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Remittances, Household Consumption, And Financial Resilience During Economic Shocks

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ABSTRACT: This paper examines how international remittance flows influence household consumption smoothing and financial resilience during periods of macroeconomic stress, using household survey data from remittance-dependent economies across two recent shock periods: the COVID-19 pandemic (2020–2021) and the subsequent global inflationary episode (2021–2023). Comparing consumption volatility between remittance-receiving and non-receiving households, the analysis employs a differencein-differences framework alongside household fixed-effects regression to identify the causal effect of remittances on consumption stability and savings recovery. Results indicate that remittance-receiving households exhibit significantly lower consumption volatility and faster recovery in savings rates, suggesting remittances act as an informal insurance mechanism. The paper discusses policy implications for leveraging remittance channels as a complement to formal social safety nets in shock-prone economies.

KEYWORDS: remittances, household consumption, financial resilience, economic shocks, consumption smoothing, informal insurance, difference-in-differences

1. INTRODUCTION

International remittances — transfers of money by migrant workers to their families in origin countries — represent one of the largest and most stable sources of external financing for developing economies. In 2023, global remittance flows to low- and middle-income countries reached an estimated USD 669 billion, surpassing foreign direct investment and official development assistance combined as a source of external finance (World Bank, 2024). For individual recipient households, remittances often constitute a substantial proportion of total income, providing a financial lifeline that enables consumption of basic necessities, investment in education and healthcare, and accumulation of precautionary savings.

The macroeconomic literature has long recognised remittances as a countercyclical financial flow — tending to increase when origin economies face downturns, as migrants send more money home to support families during hardship (Frankel, 2011). This countercyclical property has led development economists to characterise remittances as a form of informal insurance that complements — and in many contexts substitutes for — formal social protection mechanisms. However, the COVID-19 pandemic and subsequent global inflationary shock presented an unprecedented test of this insurance hypothesis: simultaneous economic stress in both origin and destination countries threatened to disrupt the countercyclical pattern of remittance flows.

This paper contributes to the remittance-resilience literature by exploiting the quasinatural experiment provided by these two sequential shock periods to identify the causal effect of remittance receipt on household consumption stability and financial recovery. By comparing outcomes between remittance-receiving and non-receiving households using a difference-in-differences framework, the study provides credible causal estimates that address the endogeneity challenges that have plagued earlier crosssectional work in this area.

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2. LITERATURE REVIEW

2.1 Remittances as Consumption Insurance

The theoretical foundation for the remittance-as-insurance hypothesis draws on the seminal work of Lucas & Stark (1985), who proposed an altruistic-cum-exchange model of remittance motivation. Under this framework, remittances are characterised as part of a long-term contractual arrangement between migrants and their origin households, whereby origin household members are implicitly compensated for investments in the migrant's human capital through ongoing income transfers. This contractual interpretation predicts that remittances will respond countercyclically to origin household income shocks, providing insurance against idiosyncratic and aggregate shocks that formal insurance markets cannot efficiently cover.

2.2 Consumption Smoothing in Developing Economies

Consumption smoothing — the ability of households to maintain stable consumption levels in the face of income fluctuations — is a central concern of development economics, reflecting the concavity of the utility function and the high marginal utility of consumption at low income levels. In the absence of complete insurance markets, households in developing economies typically rely on a portfolio of informal risksharing mechanisms, including gifts and transfers from extended family networks, rotating savings and credit associations (ROSCAs), and intergenerational transfers (Townsend, 1994).

2.3 Remittances During the COVID-19 Pandemic

The COVID-19 pandemic provided a significant test of the remittance-as-insurance hypothesis. Early predictions of a sharp remittance decline proved partially correct: global flows fell by approximately 2.4% in 2020, substantially less than the 20% decline initially projected by the World Bank (World Bank, 2021). The resilience of remittances during the pandemic has been attributed to the combination of fiscal stimulus in major migrant destination countries — which protected migrant workers' incomes — and the strong altruistic motivation of migrants to support family members during a global health crisis.

3. METHODOLOGY

3.1 Data Sources

The primary data source is a balanced panel of 4,218 households drawn from nationally representative household income and expenditure surveys conducted in four remittance-dependent economies — Bangladesh, Pakistan, the Philippines, and Mexico — covering the periods 2018–2019 (pre-shock baseline), 2020–2021 (COVID shock), and 2021–2023 (inflationary shock). These countries were selected based on the combination of high remittance dependence (remittances exceeding 5% of GDP), availability of longitudinal household survey data, and diversity of regional and institutional contexts. Supplementary data on remittance flows at the regional level are sourced from central bank remittance statistics.

3.2 Identification Strategy

The primary identification strategy is a difference-in-differences (DiD) estimator that compares changes in consumption outcomes between remittance-receiving households (treatment group) and non-receiving households (control group) across pre- and postshock periods. The key identifying assumption is that, in the absence of the economic shocks, treated and control households would have followed parallel consumption trends — an assumption supported by the parallel pre-trends observed in the 2018–2019 baseline data.

The baseline DiD specification is: $CONS_{it} = \alpha + \beta_1 REM_{it} + \beta_2 SHOCK_t + \beta_3 (REM_{it} \times SHOCK_t) + \gamma X_{it} + \mu_i + \varepsilon_{it}$, where $CONS_{it}$ is log per capita household consumption, REM_{it} is an indicator for remittance receipt, $SHOCK_t$ is a period dummy, and the interaction term β_3 captures the differential consumption change for remittancereceiving households during shock periods. Household fixed effects (μ_i) absorb timeinvariant unobservables.

4. FINDINGS AND ANALYSIS

4.1 Consumption Volatility During COVID-19 Shock

DiD estimates reveal that remittance-receiving households experienced significantly lower consumption declines during the COVID-19 shock period relative to nonreceiving households. The estimated treatment effect (β_3) indicates that remittance receipt was associated with a 12.3 percentage point smaller decline in per capita consumption (SE = 2.84, $p < 0.001$). This effect is largest for food consumption — the category with the highest immediate welfare significance — where the differential protection effect reaches 15.7 percentage points (SE = 3.12, $p < 0.001$).

4.2 Savings Recovery During the Inflationary Period

Analysis of savings rates during the 2021–2023 inflationary period reveals a significant differential recovery pattern between treatment and control households. Remittancereceiving households recovered to pre-shock savings levels within an average of 14 months post-COVID nadir, compared to 26 months for non-receiving households — a difference of 12 months that is statistically significant at the 1% level ($t = 4.23$, $p < 0.001$). This faster savings recovery suggests that ongoing remittance flows not only cushion consumption during shocks but accelerate the rebuilding of financial buffers that enable resilience to subsequent shocks.

4.3 Heterogeneous Effects by Transfer Cost

A novel contribution of this study is the analysis of how remittance transfer costs moderate the insurance effect. Exploiting variation in transfer costs across remittance corridors and over time, the study finds that households in high-cost corridors (defined as transfer costs exceeding the G20 target of 5% of transaction value) exhibit significantly smaller insurance effects ($\beta_3 = 0.074$, SE = 0.031, $p < 0.05$) compared to households in low-cost corridors ($\beta_3 = 0.147$, SE = 0.028, $p < 0.001$). This finding has direct policy implications: reducing transfer costs through the promotion of digital payment channels could substantially amplify the welfare benefits of remittances during future shocks.

5. DISCUSSION

The findings provide strong empirical support for the role of remittances as informal insurance in remittance-dependent economies, while also highlighting the critical importance of transfer cost reduction as a policy lever for amplifying welfare benefits. The differential protection effect

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documented in this study — equivalent to preserving approximately 12% more purchasing power during the COVID-19 shock for receiving households — represents a welfare gain of considerable magnitude in economies where household consumption margins are thin.

For policymakers in remittance-dependent economies, the results suggest several priorities. First, reducing transfer costs through regulatory reform of the money transfer operator market and active promotion of mobile money and digital payment channels should be treated as a social protection policy rather than merely a financial regulation concern. Second, the countercyclical nature of remittances could be leveraged through dedicated remittance-backed sovereign bond instruments that mobilise diaspora savings for public investment during downturns. Third, social protection programme design should explicitly account for remittance receipt in means-testing frameworks, recognising that remittance income — while informal — represents a genuine and relatively stable income stream for recipient households.

6. CONCLUSION

This paper has provided causal evidence that remittances significantly enhance household consumption resilience and accelerate financial recovery during economic shocks. Using a difference-in-differences framework applied to panel household survey data across four remittance-dependent economies, the study demonstrates that remittance receipt is associated with substantially lower consumption volatility during the COVID-19 shock and markedly faster savings recovery during the subsequent inflationary period.

The finding that transfer costs significantly moderate the insurance effect of remittances carries direct and actionable policy implications. Achieving the G20's stated goal of reducing global average transfer costs to below 3% — from a current average of approximately 6.2% — could meaningfully amplify the welfare impact of remittances, effectively expanding the social protection coverage of these private transfers without additional public expenditure. Future research should examine the long-term human capital and intergenerational welfare effects of remittance-enhanced resilience during economic shocks.

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