REMITTANCE-LED GROWTH HYPOTHESIS: A CONCEPTUAL ANALYSIS

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Abstract

This research centered on the conceptual and empirical analysis of the remittance-led growth hypothesis. There exist four views with regard to the relationship between remittances and economic growth and these include the remittances-led growth, growth-led remittances, feedback view and the neutrality view. Remittance-led growth mentions that remittances inspire economic growth whilst the growth-led remittances view says that economic growth attracts more remittances into the country. The feedback view suggests that both remittances and economic growth promotes each other whilst neutrality hypothesis stipulates that there exists no relationship at all between remittances and economic growth. Majority of literature concur that remittances plays a significant role in boosting economic growth especially in developing countries. It is against this backdrop that this study focuses on conceptually and empirically analyzing the remittance-led growth hypothesis. Trend analysis between remittances and economic growth for Botswana as a case study was done using time series annual data ranging from 1980 to 2011. The literature conceptual framework analysis shows beyond any reasonable doubt that indeed remittances are an integral element of economic growth especially for developing countries. The study therefore recommends nations especially developing countries to make available the necessary infrastructure that attracts personal remittance inflows from its citizens working in other countries in order to boost economic growth.

Keywords: Remittances, Growth, Conceptual, Empirical, Analysis

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1. Introduction

Remittances flows to developing countries are equivalent to more than three times the quantity of official development assistance and as a result have positive economic growth implications (World Bank, 2013). In 2012 alone, remittance flows to developing countries was approximately US$401 billion, representing a 5.3% growth from year 2011, according to the World Bank (2013). Acosta (2008) also revealed that workers' remittance flows have become one of major sources of finance for developing countries.

Quite a number of empirical studies have so far investigated the relationship between remittances and economic growth. In a study on India, Jayaraman et al (2012) revealed remittances and the relationship between remittances and financial sector development had a positive impact on economic growth between 1970 and 2009. Using panel data approach from 64 countries made up from 29 African, 14 Asian and 21 Latin American countries, Nsiah and Fayissa (2013) established that remittances, openness and capital labour ratio had significant positive influence on economic growth for all the regions as a collective. The economic growth impact of remittances however was found to be more significant in Asian countries as compared to other region, revealed Nsiah and Fayissa (2013). An increase of remittances by 10% resulted in economic growth increase by 1.56%, 0.13% and 0.3% in Asia, Africa and Latin America and Caribbean regions respectively, argued Nsiah and Fayissa (2013). On the contrary, Akano (2013) discovered a uni-directional causality relationship running from gross domestic product (GDP) and gross capital formation (GCF) to remittance inflows into Nigeria's economy. While recorded remittances flowing into developing countries have increased over the last decade, very few conceptual analysis studies have been done to investigate the impact of remittances on economic growth in developing countries, argued Catrinescu et al (2009).

To the best of the author's knowledge, no study has so far been carried on the conceptual analysis of the remittances-led growth hypothesis. The current study aims to fill in that empirical literature gap. The findings from this research are going to help particularly developing countries in crafting a remittance policy and strategy that if implemented will go a long way in boosting economic growth.

The second section looks at conceptual literature analysis whilst the third section discusses personal remittances received and economic growth trends for Botswana. The fourth section concludes the study and put forward some policy recommendations.

2. A Conceptual and Empirical Analysis: Remittance-led Growth Hypothesis

Majority of both the theoretical and empirical literature review agree that remittances inspire economic growth. However, other researchers mention that certain minimum conditions and environment has to be in place first before the migrant exporting country can begin to enjoy remittance-led growth benefits.

Remittances-led growth hypothesis stipulates that remittances spur economic growth and studies whose findings resonate with this view include but are not limited to Guha (2013), Strielkowski (2013), Nsiah and Fayissa (2013), Castello and Boike (2011), Banaian and Roberts (2007), Ang (2009), Jayaraman et al (2012), Tansel and Yasar (2010), Haas (2006), Singh (2010), Jackman et al (2008), Sharma (2010), Haas (2005), Nikas and King (2005), Mundaca (2009), Richard et al (2005), Acosta et al (2008), Catrinescu et al (2009), Pradhan et al (2008), Giuliano and Arranz (2009), Ahortor and Adenutsi (2009), Bettin and Zazzaro (2012), Le (2009) and Balde (2011).

According to Guha (2013), remittances positively impact on the current account and improve the balance of payment of a recipient country. The same study by Guha (2013) revealed that remittances strengthen the currency of a recipient country assuming all other factors remains constant. Nikas and King (2005) concurred that remittances improve the balance of payment and lead to appreciation of the local currency apart from helping in modernizing the migrant-exporting country. However, the size of remittances plays a key role in determining the extent of its economic growth impact in the migrant-exporting country, argued Nikas and King (2005).

Economic growth impact of remittances is not uniform as it depends on the availability of an efficient remittance transfer mechanism in the migrant exporting country, revealed Strielkowski (2013). Due to differences in the efficiency level of remittance transfer mechanism, Strielkowski (2013) found out that remittances contributed to more GDP per capita growth in South Asian countries than in Official Development Assistance (ODA) countries. However, Castello and Boike (2011) established that the economic growth impact of remittances is far much more pronounced in smaller developing nations such as Guinea-Bissau, Tajikistan, Moldova, Honduras, Grenada, West Bank and the Gaza Strip than in larger and more developed nations such as India, China, Mexico and Brazil. However, Ang (2009) suggested that economic growth impact of remittances was very low in the rural areas as compared to urban areas of Philippines. The argument proffered by Ang (2009) was that remittances were more used for consumption purposes in the rural areas as compared to urban areas of Philippines where remittances are translated into value-addition activities and investments which are the cornerstone for economic growth. Tansel and Yasar (2010) also found out that remittances-inspired economic growth was not uniform in Turkey during the period 1970 to 2009.

A 10% increase in remittances inflows led to an annual economic growth rate of 1.6% in Armenia, further revealed Banaian and Roberts (2007). Apart from boosting economic growth, Banaian and Roberts (2007) discovered that remittances reduced poverty, impacted positively on education and resulted the decline of the most productive labour force in Armenia. Tansel and Yasar (2010) however discovered that remittances had an indirect significant impact on economic growth in Turkey via by boosting consumption, investment, income and imports both in the short and long run. However, using the panel approach comprising of 36 Sub-Saharan countries, Singh (2010) discovered that remittances was higher for nations with larger number of citizens living in the diaspora and for nations with more citizens living in more richer economies.

Moreover, Singh (2010) suggested that remittances-inspired economic growth is also higher for migrant exporting countries with stable political environments and deeper financial institutions. On the contrary, Giuliano and Arranz (2009) in a study of 100 developing countries discovered that remittances boost economic growth in countries with shallow financial markets by acting as an alternative method of financing investments.

In a study on Morocco, Haas (2006) established findings that were consistent with other proponents of the remittances-led growth hypothesis. Haas (2006) specifically revealed that remittances and international migration not only inspired economic growth but significantly improved the standard of living of the general populace in Morocco. In concurring with Haas (2006), Jackman et al (2008) revealed that remittances indirectly positively impact on economic growth through providing a stabilizing influence on investment and output volatility. Haas (2005) further argued that the remittance-inspired growth would be much more pronounced if the investment environment and immigration policies in the recipient country are conducive.

Sharma (2010) concluded the remittances-led growth hypothesis is only valid up to a certain point, beyond which its relevancy ceases to exist because of the role that other factors begin to play such as characteristics of migrants, socio/economic/political environment prevailing in the country of origin, immigration policies of the host country and the size of the remittances. According to a study by Mundaca (2009), remittance-inspired growth is heavily influenced by the level of financial development in the migrant-exporting nation. The availability of financial services leads to more and even better usage of remittances thus boosting economic growth in a recipient country, argued Mundaca (2009). The latter also revealed that remittances have an overall effect of increasing the positive impact of investment per capita on economic growth of the migrant exporting country.

Using panel data approach for 71 developing countries, Richard et al (2005) discovered that remittances do not only positively impact on economic growth but reduce the level of poverty in the recipient country. According to Richard et al (2005), a 10% increase in per capita remittances leads to a 3.5% decrease in the number of people living in poverty in the migrant exporting country. These results are consistent with those found out by Acosta et al (2008). Remittances contribute to long term economic growth in recipient countries where economic, political and institutional policies of high quality exist, argued Catrinescu et al (2009).

Using panel data approach on 39 developing countries, the study by Pradhan et al (2008) produced statistically significant results that are consistent with other remittances-led growth proponents. Remittances boost national gross savings and investment resulting in long term economic growth of the migrant exporting country, argued Pradhan et al (2008). The same study by Giuliano and Arranz (2009) revealed that remittances inspire economic growth by improving capital allocation and ameliorating credit constraints in the migrant exporting country. Remittances ensure allocative efficiency by contributing more towards economic development than foreign aid because they are received by the people in need, argued Balde (2011).

The existence of a good investments climate and strong human capital development index accelerate the positive impact of remittances on economic growth in the migrant exporting country, revealed Ahortor and Adenutsi (2009). It is against this reason that remittances contributed more towards long run economic growth in Latin America and the Caribbean as compared to Sub-Saharan Africa, according to Ahortor and Adenutsi (2009). Bettin and Zazzaro (2012) stressed that the migrant exporting country can only meaningfully economically benefit from remittances inflow if the banking sector is efficient and economic risk is high.

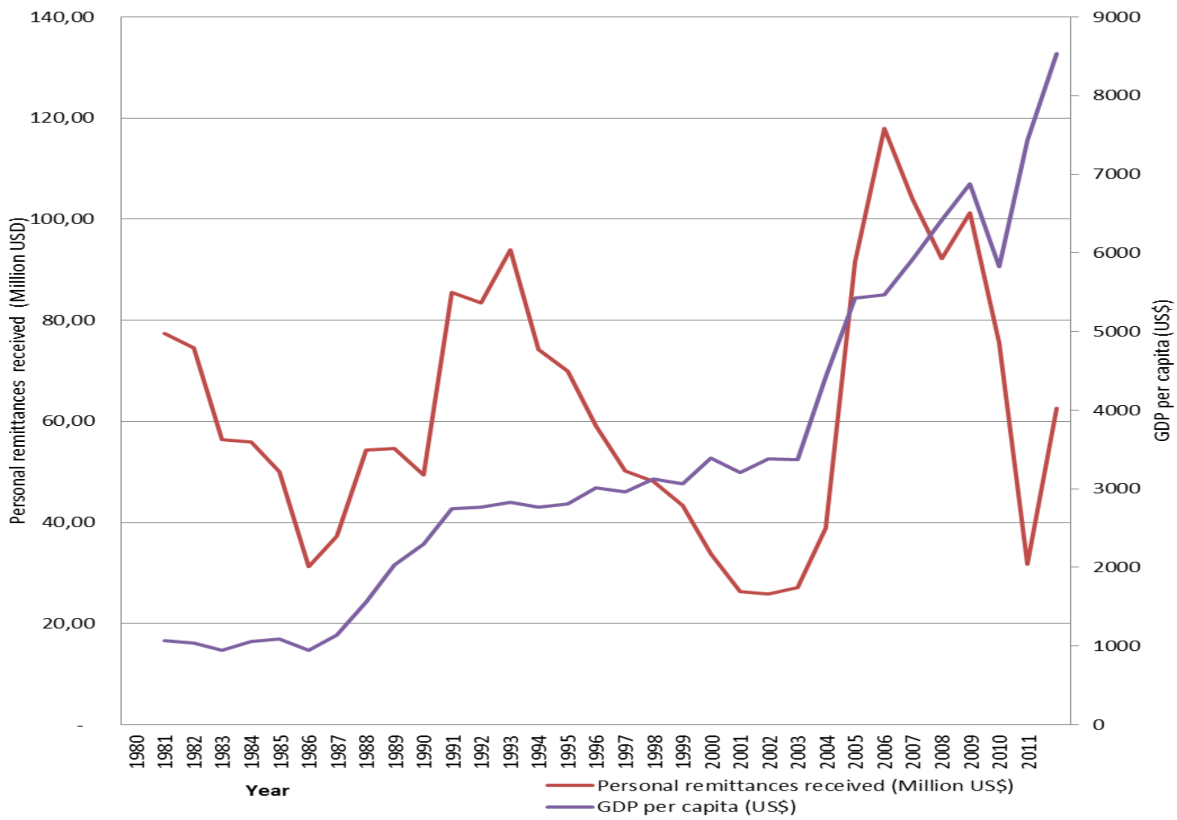
However, Guha (2013) argued that remittances will not positively influence economic growth of a recipient country in the absence of a conducive investment environment in the country. The true positive influence of remittances on economic growth can not be realised unless there is appropriate avenues for absorption of these inflows into the economy of the recipient country, revealed Guha (2013). Balde (2011) discovered that remittances indirectly positively influenced economic growth by boosting savings and investment in the Sub-Saharan African (SSA) countries. On the contrary, Le (2009) established that remittances reduce the desire to work by residents in a migrant exporting country thereby negatively impacting on economic growth.

3. Remittance and Economic Growth Trends: A case of Botswana.

The 31 year period from 1980 to 2011 was characterised by a general upward trend in GDP per capita and mixed trend in personal remittances received by Botswana (see Figure 1). According to the World Bank (2012), personal remittances received went down by 59.56%, from US$77.33 million in 1980 down to US$31.27 million in 1985. During the same time frame, GDP per capita declined by 11.50%, from US$1 064.92 in 1980 down to US$942.49 in 1985. The period 1985 to 1990 saw both personal remittances received and GDP per capita going up by 173.62% and 190.94% respectively.

GDP per capita increased by 9.78%, from US$2 742.13 in 1990 to US$3 010.38 in 1995 whilst personal remittances received further plummeted by 30.87% during the same time frame. Personal remittances received declined by a significant 55.64%, from US$59.16 million in 1995 down to US$26.25 million in 2000 whilst GDP per capita further surged by 6.44% during the same period. However, both GDP per capita and personal remittances received both registered an increase of 70.64% and 349.19% respectively during the five year period ranging between 2000 and 2005. Moreover, personal remittances plummeted by 73.12%, from US$117.89 million in 2005 down to US$31.69 million in 2010 whilst GDP per capita experienced a 35.83% surge during the same time frame to finish year 2010 at US$7 426.63. The year 2011 saw both personal remittances received and GDP per capita increasing by 97.62% and 14.89% respectively. GDP per capita went up from US$7 426.63 million in 2010 to US$8 532.62 million in 2011 whilst personal remittances grew from UD$31.69 million to US$62.64 million during the same time frame.

Figure 1. Personal remittances received (Million US$) and Gross Domestic Product per capita (US$) trends for Botswana – 1980-2011



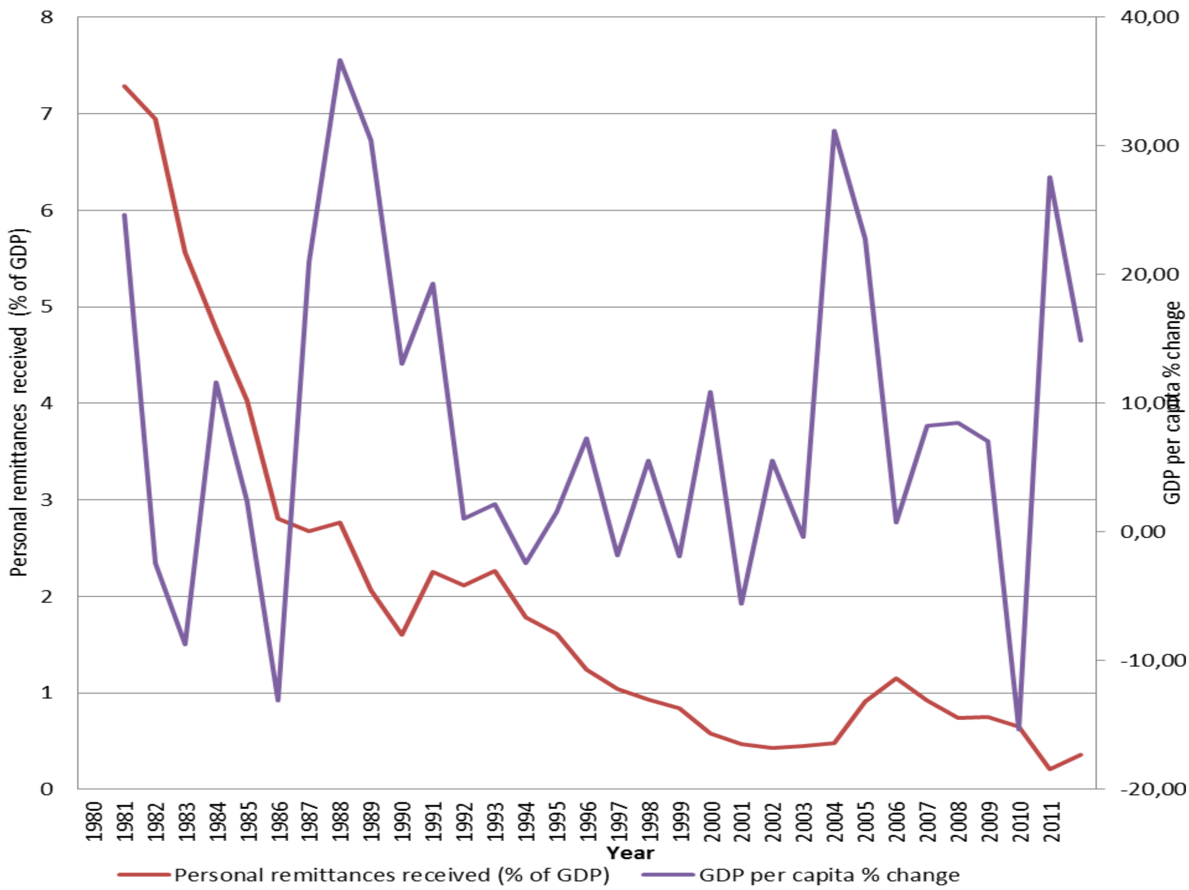
Source: World Development Indicators (2012)

Whilst personal remittances received (% of GDP) was characterized by a general gradual decline during the entire period between 1980 and 2011, GDP per capita growth exhibit a mixed trend during the same time frame (see Figure 2). Personal remittances received (% of GDP) declined by 4.48 percentage points, from 7.29% in 1980 down to 2.81% in 1985. It further declined by a paltry 0.55 percentage points between the five year period 1985 and 1990 whilst GDP per capita growth surged by a massive 202.44 percentage points during the same time frame.

Both remittances received (% of GDP) and GDP per capita growth declined by a paltry 1.02 percentage points and a huge 181.16 percentage points respectively during the period 1990 to 1995. Moreover, the subsequent five year period between 1995 and 2000 again saw both personal remittances received (% of GDP) and GDP per capita growth going down by 0.77 percentage points and 3.34 percentage points respectively.

Personal remittances received (% of GDP) increased by a slight 0.68 percentage points, from 0.47% in 2000 up to 1.15% in 2005 whilst GDP per capita growth went up by a significant 64.20 percentage points (from 6.44% to 70.64%) during the same time frame. However, GDP per capita growth recorded a 34.81 percentage points negative during the subsequent five year between 2005 and 2010 whilst personal remittances received (% of GDP) went down by a paltry 0.94 percentage points during the same period. The year 2011 was characterized by a slight increase by 0.15 percentage points in personal remittances received (% of GDP) and a significant decline of 20.94 percentage points in GDP per capita growth. The latter plummeted from 35.83% in 2010 down to 14.89% in 2011 whilst the former surged from 0.21% in 2010 to 0.36% in 2011.

Figure 2. Personal remittances received (% of GDP) and GDP per capita % change trends for Botswana – 1980-2011



Source: World Development Indicators (2012)

4. Conclusion and Recommendations

This research centered on the conceptual and empirical analysis of the remittance-led growth hypothesis. There exist four views with regard to the relationship between remittances and economic growth and these include the remittances-led growth, growth-led remittances, feedback view and the neutrality view. Remittance-led growth mentions that remittances inspire economic growth whilst the growth-led remittances view says that economic growth attracts more remittances into the country. The feedback view suggests that both remittances and economic growth promotes each other whilst neutrality hypothesis stipulates that there exists no relationship at all between remittances and economic growth. Majority of literature concur that remittances plays a significant role in boosting economic growth especially in developing countries. It is against this backdrop that this study focuses on conceptually and empirically analyzing the remittance-led growth hypothesis. Trend analysis between remittances and economic growth for Botswana was done using time series annual data ranging from 1980 to 2011. The literature conceptual framework analysis shows beyond any reasonable doubt that indeed remittances are an integral element of economic growth especially for developing countries. The study therefore recommends nations especially developing countries to make available the necessary infrastructure and investment climate that attracts personal remittance inflows from its citizens working in other countries in order to boost economic growth.

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