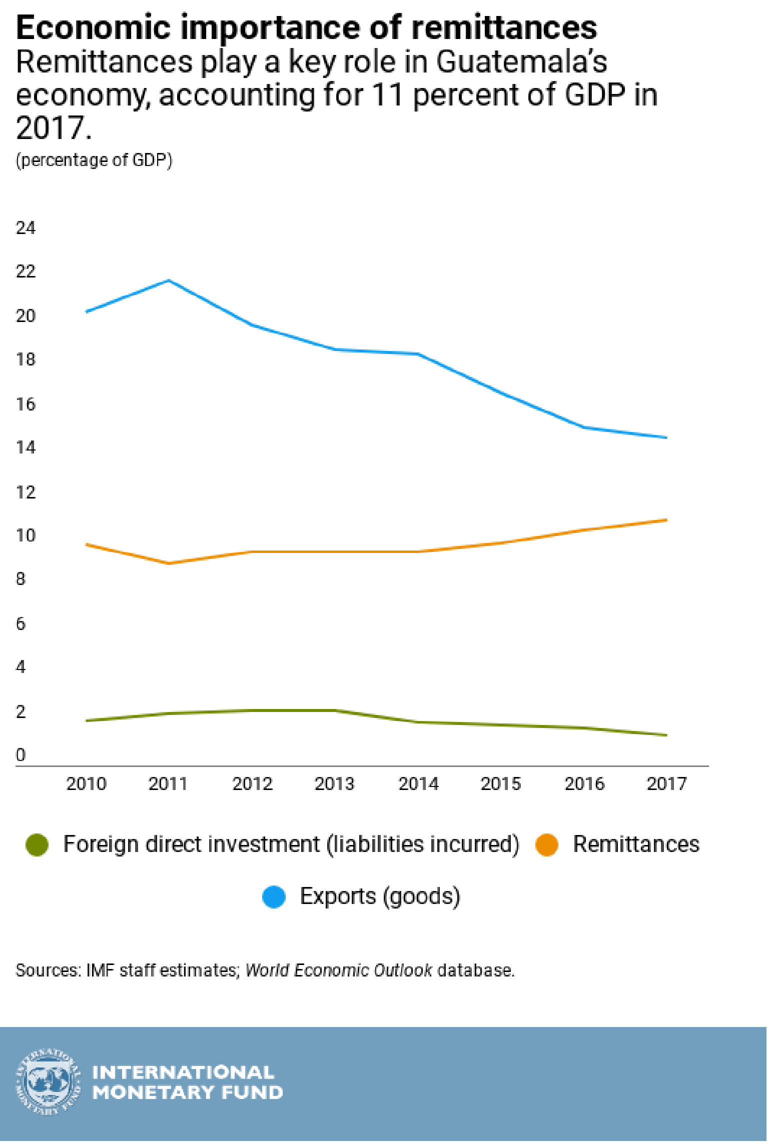
Remittances are critical to Guatemala's economy—accounting for more than 11 percent of GDP in 2017. Coming mostly from the U.S., these income transfers have helped to reduce poverty in the country and have contributed to higher investments in education by households that receive remittances.

In our latest research, we looked at how important remittances were in the decision-making process of recipient households to invest in education and to join the labor force. We argue that policies that improve labor market conditions in Guatemala can help boost the employment of remittance recipients, and ultimately support growth prospects for the country.

Remittances play a key role

With a net outward migration rate of 14 percent in 2017, Guatemala ranks eleventh among the world's remittance-receiving emerging economies, and second in Latin

America and the Caribbean, behind Mexico. In recent years, income from remittances in Guatemala has trended upward, reaching 11 percent of GDP in 2017 and accounting for 46 percent of the total income of households that rely on remittances (one in ten) in 2014.



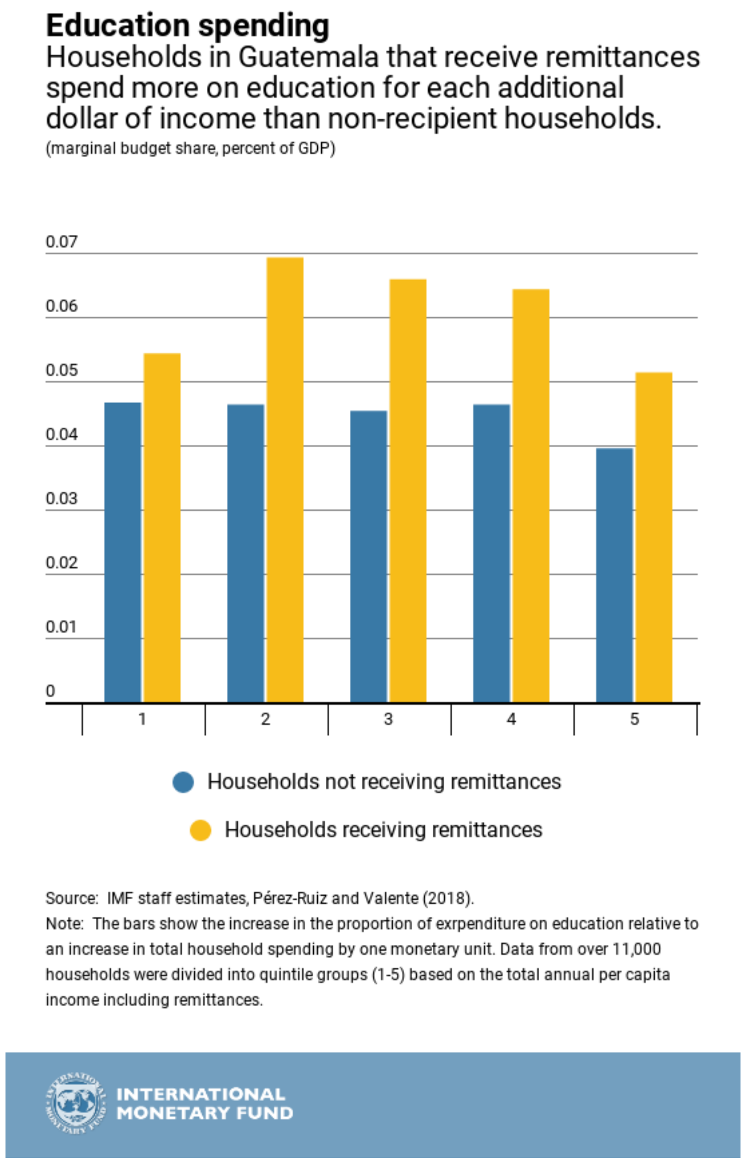
Remittances are the second highest foreign currency income category behind exports, exceeding by far foreign currency income from tourism or foreign direct investment.

Impact on households' welfare and education investments

High remittance income has sparked interest owing to its impact on recipient households.

Numerous studies have shown that remittances ease poverty and significantly increase the quality-of-life and health for people in these households, which tend to spend relatively more on electricity and on sanitation, water, and waste collection services.

Households that receive remittances also tend to raise investment in education, our analysis finds. This is because remittances help to finance the cost of education and/or reduce the need for younger members of the household to drop out of school early in order to work and contribute to the household's income.



Deciding to work

That said, greater investment in human capital would only lead to better growth if those individuals that get remittances wanted to join the workforce. Two questions must therefore be asked: Do remittances discourage participation in the labor market? And does Guatemala's labor market offer sufficiently well-paid job opportunities for the investment in education to pay off?

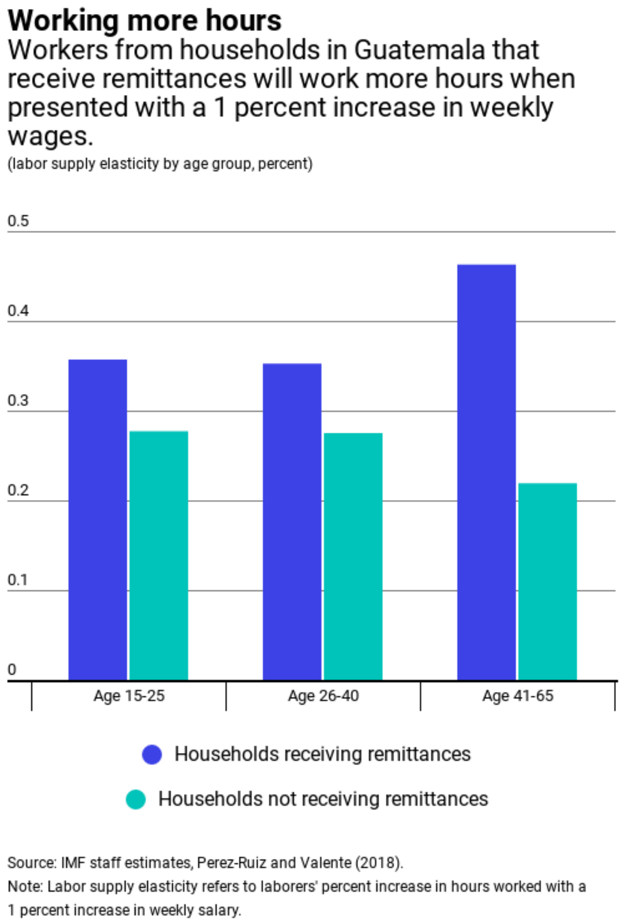
To answer these questions, we took a closer look at labor supply decisions of households that receive remittances, and those that do not.

As they are simple income transfers, one might think that remittances might have a negative effect on participation in the labor market if their recipients substitute (hard-earned) employment income for remittances. And since the distance between the remitter and the receiver makes monitoring difficult, moral hazard problems may arise and induce recipients to divert resources to consumption of leisure.

Conversely, our analysis suggests that the labor supply of members of households that receive remittances is relatively more elastic and responsive to wage changes for the three age groups considered—namely 15–25, 26–40, and 41–65.

For example, for the 41–65 age group, a 1-percent increase in weekly wages increases the weekly hours offered by members of recipient households by 0.5 percent, compared to an increase of just 0.2 percent for members of non-recipient households.

There is also evidence of a higher percentage of microentrepreneurs among households receiving remittances, which would suggest that remittances tend to ease the financial constraints of self-employed households.



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Labor market reforms

The absence of disincentives to labor supply suggests that the key to expanding the positive impact of remittances to employment and growth is to promote attractive job opportunities by reducing employment in the informal sector.

At 3.1 percent of the labor force, the unemployment rate seems low. However, most employment is occurring in the informal sector, which accounts for 70 percent of total employment (40 percent in Latin America).

Curbing informality in Guatemala requires a comprehensive program that entails means of raising productivity and expanding social benefit coverage to all workers, including those who are self-employed. Enhancing apprenticeship programs, such as *Mi Primer Empleo* and vocational training, and ensuring that part-time work is a successful path towards formal employment that guarantees the labor rights of this group and matches their remuneration to time actually worked, are also important to promote formal employment.

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