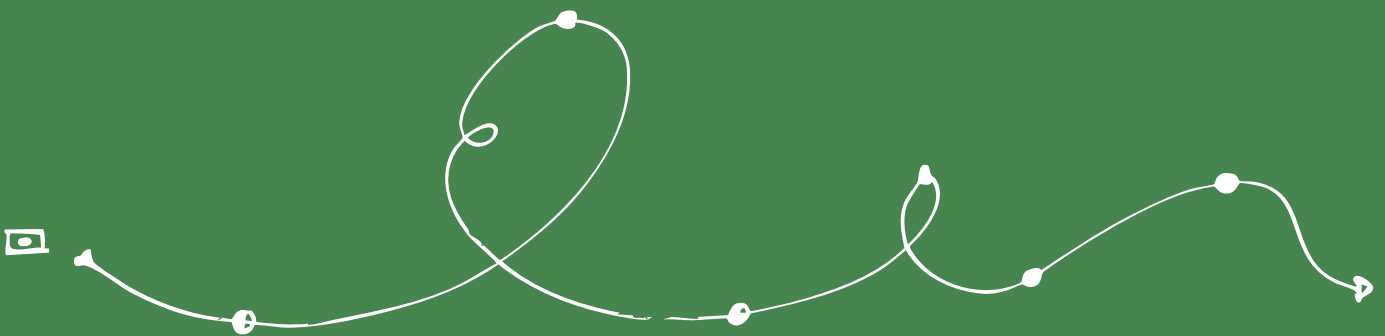


The Missing Link: Remittances & Socially Trusted Financial Intermediation as Key Element for Addressing Root Causes of Migration.



By Raúl Hinojosa-Ojeda, Roberto Valdovinos Alba, Isabel Cruz Hernández, Yvonne Su



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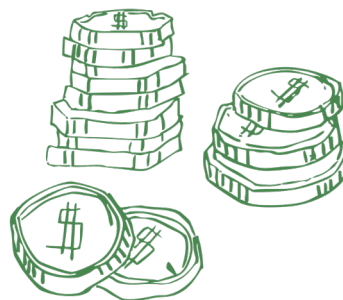
MEXICO

Abstract

This paper argues that properly intermediated remittances represent a critical yet underutilized resource for addressing the root causes of migration. Current public policies have largely overlooked the potential of community-based financial institutions, when combined with fintech infrastructure, to channel remittances into sustainable local development in rural, remittance-dependent regions. In the absence of robust financial intermediation, cash-based inflows often trigger localized inflation, weaken the competitiveness of productive sectors, and entrench economic dependence on migration, what we call the vicious cycle of remittances. By contrast, when remittances are directed through socially trusted financial institutions, they can be mobilized into savings, credit, and investment, fueling entrepreneurship, employment, and community development, what we call the virtuous cycle of remittances. Drawing on empirical evidence and international experiences, particularly from rural

Mexico and Central America, this paper sets out actionable policy recommendations across regulatory, technological, and social dimensions, advocating a dual framework of fintech innovation and socially trusted financial intermediation as a cost-effective pathway to development. In particular, we highlight the strategic complementarity between fintech innovations, which provide efficiency and infrastructure, and community-based financial institutions, which contribute local trust, advisory services, and accountability. Harnessing remittances through this dual approach offers one of the most cost-effective pathways to sustainable development and reduced migration pressures.

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I. Introduction: Remittances and Socially Trusted Financial Intermediation.

2



“Remittances are not a guaranteed engine of development: their impact is mediated by the strength of local institutions and, in particular, by the quality of financial intermediation.”

Migrant remittances are a principal source of capital for migrant-sending regions throughout the globe. In this paper, we focus on the case of rural areas of Mexico, Guatemala, El Salvador, and Honduras, four neighbouring countries that epitomize comparable structures of migrant-sending, remittance-recipient regions that can help us identify key policy changes that could allow governments and organizations to promote regional sustainable development. For these four countries, the worth of remittances currently amounts to up to a quarter of GDP and several times the amount of foreign direct investment (FDI). What’s more, in contrast to FDI, the value of remittances hasn’t stopped growing over the last few decades (see Figure 1). At the micro level, remittances are an invaluable aid to families and communities. At the macro level, they offer much-needed foreign currency to low to mid-income countries that would otherwise be left without means of paying for goods abroad. In absolute terms, remittances represent a vital asset for receiving countries.

Literature on remittances’ contribution to local development is abundant. Yang (2008), for example, demonstrates empirically that financial ‘shocks’ increasing the value of remittances received by households (such as a favorable exchange-rate shift) significantly increase investments in entrepreneurship and human capital. Yang’s findings demonstrate the potential of remittances for local investment, but also imply that the productive potential of remittances could be amplified through effective financial channels that facilitate savings and investment decisions. ¹

Figure 1. Absolute value of remittances, GDP and FDI (billion USD)

	2014			2024			2014-2024 growth rate		
	Remittances	Foreign Direct Investment	GDP	Remittances	Foreign Direct Investment	GDP	Remittances	Foreign Direct Investment	GDP
El Salvador	4.14	.31	22.59	8.48	0.64	35.36	104.56%	108.76%	56.53%
Guatemala	5.54	1.44	57.85	21.51	1.69	113.20	287.98%	17.34%	95.67%
Honduras	3.44	1.42	19.76	9.74	0.99	37.09	183.46%	-29.88%	87.75%
Mexico	24.40	22.84	1,364.51	64.75	32.03	1,852.72	165.37%	40.24%	35.78%
TOTAL	37.52	26.01	1,464.71	104.48	35.36	2,038.38	178.47%	35.95%	39.27%

Note: Data collected by the authors from the Bank of Mexico, the World Bank, and SECMA.



Similarly, Adams (2011), drawing from household survey data, reviews extensive micro-economic evidence showing that remittances consistently reduce poverty and stimulate household consumption, but finds varied results on productive investment with long-term impact. This indicates that local institutional contexts, including the quality and availability of financial infrastructure, significantly influence these outcomes.

Experimental household-level evidence supports this view: Ashraf, Aycinena, Martínez, and Yang (2015) show that improving access to bank accounts significantly increases remittance savings, thus bridging flows to productive uses. At the same time, macro-level studies emphasize the role of institutions: Giuliano and Ruiz-Arranz (2009) and Aggarwal, Demirgüç-Kunt, and Martínez Pería (2011) show across countries that remittances act more as substitutes than catalysts for local investment where financial systems are underdeveloped. More recently, Alhassan, Maswana, and Inaba (2025) find that remittances spur entrepreneurship only in countries with stronger financial intermediation.

¹ While this paper considers the case of local investment resulting from household remittances and financial intermediation, there is another form of binational investment that, although out of the scope of this research, the reader should have in mind: broader diaspora investment mechanisms that channel funds into structured financial instruments and organizations in the country of origin. For example, Gelb et al. (2021) have defined diaspora investment as asset-producing transactions, such as equity, loans, or bonds, which differ fundamentally from interpersonal remittance flows. Their worldwide review identified over 300 diaspora finance initiatives worldwide, demonstrating that migrants and their descendants are often eager to fund productive projects in their home communities, ranging from direct support for small local businesses, infrastructure, and community-led initiatives, to more structured investments through equity, loans, and diaspora bonds. While diaspora investment should not be confused with remittances, they both speak about the need for effective financial channels to amplify the positive impact of funds transferred to migrants' communities of origin.

Recent cross-country research has reinforced these views. A global meta-analysis by Cazachevici, Havranek, and Horvath (2020), synthesizing nearly 100 studies, finds that the average growth impact of remittances is generally positive, with effects highly dependent on country context—stronger in low-income economies with better financial systems and weaker where institutions remain fragile. Similarly, Eggoh, Bangaké, and Semedo (2019), analyzing over four decades of data across developing countries, show that while remittances do not consistently spur short-run growth, their long-run impact becomes significant when accompanied by financial development, underscoring the central role of financial intermediation. Complementing these findings, Ekanayake and Moslares (2020) show for Latin American countries that remittances can reduce poverty, but that their impact on economic growth depends on structural conditions that allow transfers to be transformed into productive investment, such as the presence of financial infrastructure.

capacity to foster sustained development. In other words, remittances are not a guaranteed engine of development: their impact is mediated by the strength of local institutions and, in particular, by the quality of financial intermediation.

On the basis of these views, it may seem reasonable to assume that access to financial intermediation would have become a priority for remittance-receiving countries, so that remittances' positive impact can have long-term impact. However, many rural regions in Mexico and Central America lack the financial intermediation that could amplify that positive effect. That is, they do not have a financial institution in which inhabitants could open accounts and keep their savings. For instance, for every 100,000 inhabitants, there are only 14.1 points of access to financial services in Mexico (see Figure 2). This ultimately means that remittance-receiving households in most regions have no alternative but to receive their remittances in cash.

Taken together, these diverse studies reinforce Adams's early insight, emphasizing that it is not remittances *per se* but the quality and accessibility of financial intermediation that determine their

4

Figure 2. Financial services access points & distribution of access points (%)

	Mexico*	EL Salvador**	Guatemala***	Honduras*
Financial Infrastructure Access Points per 10,000 adults	14.1	6.8	49.4	28
Distribution of Financial Access Points (% of total)				
Bank Branch or Teller	13.1	10.28	4.97	13.07
ATMs	48.47	39.26	7.61	10.85
Merchant partners	38.46	46.46	87.43	75.46
Others		4.0		0.62

* Mexico & Honduras data is from 2023
 ** El Salvador data is from 2021
 *** Guatemala data is from 2024
 Note: Authors' compilation of data from national bank regulation entities in Mexico, El Salvador, Guatemala, and Honduras.

Without financial intermediation, cash remittances cannot be converted into savings deposited in financial institutions. Instead, the liquidity of remittances is pulverized into individual recipients. This situation prevents the use of remittance related savings for local lending and investment. For example, eastern El Salvador, the poorest region of the country, receives 32 percent of all remittances to El Salvador, but it lacks the financial institutions that would enable those resources to foster the region's development.

Moreover, it's not only financial intermediation in general that is needed, but rather a specific kind of financial intermediation. Indeed, when only commercial banks are present in a region, the positive impact of remittances through savings and investment is narrowed by the fact that most of their lending capital is directed towards more efficient metropolitan investment opportunities rather than small, marginalized rural credits. This partially explains why commercial banks in small regions are used by families only for cashing out remittances rather than depositing them into accounts. Therefore, it's not only financial intermediation that's required: small, rural regions need financial intermediation by *socially trusted* financial institutions, that is, financial institutions that are locally trusted and willing to lend and invest in that specific region and at reasonable interest rates.

In this paper, *socially trusted financial intermediation* will refer specifically to financial institutions that (1) are deeply embedded in their communities through participatory governance or cooperative ownership, (2) maintain transparent financial practices and moderate, clearly disclosed interest rates,

(3) and explicitly mandate that deposited funds be lent or invested locally, and (4) provide personal advisory services to ensure loans are productive and repayable. This excludes predatory microfinance institutions characterized by opaque practices, excessive interest rates, and minimal engagement with local community needs.

Important literature supports the argument that financial institutions play a critical role in converting remittances into sustainable local investments. Microfinance institution (MFI) studies show that moving flows into regulated rails and embedding them in local institutions enables bundling with savings and credit products, amplifying community-level investment (Hernández-Coss, 2005; Orozco & Hamilton, 2006). At the household level, evidence from El Salvador and Mexico shows that remittance receipt raises account ownership, formal saving, and even formal borrowing, directly tying transfers to investable funds (Anzoategui, Demirgüç-Kunt & Martínez Pería, 2014; Ambrosius & Cuecuecha, 2016).

Others have made the same argument specifically for socially trusted financial institutions. Banerjee and Duflo (2011) underline the necessity of trust-based, personalized financial intermediation for poverty alleviation. Morduch (2020) synthesizes empirical research to show that microfinance institutions explicitly committed to social goals and local community involvement outperform commercial or purely profit-driven institutions, reinforcing our argument in favor of socially trusted financial intermediation as critical for sustainable development.

Figure 3. Remittance payout locations by categories (%). 2024

	Bank Account Remittances **	Cash Remittances ***	Money Orders & Hand-carried remittances	Others
Mexico	35.28	50.77	0	13.95
EL Salvador	21.97	68.31	0	9.89
Guatemala*	6.68	89.26	1.90	2.16
Honduras	7.0	87.7	0.4	4.7

* Guatemala data from 2022

** Bank Account Remittances refer to all remittances received in bank accounts or debit cards of the final recipients.

*** Cash Remittances refers to all remittances paid in cash, including those received in cash at bank branches and other payout locations, such as stores, drugstores, and other establishments that have partnerships with remittance companies (MTOs).

Note: Authors' compilation of data from national bank regulation entities in Mexico, El Salvador, Guatemala, and Honduras.

Empirical evidence from successful socially oriented microfinance institutions, such as those belonging to the AMUCSS² network (whose Bono Migrante program mobilized migrant savings into productive local investments), supports the argument that trust-based advisory services significantly sustain financial inclusion, enhance productive outcomes, and

even credit repayment (AMUCSS reports repayment rates above 95%). Similar international cases, like the Bangladesh Rural Advancement Committee (BRAC) and Grameen Bank (microfinance pioneer in Bangladesh), further confirm these outcomes (Banerjee & Duflo, 2011).

² See textbox below for more information on the Asociación Mexicana de Uniones de Crédito del Sector Social (AMUCSS) case study, illustrating how socially trusted financial intermediation concretely translates into sustainable local development.

Textbox 1

Intermediation in Latin America

Socially trusted financial institutions are community-oriented financial entities deeply embedded within local societies. In Latin America, these institutions typically take the form of savings cooperatives (SOCAP), community banks (SOFINCO), credit unions, or similar entities. Regulated under frameworks designed explicitly to facilitate community-based, non-commercial financial services, these institutions prioritize transparency, moderate interest rates, local reinvestment, and personalized advisory services. Their governance often includes local community participation, ensuring that their financial activities align closely with community needs and objectives.

A prominent example in Mexico is the Asociación Mexicana de Uniones de Crédito del Sector Social (AMUCSS), a nonprofit network founded in 1992. AMUCSS provides tailored financial services to marginalized rural communities traditionally excluded from formal banking. Its network, consisting of over 100 community-owned institutions, manages more than 200,000 accounts. AMUCSS successfully channels migrant savings into productive local investments through innovative programs like Bono Migrante, a high-yield bond that directly finances agriculture, small enterprises, and infrastructure projects. Supported by personalized advisory services, AMUCSS achieves repayment rates above 95%, highlighting its significant impact on local sustainable development.

In Guatemala, Red Fasco (Red Financiera de Asociaciones Comunitarias) exemplifies socially trusted intermediation. Comprising rural cooperatives and community banks, Red Fasco facilitates local financial services tailored to indigenous and rural populations. The network emphasizes financial literacy and personalized advisory, enabling remittance recipients and local entrepreneurs to leverage financial resources for productive purposes, including agriculture, small businesses, and infrastructure. Red Fasco thus plays a crucial role in fostering local economic growth and reducing poverty.

Honduras hosts Red Katalisis, a pioneering network of socially oriented microfinance institutions established in 2002. Red Katalisis operates mainly through savings and credit cooperatives and community-based financial organizations. The network promotes local development by providing financial inclusion, credit access, and financial education tailored to the needs of marginalized communities. Its emphasis on community governance and transparent operations has built significant local trust, ensuring remittances and diaspora investments are effectively channeled into sustainable, productive local initiatives.

Collectively, AMUCSS, Red Fasco, and Red Katalisis illustrate how socially trusted financial intermediation transforms remittance flows into powerful tools for community-driven sustainable development, thereby addressing fundamental economic pressures that drive migration.

In this paper, we argue that the potential of remittances for fostering the development of receiving regions is hindered by the absence of socially trusted financial intermediation, to the point that in some respect we can consider such forgone potential harmful to long-term sustainable development, in spite of remittances' value and continual growth. We refer to this adverse scenario as the *cash remittance vicious cycle*.

After describing how this vicious cycle occurs in rural regions of Mexico and Central America, we'll

focus on how socially trusted financial intermediation can instead promote a *virtuous cycle* of remittances that fosters local development. The paper concludes by addressing in some detail the main policies required for the transition from a vicious cycle to a virtuous cycle of remittances, enabling governments, fintech companies, and societies, in general, to fully leverage the potential of remittances for sustainable development and address the root causes of migration.

II. The Vicious Cycle of Cash Remittances

For receiving countries, remittances are an essential component of households' economies and the predominant source of foreign currency for national economies. Yet, their long-term effects on rural regions often result in limited sustainable development, increasing dependency on remittances, and rising levels of out-migration, sometimes even leading to the depopulation of rural communities. These pernicious consequences are the result of the scarcity of local financial intermediation and the excess of cash remittances, both of which are central elements in the vicious cycle of cash remittances³.

For migrants in the United States and other countries with comparable levels of immigration, being undocumented means that financial inclusion will be expensive because of the need for highly commissioned intermediaries. That explains why less than half of undocumented immigrants have access to banking services⁴. This, in turn, raises the cost of payroll cashing and sending cash remittances at retail stores, which

results in lower standards of living and lower value remittances for family members in the receiving country.

Then, given the absence of financial intermediation in Mexico and Central America's rural regions, large cash remittance flows arrive in communities and are not converted into savings or investments; instead, they remain in cash, intended to be spent quickly. Through a phenomenon analogous to the Dutch disease⁵, but occurring at a local or microeconomic level, large injections of cash into these communities trigger localized inflation. Inflation from large remittance inflows reduces the competitiveness of local productive sectors such as agriculture and manufacturing, making local goods relatively expensive compared to those produced elsewhere. While initially increased consumption from remittances boosts local employment temporarily (mainly in services and retail), sustained inflation and reduced competitiveness structurally weaken the local productive sectors⁶.

7

3 Although out of scope, it must be noted that the vicious cycle begins with the lack of legal status of millions of immigrants in the United States and other countries with comparable levels of immigration: undocumented workers are often paid below legal standards, which increases demand for inexpensive labor. At the same time, the higher demand for cheap labor attracts additional unauthorized migration from low-income countries that lack economic opportunities for a portion of their populations.

4 FDIC (Federal Deposit Insurance Corporation) regularly publishes data on banking access and financial inclusion among U.S. households, but typically does not distinguish explicitly by documentation status due to sensitivity and privacy. Hall and Greenman (2015) consider less than 47% of undocumented migrants were banked (meaning they possess a checking or savings account).

5 See textbox below, in which we briefly review the original macroeconomic definition of Dutch Disease and clearly outline our adaptation to a microeconomic scenario.

6 Acosta, Lartey, and Mandelman (2009) offer empirical support at the national macroeconomic level, demonstrating that large remittance inflows can generate Dutch disease effects, appreciating the national currency and harming the export sector. While their macroeconomic perspective does not explicitly address the local or community-level impacts of cash remittances, their findings broadly support our analogy that sustained large remittance inflows can create structural economic distortions.

Over the longer term, this undermines stable employment opportunities, reduces local productivity, and increases dependence on continuous remittance inflows, thus perpetuating outmigration. The absence of job opportunities motivates members of the communities to follow the example of those who have departed and to become migrants themselves, which further narrows labor availability in rural regions of Mexico and Central America.

Also, the sudden split between those who receive remittances and those who don't introduces new forms of inequality that disrupt the social fabric and could therefore contribute to new forms of violence and crime.

To sum up, the remittances' Dutch disease process we just described is as follows:

1. Cash remittance inflows rapidly increase local liquidity.
2. Increased liquidity causes localized inflation (higher prices of goods and services).
3. Inflation reduces the competitiveness of local products relative to other regions, thereby diminishing long-term demand for local labor.
4. Labor market distortions occur as incentives shift from local employment toward migration.
5. Resulting economic stagnation creates dependency on further remittances, perpetuating migration.

“Remittance-dependent communities can become trapped in a cycle where economic stagnation, population decline, and ongoing migration reinforce one another.”

8

Essentially, remittance-dependent communities can become trapped in a cycle where economic stagnation, population decline, and ongoing migration reinforce one another. In long-standing sending regions of Zacatecas, for example, village-level ethnography documents aging and shrinking populations, limited local employment, and heavy reliance on U.S. earnings among households: symptoms of demographic decline and hollowing out despite substantial remittance inflows (Jones, 2009). In rural Jalisco, detailed architectural and ethnographic work shows that remittance-financed house-building transformed the built environment yet often yielded under-occupied or seasonally vacant homes and weak local multipliers, underscoring how consumption-oriented uses of remittances may fail to generate durable productive capacity (López, 2010, 2015).

At the municipal level, studies of collective remittances (through hometown associations) show that in very small localities these funds can rival—or even exceed—public-works budgets, creating fiscal dependence and volatility rather than broad-based economic diversification when flows slow (Orozco & Lapointe, 2004; Orozco & García-Zanello, 2009). These patterns align with macro-evidence that remittance dependence can produce a “remittance trap,” wherein incentives for self-sustaining growth weaken absent effective intermediation into savings and investment (Chami et al., 2018). Taken together, the micro- and meso-level evidence is consistent with a local remittance Dutch disease dynamic unless remittances are intermediated into productive uses.



Dutch Disease

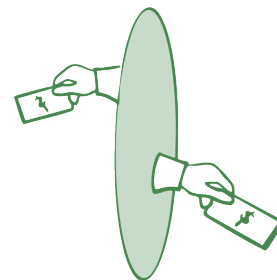
The term “Dutch disease” was first coined in the 1970s to explain the economic crisis that followed the Netherlands’ 1959 discovery of extensive natural gas fields. This discovery caused a sharp increase in foreign currency inflows, leading to rapid appreciation of the Dutch guilder. Consequently, Dutch manufactured exports became less competitive internationally, shrinking the manufacturing sector and causing widespread unemployment. Economists currently apply the term more broadly to describe situations where significant inflows of foreign currency appreciate the local currency, adversely impacting other economic sectors, particularly export-oriented industries.

In this paper, we use the term “remittances’ Dutch disease” by analogy, adapted to describe the microeconomic effects at the local level caused by large, continuous inflows of cash remittances. Unlike the traditional macroeconomic concept, the mechanism here is not currency appreciation affecting exports, but rather local-level inflation, distorted labor markets, and decreased incentives for productive economic activity. The mechanism of “remittances’ Dutch disease” thus operates differently from the classic macroeconomic concept. Rather than currency appreciation affecting exports, remittance inflows rapidly increase local liquidity, inflating prices for goods and services, and reducing local competitiveness. These price increases discourage productive local investment and employment, ultimately exacerbating dependence on migration and remittance income, creating a persistent vicious cycle.

For an example of a macroeconomic analysis of remittances and Dutch disease, see Acosta, P. A., Lartey, E. K. K., & Mandelman, F. S. (2009), who similarly adapted the Dutch disease concept to explain regional distortions and inflationary pressures created by remittance flows.



III. The Virtuous Cycle of Remittances



“By introducing socially trusted financial intermediation, communities can become more sustainable and less dependent on remittances.”

10 Now we'll describe the opposite scenario, where socially trusted financial intermediation and other conditions are met, allowing the community to capitalize on the potential of remittances for sustainable development.

In this new scenario⁷, documented and undocumented immigrants in the United States and other countries with comparable immigration rates have access to efficient, low-cost financial services. This improves their economic situation and increases the average value of remittances, benefitting receiving households.

On the recipient country side, socially trusted financial institutions are now present in most rural regions. These local financial institutions also have at least the minimal technological and operational capability, theirs or through fintech services' aggregators, required for connecting to the fastest payment systems. Remittances are therefore now transferred directly into households' saving accounts, rather than cashed out through expensive intermediaries.

The fact that remittances are credited directly into savings accounts tempers the rate of spending of the remittance: part of that capital would remain in the socially trusted financial institution as savings, at least for some time, before being spent as usual on food, clothes, health, and education; another smaller part of the remittance would remain as monthly savings. Thus, instead of keeping capital out of circulation until spent as in cash remittances (saved “under the mattress” for months or years), the capital is injected into socially trusted financial institutions as savings, no matter if for some days or several months. This, in turn, allows those entities to lend and invest in a larger number of local productive and infrastructure projects that entail new job opportunities and sustainable development.

Nevertheless, if there isn't enough local demand for loans and investments, a financial institution that receives remittances in its accounts could end up with a capital surplus that carries with it a considerable financial burden. That problem is solved if socially trusted financial institutions are not isolated, but rather work in larger networks of similar institutions. Then, a financial institution with a capital surplus would lend that surplus to other financial institutions in the same network which are in need of additional capital to cover their excess lending demand. The regional dynamics of lending and investing between socially trusted financial institutions would enable marginalized communities to thrive modestly but consistently, without the risk of an excess of capital.

⁷ Although out of the scope of this paper, it must be noted that the virtuous cycle should begin with the implementation of some sort of immigration or labor reform that would regularize the work status of remittance-sending immigrants in the United States, meant to facilitate access to financial services by immigrants and to reduce the artificial divide between cheap undocumented labor and more expensive legal labor, which itself fosters immigration. This would eliminate the cost advantage of undocumented wages and thus contribute to cutting down immigration.

That's something that several socially trusted financial institutions have implemented for years, such as the small entity Ixpantepec Nieves in the Mexican State of Oaxaca, whose inhabitants migrated long ago to California. All along the year 2024, Ixpantepec Nieves was able to reinvest locally 7.5% of the total value of remittances it received in the same period. Thankfully, that small rural bank is part of a larger network called SMB Contigo, itself part of AMUCSS, thanks to which it was able to lend its capital surplus to different financial institutions in Oaxaca and other states with higher demand for credit. By working in such a network, the positive impact of socially trusted financial institutions can become exponential.

Similarly, the split between those who receive remittances and those who don't would be mitigated by the fact that financial intermediation and lending power would benefit the whole community, not just remittance-receiving households: all members of the community, in principle, would have access to credit, without any consideration to whether they have family members sending them remittances from abroad or not. This, in turn, would strengthen the social fabric by reducing inequality, which could have a positive impact on local social tensions and even mitigate crime rates—were we to take for granted the causal relationship between social inequality and violence.

Moreover, financial institutions' lending capacity would allow potential local microentrepreneurs to thrive, regardless of their relationship with migrating community members. It is worth noting that non-migrating inhabitants (those who remain) tend to have a better understanding of local commercial and business opportunities. This positive impact would be further enhanced if financial institutions were to offer additional financial products beyond savings, such as investment bonds for migrants abroad, which would increase the financial institutions' lending capacity even more.

As a consequence, the virtuous cycle of remittances would help reduce the economic pressures that force migration. By fostering local, sustainable development, providing stable employment, and increasing local economic opportunities, the virtuous cycle diminishes dependency on migration and remittances as an economic survival strategy, which is likely to lower migration rates over time.

In short, by introducing socially trusted financial intermediation with the technological capability to interconnect with efficient remittance channels, communities can become more sustainable and less dependent on remittances. Remittances' Dutch disease would still happen, but to a lesser degree. Communities receiving large amounts of remittances through socially trusted financial intermediation enter a virtuous cycle that fosters development and contributes to tackling the root causes of migration. That is what we call the virtuous cycle of remittances.

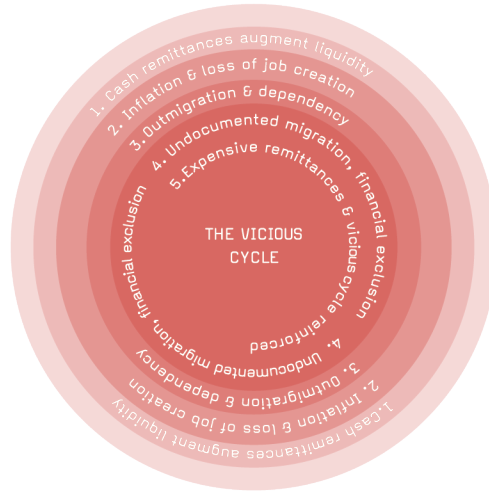


VICIOUS CYCLE OF CASH VS VIRTUOUS CYCLE

Figure 4. Vicious and virtuous cycles

12

VICIOUS CYCLE OF CASH REMITTANCES WITHOUT FINANCIAL INTERMEDIATION
 CYCLE FEEDS BACK INTO GREATER RELIANCE ON CASH REMITTANCES.



CASH REMITTANCES
NO INTERMEDIARY

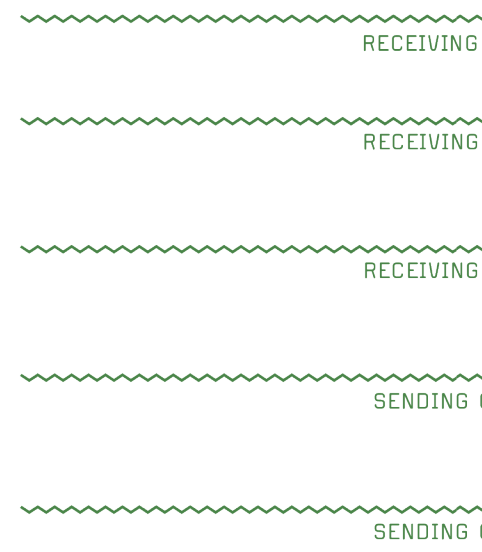
- 1.- Cash remittances augment liquidity**
Cash remittances inflows
Liquidity surge
- 2.- Inflation & loss of job creation**
Regional inflation
Loss of competitiveness
Weak job creation
- 3.-Outmigration & dependency**
Inequality/social fragmentation
Outmigration, less labor supply
Dependency on remittances
- 4.-Undocumented migration, financial exclusion**
More undocumented migrants
Low access to financial services
High-cost cash remittances
- 5.-Expensive remittances & vicious cycle reinforced**
Less income for recipients
Cash-based cycle reinforced

Interrupting the vicious cycle

The Miss



SOCI
TRUS
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transforming remittances from a cycle

through public policies

Link

SOCIALLY
INTERMEDIATED
FINANCIAL
MEDIATION



COUNTRY

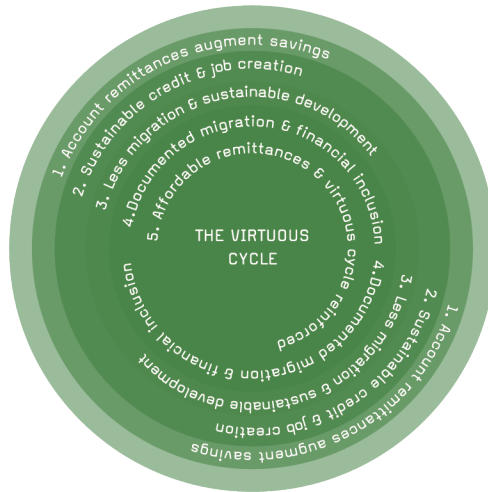
COUNTRY

COUNTRY

COUNTRY

COUNTRY

of dependency into a cycle of growth



ACCOUNT BASED REMITTANCES
SOCIALLY- INTERMEDIATION

1.-Account remittances augment savings

Remittances to local accounts
Funds pooled as savings

2.-Sustainable credit & job creation

Stable consumption, lower inflation
Capital converted into local credit
Business growth & job creation

3.- Less migration & sustainable development

Benefits beyond recipient households
Reduced outmigration pressures
Higher income, less dependency

4.- Documented migration, financial inclusion

Documented migrations
Migrants gain financial inclusion
Safer transfers, lower costs

5.-Affordable remittances & virtuous cycle reinforced

Higher remittance value transferred
Productive remittances' cycle reinforced

VIRTUOUS CYCLE OF SOCIALLY- INTERMEDIATED REMITTANCES
CYCLE REINFORCES ACCOUNT-BASED REMITTANCES WITH INTERMEDIATION.

IV. Addressing Potential Critiques

“The virtuous/vicious dichotomy is less about portraying a simplified reality than about signaling clear policy pathways.”

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The scenario outlined above should lead to concrete policy strategies that would enable remittance-receiving countries to fully benefit from the potential of remittances. Before proceeding, however, several significant critiques warrant explicit attention.

Some critics quoted in the first section of this paper have argued that remittances rarely translate into sustained productive investments, typically being directed toward immediate consumption or status-related goods, resulting in limited long-term economic growth (e.g., Chami et al., 2005; Adams, 2011). This would contradict our intention to consider remittances as a primary driver of sustainable development in rural regions.

While it is indeed true that remittances often initially boost consumption, this paper argues that the main obstacle is not inherent in remittances themselves but in the absence of appropriate financial intermediation. Evidence from socially trusted financial institutions, such as AMUCSS in Mexico, demonstrates that with effective intermediation, significant portions of remittance flows can and do generate sustained productive investments, local employment, and enduring development. Thus, the challenge lies not in remittances *per se*, but in how effectively these

resources are locally managed. In other words, critics accurately describe what we term the vicious cycle of remittances. Yet, our argument stresses that appropriate technological and institutional transformations can turn these flows into powerful drivers of sustainable economic growth: the virtuous cycle of remittances.

Moreover, experts with extensive experience in migration issues emphasize that financial mechanisms alone are insufficient to resolve the deeper structural drivers of migration, such as immigration status, labor rights, governance quality, and corruption (Orozco, 2018; Clemens & Gough, 2018).

We fully agree that comprehensive immigration, labor, and governance reforms are vital for sustainably addressing the root causes of migration. However, promoting financial intermediation, and socially trusted financial intermediation in particular, represents a practical and immediately actionable strategy for improving the developmental impacts of existing remittance flows. It provides a politically feasible and concrete mechanism to enhance local economic outcomes rapidly, complementing broader policy initiatives. Therefore, financial intermediation is not a standalone solution but an essential component of a wider strategy for development.

Furthermore, advocates of fintech solutions could argue that entirely digital platforms (e.g., neobanks, digital wallets, blockchain-based remittance networks) offer cheaper, more scalable, and more efficient solutions than traditional or community-based intermediaries. From their perspective, investing in local community financial institutions appears redundant when digital solutions can efficiently serve entire regions.

In response, we acknowledge the clear advantages of fintech innovations, including efficiency, speed, and lower costs. Yet, purely digital solutions encounter critical barriers in rural and marginalized communities: digital literacy gaps, limited connectivity, and the (often justified) lack of local trust and familiarity. Without on-the-ground knowledge of local conditions, digital-only platforms struggle to channel resources effectively into sustained community-based investments. Socially trusted financial institutions can bridge these gaps, complementing fintech's strengths with digital financial literacy programs, personalized advisory, community trust, and local accountability. On the other hand, the use of fintech infrastructure and channels is a key element for socially trusted financial institutions to connect with remittance channels and offer efficient and innovative financial services to their account holders (specially if those local financial institutions have a say on the technological models and use cases that are proposed to their clients, so that these tools can be adapted to local contexts and idiosyncrasies). Thus, fintech and socially trusted institutions should be considered complements, not substitutes.

Finally, we must recognize that framing remittance dynamics as a strict opposition between “vicious” and “virtuous” cycles can appear overly binary. In practice, both positive and negative effects of remittances often coexist, even within the same community. Our intention is not to suggest that financial intermediation magically eliminates all risks, but rather to highlight the direction in which public policy and institutional design can tilt the balance of outcomes. The “cycle” framing serves as a heuristic device to clarify how different institutional settings amplify either the developmental or dependency effects of remittances. Seen in this way, the virtuous/vicious dichotomy is less about portraying a simplified reality than about signaling clear policy pathways: strengthening socially trusted financial intermediation increases the likelihood that remittances foster savings, credit, and investment, while weak intermediation leaves communities more vulnerable to the downsides of cash-based dependence. By acknowledging this nuance, we emphasize that our argument is not that only two possible futures exist, but that governments and societies have a policy choice about which set of dynamics they should reinforce.

With these critiques acknowledged, the argument remains: remittances alone are not inherently virtuous or vicious; rather, their developmental impact depends on the financial and institutional frameworks that mediate them. We can now proceed to outline some of the key policy reforms that can foster remittances' potential as a motor of sustainable development.

V. Regulatory, Technological, and Social Progression towards the Virtuous Cycle

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Transitioning to the virtuous cycle of remittances requires simultaneous progress in three intertwined dimensions: regulatory frameworks, technological innovation, and social structures. Important developments have occurred in each of these areas over recent decades, significantly advancing the potential of remittance-receiving countries to harness remittances for sustainable local development.

On the regulatory front, critical reforms since the late 20th century have facilitated the emergence of community-based financial institutions across Latin America, including savings cooperatives, credit unions, and similar entities that provide microcredits to small communities. In some cases, those entities have evolved into well-constructed networks of microbanks that represent marginalized communities, such as AMUCSS in Mexico, Red Fasco in Guatemala, or Red Katalisis in Honduras. These pioneers demonstrate that financial institutions in rural, marginalized regions can be sustainable and have a significant impact on their respective regions.

However, regulatory frameworks remain incomplete, particularly concerning the ability of smaller, socially trusted institutions to access national and international payment systems, meet compliance requirements, and efficiently process digital transactions. Continued

regulatory reforms are crucial to ensure that small institutions are not left behind in the digital transition.

On the social front, binational organizations have evolved similarly. From the precarious *mutualista* associations of migrants first described in the 1920s by anthropologist Manuel Gamio (Gamio, 1931) to hometown associations of migrants starting in the 1970s, the trend has always been towards more complex binational dynamics. Hometown associations have traditionally been responsible for managing binational investment programs and implementing cultural and political strategies for their regions of origin. Today, with the advent of social networks and instant messaging platforms, these groups are ripe for new technological solutions and investment ecosystems that aim to produce sustainable development in their regions, such as crowdfunding investments and digitally managed investment accounts.

As for technological advancement, money orders were the most common method for sending remittances still in the 1990s, but became obsolete by the 2010s, replaced by electronic transactions initiated mainly at retail stores, which were safer, cheaper, and faster. Similarly, the apparition of cellphones and digital wallets, which have now become mainstream, is likely to transform the way people send and

“Fintech and socially trusted institutions should be considered complements, not substitutes.”

receive remittances: from using hefty-commission retail stores to send and cash out remittances, to using safer and cheaper Wallet-to-Wallet systems to transfer and receive real-time remittances through their phones. Many financial institutions, including small, rural ones, are at the brink of a new model, integrating P2P technologies for both local payments and cross-border remittances that have the potential of lowering costs and hastening the process towards account-to-account transfers.

These policy changes call for a new approach that integrates fintech and social finance in a complementary relationship. Recent fintech innovations, such as mobile wallets, digital banking apps, and real-time remittance transfers via innovative protocols like Interledger, provide faster, cheaper, and safer alternatives to traditional cash-based methods. Yet, fintech solutions alone cannot fully resolve the structural problems of financial inclusion in marginalized, rural communities. Digital literacy gaps, limited connectivity, and the essential need for personalized financial advisory and local trust remain barriers that digital-only institutions struggle to overcome. Thus, as mentioned earlier, fintech and socially trusted financial institutions must operate in a complementary manner: fintech solutions providing efficient infrastructure and transparency, while socially

trusted institutions ensure personalized advisory services, local accountability, and community-driven investment.

Bridging the digital divide expanding rural connectivity, enhancing digital literacy, and fostering trust in digital tools requires coordinated policy efforts involving governments, local communities, and private fintech providers. The practical experience of People's Clearinghouse, a high-performance payment switch that connects financial institutions between themselves and with remittance channels, highlights exactly how innovative technological platforms, combined with trusted community financial institutions, can help regions transition into a virtuous cycle of remittance-driven development⁸.

This progress in regulatory, technological, and social structures makes it easier for societies to transition to the virtuous cycle of remittances through socially trusted financial intermediation. In the next section, we'll address the most urgent policies needed for that transition.

8 See textbox below on People's Clearinghouse, which intends to illustrate how fintech platforms combined with local institutions can drive a successful transition to the virtuous cycle.

Figure 5. Progress towards the virtuous cycle

	STAGE 1 (PAST)	STAGE 2 (PRESENT)	STAGE 3 (EMERGING)
SOCIAL PERSPECTIVE	Mutualist migrant associations (1920s)	Hometown Associations (migrant clubs and federations since 1970s)	Digital binational networks, crowdfunding, and digitally managed investment for communities
TECHNOLOGICAL PERSPECTIVE	Money orders	Electronic transaction via retailers and Money Transfer Operators (MTOs)	Real-time Wallet-to-Wallet remittances, digital wallets, fintech apps, blockchain-based remittance platforms, and Central Banks cross-border systems
REGULATORY PERSPECTIVE	Isolated government initiatives (migrant bonds, national banks)	Popular savings and credit laws enabling microfinance networks (AMUCSS in Mexico, Red Fasco in Guatemala, Red Katalisis in Honduras)	Updated regulatory frameworks for second-floor social banks, cross-border account opening, standardized digital onboarding, binational payment integrations (e.g., FedGlobal, People's Clearinghouse)

18 People's Clearinghouse and the Interledger Protocol

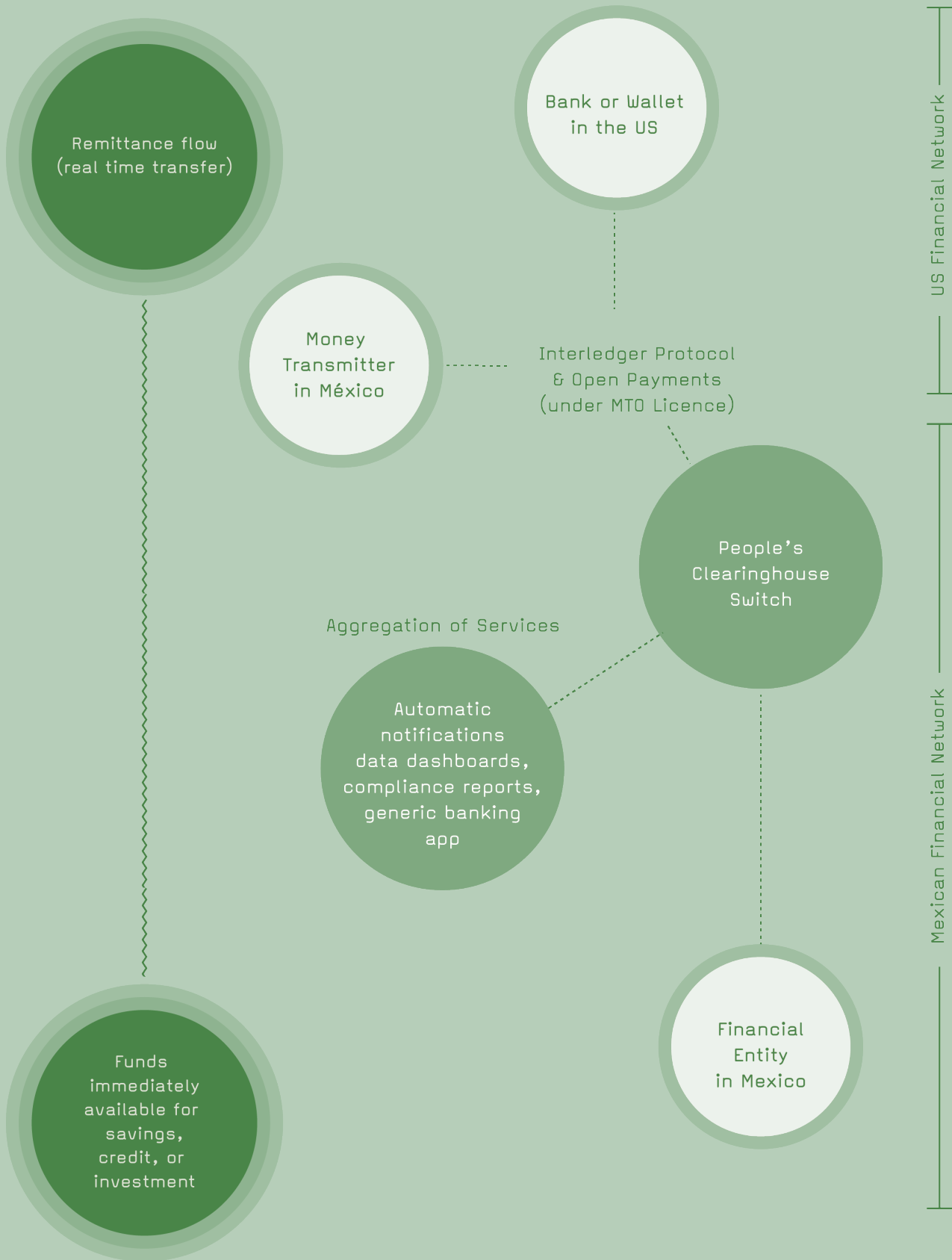
Traditional methods of sending remittances are costly, slow, and often opaque, limiting their potential for promoting local development. In response, new technologies have emerged, such as the Interledger Protocol, and innovative financial infrastructures, like the People's Clearinghouse.

The Interledger Protocol (ILP) is an open-source protocol that facilitates instant, secure, and cost-effective cross-border financial transactions by connecting various payment systems. Instead of requiring senders and recipients to share the same financial infrastructure, ILP allows seamless and transparent transfers across banks, digital wallets, and mobile payment services, significantly lowering the cost and increasing the speed and transparency of remittance flows.

Leveraging Interledger and other open-source technologies, People's Clearinghouse (*Cámara de la Gente*), currently under active development as a digital payments platform in Mexico ([see: lacamara.mx](http://lacamara.mx)), aims to channel remittances directly into regional financial institutions. People's Clearinghouse aggregates technological and compliance requirements to facilitate the process of receiving account remittances for locally trusted financial institutions, which in turn aims to reallocate resources into community-driven projects in agriculture, small businesses, and essential infrastructure. The project operates through close collaboration with local institutions and communities in order to genuinely reflect local needs.

Currently in its pilot phase in selected regions and pending authorization by the Central Bank of Mexico, the People's Clearinghouse seeks to demonstrate the feasibility and effectiveness of combining advanced fintech protocols with community-based, socially trusted financial intermediation. This practical integration of modern fintech and local financial trust networks has the potential to significantly amplify the developmental impact of remittance flows, turning them from mere consumption into powerful tools for sustainable local economic growth.





VI. Conclusions & Policy Recommendations

“ Strengthening socially trusted financial intermediation is not a standalone solution, but it is an essential component of a wider strategy to tackle the root causes of migration.”

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This paper argues that a valuable yet overlooked asset for addressing some of the main root causes of migration is remittances, specifically when paired with socially trusted financial intermediation and suitable technological infrastructure⁹.

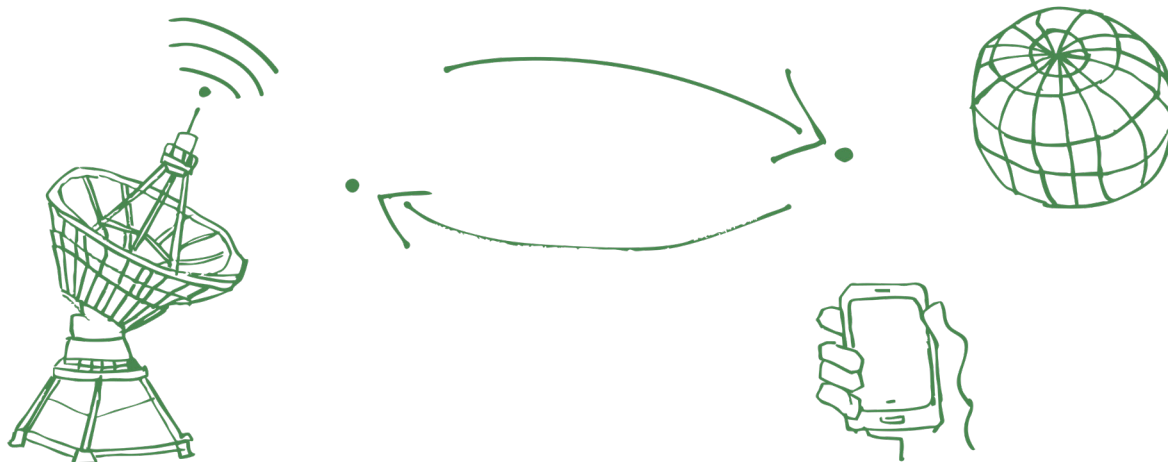
The most cost-effective investment by governments, development agencies, and NGOs, for addressing the root causes of migration, is the development and extension of networks of socially trusted financial institutions that can help transit from the vicious cycle of cash remittances to the virtuous cycle of remittances, by exponentially boosting regional credit and investment based on the capitalization of accounts by means of remittances. Any institution interested in implementing or promoting this solution should review the living examples of AMUCSS (Mexico), Red Fasco (Honduras), and Red Katalisis (Guatemala). The following policy recommendations are based on the experience of existing networks of socially trusted financial institutions. They pertain to regulatory, technological, and social policies,

three intertwined dimensions that policymakers should simultaneously address to maximize the potential of remittances in tackling the root causes of migration. While all recommendations are interconnected, prioritizing regulatory reforms (Recommendations 1 and 2), binational payment infrastructures (Recommendation 3), and the appropriate use of fintech technology (Recommendation 4) will provide immediate foundational support, enabling subsequent social empowerment (Recommendation 5) and multilateral cooperation (Recommendation 6).



⁹ The term “socially trusted financial intermediation” was explained in the introduction.

List of six recommendations



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1) Update regulatory framework and infrastructure for financial institutions.

National legal frameworks for savings cooperatives and microfinance institutions should be simplified and transparent, enabling small communities to establish local financial institutions easily. Transparent guidelines on interest rates and financial products should protect communities from predatory practices.

It's essential to have a tiered regulatory process so that small, low-volume financial institutions can register easily and quickly, with further, deeper regulatory standards applying only as these entities grow in capital and transaction volume. Authorities should prioritize extending small, regional, socially trusted financial institutions into unbanked regions. They should avoid favoring commercial banks, which often prioritize international investments over local ones.

Developing new infrastructure for stable electricity and internet connectivity, as well as pathways for value transportation, is key to fostering the expansion of socially trusted financial institutions in isolated regions. The implementation of technological tools that substitute cash (digital wallets and phone-to-phone payments) is also important for lowering and eventually eliminating the cost of value transportation.

2) Update regulatory framework for second-floor institutions and technology aggregators.

Due to their scale, socially trusted financial institutions often have limited capital and technological capabilities. Therefore, second-floor banks and technology providers must exist to help smaller financial institutions integrate into national and international payment networks and access modern financial technologies through APIs. For this purpose, policymakers should create or update regulations on second-floor social banks, understood as an intermediary between commercial banks and small financial institutions, which aim to offer credit to small finance institutions (commercial banks are often reluctant to do so). A laudable example of social banking is Guatemala's Banrural, established in the context of the 1985 pacification agreements and owned by thousands of social organizations. Under its auspices, many important financial institutions have flourished, such as Red Fasco.

As for technology, policymakers should ensure that smaller financial institutions can access larger payment infrastructures and remittance channels by means of innovative platforms like People's Clearinghouse. Additionally, fintech solutions can amplify collective action through applications for group savings, crowdfunding, diaspora investments, even using blockchain-based transparency and open data standards. Well employed fintech platforms can serve not only individuals, but also help organize communities around shared goals.

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With the existence of social banks and accessible payment networks, alliances and collaborations between socially trusted financial institutions can be quickly and easily implemented. Such partnerships are essential for redistributing excess remittance capital from a financial institution, directing it towards other financial institutions with higher demand for credit. They are also useful for disbursing support from NGOs and development banks, for which it would be too painstaking to implement initiatives with each financial institution individually rather than with networks and groups of socially trusted financial institutions.

It's crucial to acknowledge potential implementation challenges, including institutional inertia, limited political will, infrastructure gaps, and resistance from incumbent commercial banks. Overcoming these barriers will require coordinated advocacy, political engagement, and technical assistance from international development actors.

3) Update Central Bank regulatory framework for remittances.

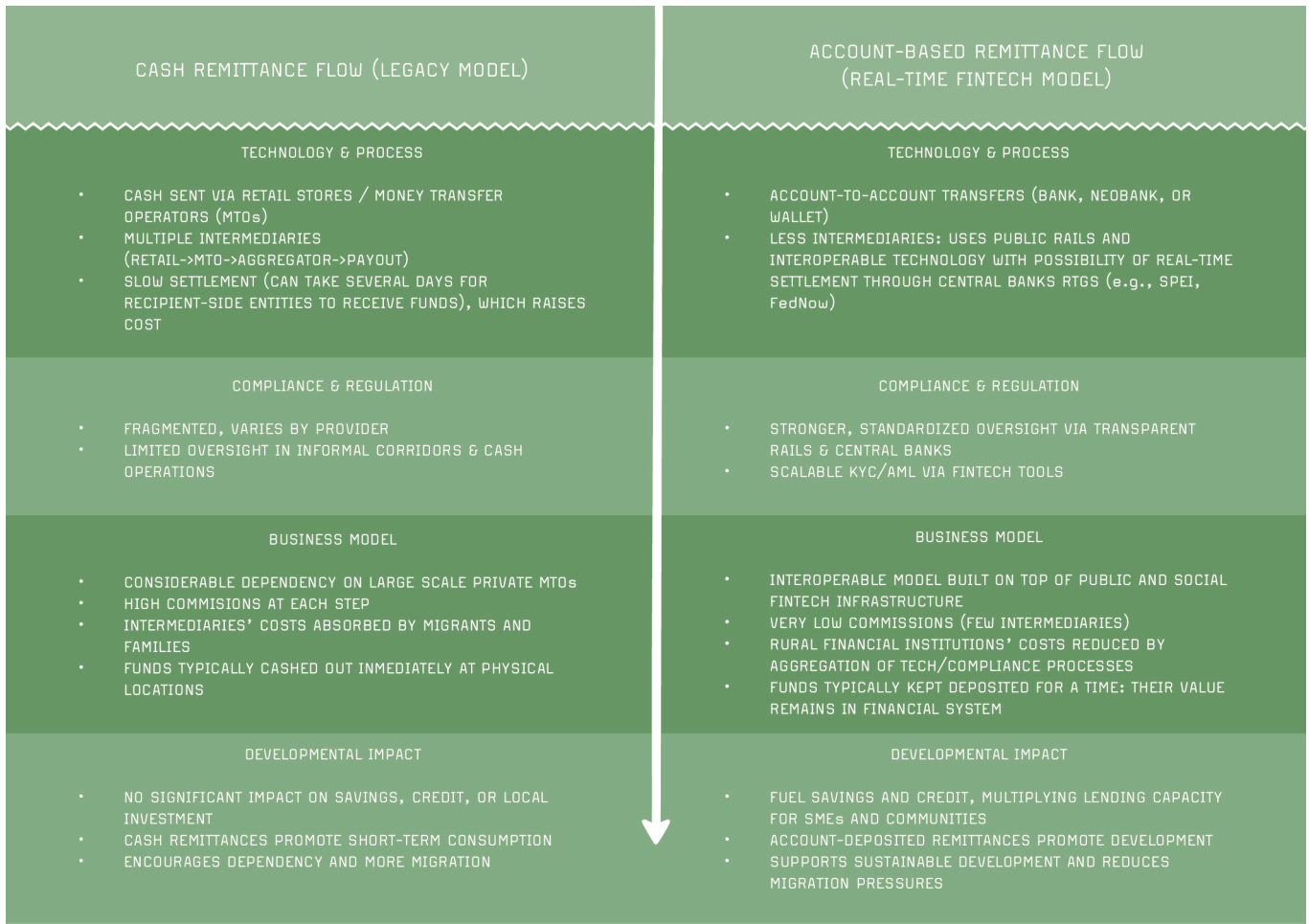
Policymakers must update binational regulatory frameworks to expand migrants' access to financial services, facilitate cross-border account opening, and lower remittance transaction costs. Currently, undocumented migrants in the United States can open bank accounts only in limited states and institutions. Policymakers should standardize financial inclusion rights for undocumented migrants nationwide, significantly reducing reliance on costly cash-based financial services.

Similarly, migrants in the United States should be allowed to open bank accounts in their home country from abroad. The Bank of Mexico and the National Commission of Banks and Securities (CNBV) introduced legislation for this purpose in May 2021, regulating how new account holders can be onboarded from abroad. While these legal reforms promote account remittances and increase migrants' involvement in hometown spending and planning, they were paradoxically limited to commercial banks, which do not invest in local development.

Moreover, the Federal Reserve and the Bank of Mexico are interconnected, allowing remittances to be sent between financial institutions on both sides of the border with reasonably low commissions and exchange rates (FedGlobal/DirectoAMexico). That laudable initiative must be extended to Central American countries, and the US payments infrastructure should be updated

to meet RTGS standards that could lower FedGlobal remittances' sending time (from around 24 hrs to only seconds). Such binational initiatives benefit hometowns, promote financial inclusion on both sending and receiving countries, and force dominant Money Transfer Operators to lower their prices to remain competitive.

Figure 6. Transformation of remittances' business model



4) Implement new fintech services for immigrants.

While fintech innovations in sending countries are essential and beneficial, purely digital solutions (e.g., NeoBanks) cannot yet effectively replace socially trusted financial institutions in remittance-receiving rural communities. NeoBanks typically lack personalized advisory services, community-based trust, and the detailed local knowledge essential to fostering sustainable local investments. Nevertheless, fintech tools can strongly complement socially trusted institutions, enhancing overall effectiveness (for example, clearinghouses and payment systems).

Other new developments that could be implemented based on fintech solutions include binational credits, assistance programs for family members, education and housing programs, and local investment plans for groups (such as crowdfunding). These could complement powerful initiatives already implemented, such as the aforementioned Bono Migrante (a year-long high-yield bond for migrant account holders).

5) Empower local and binational social organizations.

Socially trusted financial institutions depend on deep community trust and participation. Successful new institutions must build upon existing social dynamics and local organizations with established community recognition. This ensures meaningful local involvement, lower default rates, and genuine economic empowerment. Furthermore, successful financial education, digital literacy and trust-building initiatives should incorporate binational

strategies involving government agencies, consular representatives, and diaspora associations.

Social policies should be conscious of the fact that diaspora communities themselves can be co-creators of fintech solutions and community platforms for the development of their hometowns.

6) Promote multilateral alliances.

International organization's technical and financial support is key to promoting the opening of socially trusted financial institutions in new regions. Public and private funds should invest in the development of more of these institutions, particularly in unbanked areas: each socially trusted financial institution has an initial cost of 50,000 to 150,000 US dollars, depending on the country and the type of financial institution. Given their potential impact, their cost is extremely low, but still unaffordable for the poorest and most isolated regions of Mexico and Central America. Thus, external investment is required to accelerate the extension of regional networks of socially trusted financial institutions.

Due to the complexity of migration dynamics, the creation of a dedicated multilateral task force involving sending and receiving countries, NGOs, development banks, and financial networks is strategically essential. Such a coordinated effort ensures coherent, effective, and context-specific solutions. Other forms of collaboration could involve currently active transnational and regional networks of people related to remittance-recipient communities and directly impacted by public policies as the ones proposed here, such as Indigenous Migrant Frontline Communities.¹⁰

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¹⁰ The notion of Indigenous Migrant Frontline Communities (IMFC) encompasses indigenous and migrant communities who stand at the intersection of migration, climate change, and economic exclusion. IMFC highlights how indigenous, migrant populations—often among the most remittance-dependent groups—are also leaders in developing innovative practices of resilience, solidarity, and local investment. Similarly, IMFC exemplifies how diasporas and frontline communities can move beyond being seen merely as remittance senders or aid recipients. Instead, they can become active agents in shaping financial ecosystems that channel resources toward community-controlled, sustainable development.

Final conclusions.

These six recommendations face practical implementation challenges, including institutional resistance, limited political will, infrastructure deficiencies, and the entrenched interests of commercial banks. Addressing these requires sustained advocacy, coordinated political engagement, technical expertise, and strong support from international development agencies. Additionally, while our proposal emphasizes remittances and socially trusted financial intermediation, we recognize that broader structural factors such as labor markets, governance, and corruption also critically shape migration patterns. This paper provides actionable recommendations that specifically

address financial dimensions as a key component within a broader set of needed reforms.

These recommendations represent concrete opportunities for countries to harness the enormous potential of remittances, turning binational communities into agents of their development. Ultimately, the most impactful public policies empower communities to shape their collective future. Remittances, combined with socially trusted financial intermediation, provide a clear and effective pathway for communities and institutions to achieve together local sustainable development and reduce migration pressures.

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