Remittances may redefine the demographic support ratio

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When measuring the demographic support ratio, including only the country's residents may prove insufficient. Lukas Tohoff, Daji Landis, Letizia Mencarini, and Arnstein Aassve develop a novel demographic indicator to account also for remittances, and show that, especially in middle-income countries, figures changes considerably.

It is much easier and cheaper to send money across national borders today because of new financial service providers such as Wise, Remitly, or WorldRemit, which have substantially reduced international financial transaction costs. These new financial service providers, as well as an earlier wave of improved access to banking, have massively promoted cross-country money transfers – even those of only small amount. As a result, total remittances sent to low- and middle-income countries have increased approximately twelvefold in the last 30 years and amounted to $626 billion in 2022. In fact, remittances have already outpaced other capital flows into developing countries, including foreign direct investment and official development assistance.

In a recent publication (Tohoff et al. 2024), we examine the previously overlooked link between remittances and demographic support. Why do money transactions matter to demography? Because the interaction between the demographic composition of a country and its economy matters. As we know, during the period when a country transitions from high fertility and mortality rates to low ones, there are many working adults and relatively few dependent children and seniors. This advantageous ratio can pave the way for rapid growth, during this period and beyond. It can kickstart economic growth and poverty reduction. In other words, a country can fully cash in on its *demographic dividend*.

However, if there are not enough jobs for the growing workforce, demographic transitions can go terribly wrong. High unemployment, coupled with large *youth bulges*, increases the risk of conflict, and can have a destabilizing effect on society. While emigration helps reduce population pressures, the demographic dividend has (historically) been lost with the exodus of workers. As we show, the burgeoning role of remittances is changing that paradigm.

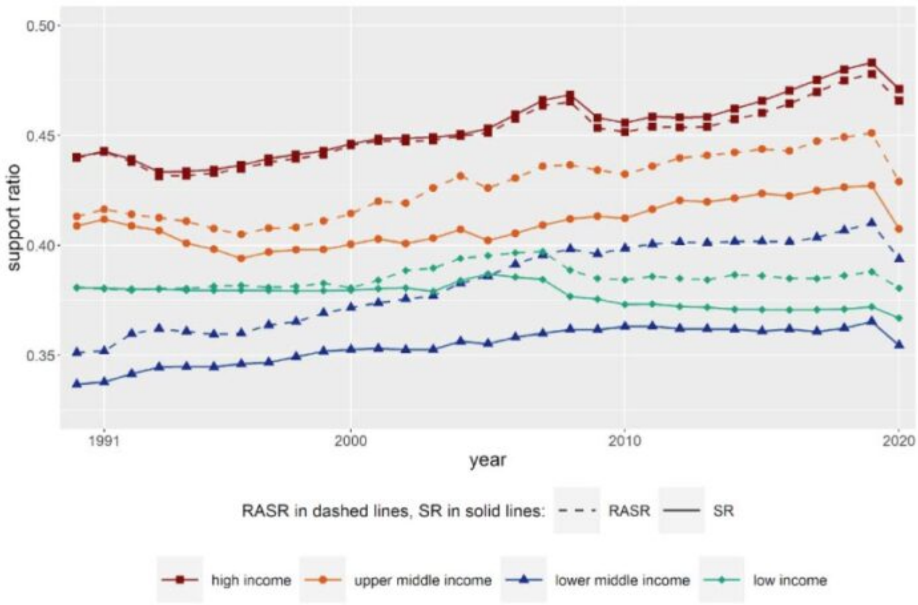
A remittances-adjusted support ratio: RASR

To account for the support offered through remittances, we developed a new demographic indicator: the remittances-adjusted support ratio (RASR). We incorporate remittances into the well-established support ratio (SR) by expressing them as worker equivalents. The support ratio is generally defined as the ratio of effective workers to effective consumers in a population. To express remittances (money) as effective workers (people), we divide net remittances by a country's average per capita labour income. This yields what we call *effective shadow workers*. For example, if a country receives 1 million USD in remittances and the mean annual per capita labour income of this country is 10,000 USD, then this equates to 100 shadow workers. The money sent by migrants is equal to 100 average annual incomes back home or, in other words, the remittances are equivalent to the support of 100 average workers. To calculate the RASR, we simply add these shadow workers to the numerator of the established support ratio, thereby incorporating their supportive role into the indicator.

Adjusting for remittances may make a large difference

Our findings reveal significant differences between traditional support ratios and the remittances-adjusted support ratio, particularly in middle-income countries (Figure 1). Even as early as the 1990s, the remittances adjustment makes a clearly visible difference, and the gap between the two support ratios has steadily increased since then. Today, the remittance adjustment is particularly large in the Caribbean, Central America, Southern Asia, Eastern Europe, and Central Asia. In the Philippines, for instance, the RASR is more than 10 percent larger than the classical support ratio; in El Salvador it is more than 30 percent larger, underscoring the pivotal role of remittances in bolstering demographic support.

Figure 1: Classical support ratios (SR) and remittances-adjusted support ratios (RASR) by country income class



NOTE: The figure shows weighted averages of the SR and the RASR by income class using the World Bank country classifications by income level. Weights were computed for each country as the product of the logarithmized total population in millions (plus 1) and the number of years for which the RASR could be calculated. Dashed lines denote the RASR and solid lines the SR. The clear dip in both SR and RASR across all income classes in 2020 can likely be explained by the onset of the COVID-19 pandemic, low mobility of migrants, and rising unemployment rates.

In high income countries, the RASR is not notably different from the classical support ratio, as (negative) net remittances divided by high average incomes yield a negligible number of (negative) shadow workers. In Germany, the US, or the UK, for instance, we see basically no effect of remittances on demographic support. When migrants work in these high-income countries, they might even play a dual supporting role. They support their host country by working and paying taxes and they support people in their country of origin via remittances.

Promoting migration while facilitating remittances may now be an attractive policy approach for countries facing a large youth bulge and too few employment opportunities. Such a solution is not equivalent to keeping and employing the youth at home, however. While remittances can be very valuable in supporting a country’s population in good times, they tend to make countries more dependent and vulnerable in times of global crises. Furthermore, the outflow of high-skilled workers is not in the long-term interest of developing countries, even if it leads to higher remittance inflows in the short to medium term.

It is difficult to assess the extent to which countries are already exploiting remittances as part of their growth strategies. The identification of causal links between the RASR and economic growth is ambiguous. It is plausible that the additional support of remittances leads to more economic growth. However, in a country where the economy and wages are growing fast, there is little reason for its citizens to emigrate. So, a simple correlation coefficient between remittances and economic growth will not be particularly informative.

Conclusion

The RASR shows that demographic support in many countries is much higher than the classical support ratio would suggest. Remittances already play a critical role in economic and demographic support today. Once we take them into account, we can see that a country's demographic composition matters – not just across age groups but also across national borders. Anyone who is concerned with the demographic composition of low- and middle-income countries should therefore look not just at the people who live in the country itself, but also at citizens abroad. Important demographic support comes from people who have left their homeland but continue to support their loved ones through the power of cheap and accessible remittances.

References

Tohoff L., Landis D., Mencarini L., Aassve A. (2024) Remittances-Adjusted Support Ratio, *Population and Development Review* (online first), https://doi.org/10.1111/padr.12627