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Assessment of Distributive Effects of Emigrant Remittances in Developing Countries

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Abstract Despite the rising volume of remittances flowing to developing countries, their distributional effect on the recipient countries has been largely unexplored. We examine this topic using data from World Bank. Despites the positive effects of emigrants remittances in terms of developing microfinance Institutions and welfare improvement of the recipient households, its negative effects ranges from appreciation of the national currency, hampering competitiveness, monetary management and rekindle inflationary pressures, extension of trade deficits and brain drain to mention just a few. Remittances represent a short-term fix for long-term problems. If properly channeled Remittances could be used to finance development and reduce poverty. Government of the recipients countries should promote Diaspora bonds in order to reap full benefits of emigrants remittances.

Keywords: *remittances, monetary management, statistical significance*

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1. Introduction

A remittance is a transfer of money by a foreign worker to an individual in his or her home country. Money sent home by migrants competes with international aid as one of the largest financial inflows to developing countries. Workers' remittances are a significant part of international capital flows, especially with regard to labor-exporting countries. [1] In 2014, $436 billion went to developing countries, setting a new record. Overall global remittances totaled $582 billion in 2015. Some countries, such as India and China, receive tens of billions of US dollars in remittances each year from their expatriates. In 2014, India received an estimated $70 billion and China an estimated $64 billion.

Remittances are playing an increasingly large role in the economies of many countries. They contribute to economic growth and to the livelihoods of less prosperous people (though generally not the poorest of the poor). According to World Bank estimates, remittances will total US$585.1 billion in 2016, of which US$442 billion went to developing countries that involved 250 million migrant workers. For some individual recipient countries, remittances can be as high as a third of their GDP.

Table 1. Top recipient countries of remittances (in billions of US Dollar) [7,8]

Country	Remittances 2012	Remittances 2013	Remittances 2014	Remittances 2015	Remittances 2016
India	68.82	69.97	70.97	72.20	62.7
China	57.99	59.49	61.49	63.90	61.0
Philippines	24.61	26.70	27.90	29.80	29.9
Mexico	23.37	23.02	24.50	25.70	28.5
France	22.05	23.34	23.94	24.60	18.9
Nigeria	20.63	20.89	20.88	20.89	19.0
Egypt	19.24	17.83	19.83	20.40	16.6
Germany	15.14	15.20	16.60	17.50	17.6
Pakistan	14.01	14.63	17.80	20.10	19.8
Bangladesh	14.24	13.86	15.10	15.80	13.7
Belgium	10.16	11.11	11.11	11.10	11.20
Vietnam	10.00	11.00	11.80	12.30	13.4
Ukraine	8.45	7.67	8.45	6.20	6.1
Spain	9.66	9.58	10.10	10.50	10.4
Indonesia	7.21	7.62	8.66	10.51	9.2

Note: These are the largest 15 recipient countries of remittances *only* for the year 2013. World Bank data is used for all countries and years. Source: obtained from Wikipedia, 2017.

Table 2. Remittance flows to developing countries, 2002–08 ($ billion)

	2002	2003	2004	2005	2006	2007	2008a
All developing	115.5	144.3	164.4	194.8	228.7	280.8	305.4
countries as % of GDP by region	1.9	2.1	2.0	2.0	2.0	2.1	1.9
East Asia and Pacific	29.5	35.4	39.2	46.7	53.0	65.3	69.6
Europe and Central Asia	13.7	15.5	22.2	31.2	38.3	50.4	53.1
Latin America and the Caribbean	27.9	36.6	43.3	50.1	59.2	63.1	63.3
Middle East and North Africa	15.2	20.4	23.0	24.3	25.7	31.3	33.7
South Asia	24.1	30.4	28.7	33.1	39.6	52.1	66.0
Sub Saharan Africa	5.0	6.0	8.0	9.4	12.9	18.6	19.8

Source: World Bank, 2009. *Note:* Remittances are defined as the sum of workers' remittances, compensation of employees, and migrant transfers. See www.worldbank.org/prospects/migrationandremittances for data definitions and the entire data set; 2008e = estimate.

As a share of GDP, the top recipients of remittances in 2013 were Timor- Leste (216.6%), Tajikistan (42.1%), Kyrgyzstan (31.5%), Nepal (28.8%), Moldova (24.9%), Lesotho (24.4%), Samoa (23.8%), Haiti (21.1%), Armenia (21.0%), The Gambia (19.8%), Liberia (18.5%), Lebanon (17.0%), Honduras (16.9%), El Salvador (16.4%), Kosovo (16.1%), Jamaica (15.0%) and Bosnia and Herzegovina (13.4%, which is about 1.817 billion $ on 31 December 2014).

Emigrant remittances have come to represent an increasingly important source of financial flows between developed and developing countries in recent decades. Officially recorded remittances—comprising all unrequited transfers from migrant workers to family and friends in their countries of origin—climbed steeply in the decades between 1970 and 2000, declining only in the late 1990s. They then grew sharply after 2002 ($115.5 billion), peaking at $305 billion in 2008 before dipping in response to the global financial crisis (Table 2). Future flows are bound to be affected by the simultaneous economic slowdown in the high-income countries—including the United States and Western Europe, which account for almost two-thirds of the remittances that migrants send home to developing countries—and in the developing countries that account for 10–30 percent of the rest. The fact remains that workers'remittances dwarf official aid as a source of funds for the developing world.

The distributive effect of remittances has been the subject of a large part of the evolving literature. Not only have remittances been shown to mitigate the impact of adverse shocks on an economy, but they also have been linked with helping to reduce poverty. Aggarwal and Spatafora, [1]. Kireyev [23] suggests that the decline in the poverty rate in Tajikistan from 81 to 60 percent from 2000 to 2003 was helped by the significant level of remittances to that country (where flows of remittances had reached 50 percent of GDP). Moreover, children in households receiving remittances are more likely to receive better education and healthcare.

This paper examines the distributive effects of remittances on recipient countries -welfare and poverty. It will advice policy makers and explain the significant role of remittances in financing for development of poor countries.

Improvements in banking technology that reduce the costs of formal remittance services and increase the geographical range over which remittances can be sent have steered unofficial remittances into the formal sector, enabling them to be recorded Chami, Fullenkamp, and Jahjah, [11]. That trend is expected to continue.

Nevertheless, a significant proportion of estimated remittance flows—estimated at between 35 and 70 percent of official remittances—remains unrecorded. Unrecorded remittances are channeled through the informal sector and are not captured in official balance-of-payment statistics. While remittances that move outside the formal sector may be used for legitimate reasons, they also may be channeled to unproductive and illegal activities, such as money laundering, drug money flows, and the financing of terrorism.

Examples of remittance channels, formal and informal, include:

- Interbank transfers
- Formal nonbank money-transfer operators
- Post-office transfers
- Cash and commodities carriers
- Informal money transfer operators Kireyev, [23]

Other channels are specific to a region or country, such as *fei-ch'ien* (China), *padala* (Philippines), *hundi* (India), *hui kuan* (Hong Kong), and *phei kwan* (Thailand). The *hawala* system, historically associated with South Asia and the Middle East, refers to an informal channel for transferring funds from one location to another through service providers—known as *hawaladars*—regardless of the nature of the transaction or the countries involved El-Qorchi and others, [14].

While some studies suggest that self-interest is the prime motive for remittance arrangements, most agree that the practice is primarily altruistic Stark and Lucas [34]; Chami, Fullenkamp, and Jahjah [11], and mainly confined to transfers between family members. The concentration on the household has formed the basis of studies of the microeconomic impact of emigrant remittances. Those studies have shown that remittances raise household consumption, stimulate investment (notably in real property), and result in better education and health care Kireyev [23]. Thus, from a microeconomic perspective, remittances should have a positive impact on growth.

But the literature, most of it recent, is not definitive on the macroeconomic impact of remittances. For example, Chami, Fullenkamp, and Jahjah [11] suggest that remittances have a negative impact on economic growth, whereas Aggarwal and Spatafora [1] find no effect, and Giuliano and Ruiz-Arranz [15] argue that remittances promote growth in countries with shallow financial systems but have no impact in countries with well-developed financial systems. The lack of a clear relationship is not surprising. First, the impact on growth will depend on whether the remittances are spent on consumption or investment. To this end, the research suggests that remittances have primarily been used for consumption purposes, with little impact on long-run growth. Second, the research shows that remittance inflows are countercyclical, increasing during periods of weak economic growth in the receiving countries. This countercyclical nature makes it difficult to establish the true impact of remittances on economic growth. It does suggest, however, that remittances can play a large part in maintaining macroeconomic stability and mitigating the impact of adverse shocks. A number of papers quoted in Spatafora [33] have attested to this.

However, the distributive effects of remittances can also be negative. Kireyev [23] outlines a number of negative effects of remittances for Tajikistan that also figure in studies of other countries. Remittance inflows may have any of the following negative effects:

- They may impede monetary management and rekindle inflationary pressures, as the unpredictability and seasonal nature of foreign currency inflows create uncertainties for monetary management.
- They may lead to an appreciation of the national currency, hampering competitiveness.
- They may contribute to the expansion of the trade deficit. In Tajikistan, most remittances are used to finance imports.
- They may create a strong disincentive for domestic savings. Declining savings can deplete the resource base for investment and may even turn it negative.
- They may pose a serious moral hazard (see glossary) by reducing the pressure for reforms. Remittances enable households and private businesses to support their own consumption or investment independent of the national government, thus reducing pressure on the authorities to create a better business environment and to deal with the problems that forced emigrant workers to leave the country in the first place.

A related negative associated with migration is brain drain. Although migrants may learn skills that may be useful to their country of origin when and if they return, the loss of human capital that comes with emigration hampers a country's development prospects. Mishra [29] shows, for example, that the Caribbean countries—, which have lost in excess of 70 percent of their best-educated labor, force (those with more than 12 years of schooling)—are not fully compensated for brain drain by the significant inflow of remittances.

Some research has focused on the policies and regulations that determine the flow of remittances, but further research is needed on how to create a sustainable development path for the source country.[1] In summary, remittances represent a short-term fix for long-term problems.

5. Conclusion

The paper began by demonstrating the well-established causal link between a well-functioning financial system and economic growth. It then identified the impact of macroeconomic fundamentals on the financial system, showing, for example, that imbalanced growth and high inflation harm the financial system. While the link between financial development and income inequality remains unclear, recent empirical studies have found that financial development tends to reduce income inequality. From a brief history of financial sector reform in developing countries, we saw that reforms, which began in the mid-1970s, started by liberalizing interest rates. Later reform efforts concentrated on indirect instruments of monetary control and the dismantling of directed credit before moving on to strengthen the overall financial sector infrastructure, including legal, regulatory, and supervisory frameworks. The most recent reforms have included moves toward greater transparency and better auditing and accounting standards. The paper then discussed policy measures that can be used to increase access to financial services by strengthening institutional infrastructures, liberalizing markets, and fostering greater competition. The paper concluded with a discussion of microfinance and emigrants' remittances, both increasingly important channels of financial flows to the poor in developing countries.

[1] Multiple exchange rates, restrictions on holding foreign-exchange deposits, large black market premia, high transaction costs in the form of money-transfer fees, and dual exchange rates all reduce remittance inflows.

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