Remittance Behavior of Migrants and its Macroeconomic Effects in Four Developing Countries

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ABSTRACT

The literature on the macroeconomic effects of remittances is inconclusive. This study establishes a relationship between remittances and other important macroeconomic variables, such as consumption, investment and economic growth in Bangladesh, Egypt, Pakistan, and Syria over the period 1975-2006. Overall results suggest that remittances have a positive impact on economic growth in Pakistan and Syria but a negative impact in Bangladesh and Egypt. Negative remittance-growth coefficients in those two countries suggest a counter-cyclical relationship. A key objective of this paper is to identify how the remittance behavior of migrants varies across countries. Results from panel estimation procedure shows that a combination of self-interest and enlightened self-interest behavior of migrants is responsible for the growth impact in Bangladesh. The enlightened self-interest motivation is also the most likely cause of the growth impact in Egypt. Finally, the self-interest behavior explains the growth impacts in Pakistan and Syria. Results from this paper have policy implications for developing countries which face dilemmas and debates on the impact of remittances on economic growth.

Keywords: Consumption, Economic Growth, Macroeconomic Variables, Motivations to Remit, Remittance

INTRODUCTION

For many labor exporting developing countries, it is well documented that migrants’ remittances constitute a large portion of external resources, even without considering the significant amount of flow through unofficial channels (El-Sakka & McNabb, 1999; Glytsos, 2005). A World Bank (2006) report shows that recorded remittance flows to developing countries doubled in the five years after 2000 and have continued to increase. The amount of remittances to developing countries increased to $251 billion in 2007, which is 11 per cent higher than the amount in 2006 (Ratha et al., 2008). The magnitude and significance of remittance flows have motivated researchers and policy-makers to improve their understanding of remittances with regard to: a) the remittance-sending behavior of migrants, or their motivation to remit; and b) its impact on different macroeconomic variables, such as consumption, investment and economic growth. From a macroeconomic perspective, there is no unanimous theory that explains migrants’ behavior of remitting funds to their home countries. Remittance flows could be the result of...

The disparity in the findings of the previous studies raises a number of questions: 1) Are remittances used for consumption or investment? 2) Do remittance flows in developing countries go up during periods of economic downturn? 4) Do migrants behave altruistically? 5) Are migrants guided by the self-interest motivation? These questions are intriguing for policy-makers of developing countries and thus, need to be verified empirically.

This study attempts to fill the existing gap in literature by addressing these questions. We first investigate the effect of remittances on macroeconomic variables, such as the investment rate, the consumption rate, and GDP growth. Different macroeconomic effects of remittances are then used to analyze the remittance behavior of migrants. This investigation is different from the existing literature in many ways. First, while empirical microeconomic literature commonly explains the remittance behavior of migrants, we attempt to investigate remittance behavior using macro-level data. To our knowledge, using macroeconomic data to explain migrants’ behavior is unique. Second, from a methodological point of view, we use a recently developed instrumental variable approach (two-step generalized method of moments) to accommodate the persistence characteristic of time-series variables. Finally, some policy suggestions, based on our empirical results, are provided in the last section.

To that end, this paper focuses on four developing countries: Bangladesh, Egypt, Pakistan and Syria. The selection of these four countries is guided not only by the source of remittances (the oil-rich Arab countries) but by other similar characteristics. All of these countries are known to depend heavily on the inflow of external transfers. They also experience similar inflows of remittances as a percentage of GDP. Since 1975, the average migrant remittance, as a percentage of GDP, for Bangladesh, Egypt, Pakistan and Syria was 3.3%, 7%, 4.9% and 3% respectively. The context, methodology and results of this paper are presented as follows. The next section reviews the literature. The third section presents the methodology used to determine the impacts of remittances on consumption, investment and growth. The results and the analysis of these results are presented in the following sections. The final section concludes the paper.

LITERATURE REVIEW

Remittance Behavior of Migrants

Glytsos (2001) presents a detailed review of the literature on the remittance behavior of migrants, and argues that there is no single theory of remittance determination. Within the broader literature, one can, however, identify two sets of approaches that determine a migrants’ motivation to remit to their home country (Chami et al., 2003). The first approach, i.e., the endogenous migration approach to remit, concentrates on the microeconomic aspects of the migrant-family relationship. Using the behavioral economics analysis of the migrant-family relationship, researchers give a range of reasons that explain the remittance behavior of migrants. The second approach takes macroeconomic variables into consideration, and argues that migrants’ portfolio decisions, in response to macroeconomic variables, such as the relative real rate of return on financial and real assets, exchange rates, and inflation, may influence the flow of migrants’ savings into their home country (Swami, 1981; Lianos, 1997). While the
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