

# Remittances, Monetary Policy and Partial Sterilization

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**Abstract:** *Remittances play a large and important role in certain economies, where they became a significant share of GDP. Official government records of these flows have improved systematically since we realized its importance, but a significant percentage of remittances are still unrecorded. This, together with the shadow economy, may pose a problem for monetary policy. This paper uses a limited participation model to examine the differential effect that higher shares of remittances can have on monetary policy, and describes the impact of remittances on a small open economy under partial sterilization. It demonstrates how a typical monetary shock will lead to a more pronounced liquidity effect when remittances become a higher proportion of GDP. It also shows that a positive remittances shock improves consumption and lowers the interest rate, but as it also reduces work effort it momentarily lowers output. Such dynamics are exacerbated as the degree of partial sterilization is accentuated.*