Remittance: A Double Edged Sword

Remittance Background

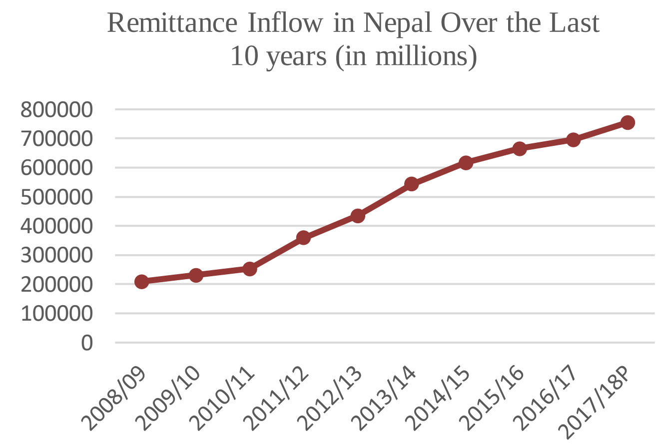
Remittance entails the money sent by migrant workers to individuals in the home country. In terms of size of the financial flows, Remittance stands shoulder to shoulder with international aid. The allure of remittance lies in the fact that remittance has historically proven to be less volatile and more reliable than other major sources of foreign exchange such as FDI and official development aid (1).

Worker's remittance is one of the forces that keeps the engine of the economy running, at least in developing nations of the world. A case in point is made by an example of Tajikistan in which remittance accounted for more than 50% of the GDP in the year 2012. There are opposing viewpoints on whether remittance boosts the economic growth or retards it. While some studies consolidate the idea that remittance enhances the livelihood by inducing capital investments and promoting education and health, some studies paint a gloomy picture by positing that remittance instigates a culture of dependency thereby, reducing the labor supply and bolstering consumption.

Remittance Statistics

While remittance declined extensively owing to financial crisis in 2008, it is still continuing the upward trend. The global remittance figure increased from $573 billion in 2016 to $613 billion in 2017, up by 7% over the previous year's figure. The inflow of remittance improved all across the globe with India, China, Philippines, Mexico, Nigeria and Egypt being the top recipients of remittance in terms of volume. In terms of remittance as a percentage of GDP, the smaller developing countries such as Kyrgyzstan, Tonga, Tajikistan, Haiti and Nepal come to the forefront (2). Remittance has occupied a crucial place in the economic fabric of developing nations with remittance considered more important than FDI, Public debt or Official Development Assistance.

Remittance Trend in Nepal



Source: Nepal Rastra Bank (CME Report)

Although the growth of remittance has slowed down from the year 2013/2014, the harmonic mean growth rate of remittance inflow over the past 10 years is still more than 11%. The remittance growth crippled slightly in the year 2016/17 but has risen to 8.57% in the recent fiscal year. The slowdown in the growth of remittance can largely be attributed to the declining trend of number of migrant workers seeking foreign employment to Malaysia and Qatar. But with a slew of recent reforms such as signing of MOU with the Malaysian government pertaining to recruitment; employment and repatriation, workers no longer have to bear recruitment service charges, two way airfare, visa fee, health check-up and so on when moving out to Malaysia as migrant workers. Therefore, the trend of migrant workers moving out to Gulf nations as low skilled workers is not expected to slow down anytime soon.

Advantages

It is well documented that households relying on remittance have more money available for consumption and consequently, lower incidences of extreme poverty than their counterparts who are deprived of remittance. The remittance can even help the households to deal with the crisis arising out of political turmoil. For instance: During the Arab spring, the Egyptian households relied on remittance to tide through difficult situation. While, FDI and donations in Egypt were declining, remittance increased during the same period. Should Nepal confront similar turmoil such as economic blockade and political instability, remittance can be a saving grace for Nepal.

Another benefit of remittance is that the families dependent on remittance tend to spend more on education than do non-remittance counterparts. In addition, other benefits of remittance include lower mortality and improved sanitary conditions in the recipient nations through the acquisition of durable goods. On a macro scale, remittance enhances the local human capital, provides a boost to the national income through the addition of foreign exchange and also serves as an important source for funding imports of the nation. With remittance accounting for more than 25% of Nepalese GDP in the present context, remittance has undoubtedly played an instrumental role in driving up the growth of Nepalese economy, particularly the service sector. By acting as a neutralizing factor to offset the current account deficit, remittance has ensured stability in the external sector. This is exemplified by the fact that share of remittance in current account receipts, shot up from 27.4% in 2001 to 61.5% in 2015 (3). In addition, remittance is the largest and a stable source of foreign exchange income for Nepal. Since the year 2013, Remittance has accounted for more than 65% of the foreign exchange earnings. Similarly, remittance has also fueled the growth of tax revenues by inducing the growth in consumption. The growth in remittance would enable the tax authorities to accumulate increased tax income in the form of consumption tax, value added tax and customs duty, which in Nepalese context accounts for a large chunk of total tax revenue. In Nepal, the tax revenue went up from 8.6% in 2000 to 15% of GDP in 2013 and the growth in tax income was largely driven by the growth in remittance (3).

Additionally, remittance is seen as stable and countercyclical source of external financing. Acknowledging this peculiar benefit of remittance IMF Debt Sustainability framework even allows recipient nations to carry higher levels of debt when the ratio of remittance is higher than certain percentage of domestic income and exported goods and services (4). While the role of remittance on economic growth can be argued, nations like Samoa and Tonga that are heavily dependent on remittance have witnessed growth in economic activities over the period 1981-2008 as remittance fuels the growth in private sector through the addition of liquidity in the banking system (5).

Disadvantages

One sobering repercussion of remittance is felt in the labor market. The potential of remittance to lower the working hours and labor market participation cannot be downplayed. For instance: in a study conducted in Haiti in 2009, it was found that Haiti witnessed a fall in both working hours and labor market participation owing to the disruptive effects of remittance. Owing to the increasing trend of migrant workers going abroad to seek employment, the hills and rural areas are virtually devoid of working population and skilled workers. Since it can be strongly contended that remittance received by households is not used for the acquisition of productive agricultural goods, remittance might adversely affect the agricultural yield because not only is rural Nepal facing the deficiency of skilled labor resources, only around 2.4% of remittance income is used for capital formation in Nepal. No wonder the contribution of agriculture in the GDP of the nation is waning (6).

The fact that many migrant workers in Nepal are concentrated on Gulf nations with Qatar and Malaysia being the top destinations should also be a cause for concern. Should there be an onset of economic crisis in these nations, this impedes the flow of remittance in Nepal and subsequently the effect will be felt on the BOP of Nepal which is already dealing with a large deficit in the current account. For example: In 2017 a number of Arab nations cut diplomatic and economic ties with Qatar. Since Qatar imports 90% of food from its neighboring nations, the news sent shockwaves amongst the Nepalese migrant workers stationed at Qatar who feared that Qatar based business would be adversely affected.

Conclusion

The reliance on remittance certainly poses a grave threat to the economy in the long run. The increasing remittance inflow is an indication of increasing outmigration of laborers, which deprives the local market of skilled and semi-skilled human resources. Furthermore, the over-reliance on remittance to correct the current account deficit and BOP problem can take away the country's capability to be competitive and productive, thereby undermining the competitiveness of the remittance receiving nation. While remittance can contribute positively in the foreign exchange reserve accumulation and stimulate the domestic market through increased deposit in the financial system, its implications on the socio-economic front in the form of decrease in agricultural yield and shortage of skilled labor resources can retard the economic growth. Therefore, the increasing remittance in Nepal is a definite red flag that needs to be addressed.

References

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