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Remittance and the Nepalese Economy

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Abstract : *The amounts of migrant remittance in Nepal have been mostly used in real estates by their families and dependents at home. In recent years, their investments in real estates have substantially gone up. But the recent global recession has adversely affected the flow of migrant remittance in the country. The Nepalese economy has, therefore, felt the pinch of the recession and the impact is evident from the slowdown of the economy to the reduction of overall spending by them. This article attempts to delve into various facets of remittances, its benefit, potential cost, trends, contribution to the Nepalese economy, policy implications, and so on*

I. INTRODUCTION

As an effect of globalization along with goods, services, and investment, people are crossing borders in record numbers. Each year between 2 million and 3 million people emigrate, with the majority of them going to just four host countries: the United States, Germany, Canada and Australia, in that order (World Bank, 2000). Due to increasing flow of international migration remittances have also been increasing in quick pace in the past few years.

When migrants send home part of their earnings in the form of either cash or goods to support their families, these transfers are known as workers' or migrant remittances (Ratha, 2005). Remittances represent the largest source of foreign income for many developing countries. In many developing countries remittances have been providing lifeline for the poor. According to the World Bank's publication (IMF, 2008) 'Migration and Remittances Fact Book 2008', India tops the list of countries that receive remittances from its citizens living in other countries. Indians living abroad sent home $27 billion in 2007. China, Mexico and the Philippines were the next largest recipient countries. For 2007, recorded remittance flows worldwide were estimated at $318 billion, of which $240 billion went to developing countries. This amount, however, reflects only transfers recorded in the balance of payments. Unrecorded flows through informal channels are estimated to be 50 percent higher than recorded flows.

In 2004, recorded remittances were the second largest source of external financing in developing countries, after foreign direct investment, and amounted to more than

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twice the size of official aid (IMF, 2005).Rich countries led by United States are the main source of remittance. United States is the largest source followed by Saudi Arabia, Switzerland and Germany.

II. BENEFITS OF REMITTANCES

Remittance inflow from foreign employment has been playing important role in developing countries like Nepal. Major benefits of remittances are as follows:

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First, remittances have more **direct impact on poverty**. Remittances augment recipient household's resources, smooth consumption, provide working capital, and have multiplier effects through increased household spending. Evidences confirm that remittances have poverty-reducing effect. The World Bank studies suggest that remittance have helped lower poverty (measured by the proportion of the population below the poverty line) in many countries.

Second, remittances have **impact on long-term growth** potential. It depends on how remittances are used. If it reduces domestic labour supply it might lower growth. However, if remittances are channelled to productive uses or investment, it may stimulate growth. Most studies suggest that a large proportion of remittances are used for human capital development such as in education, health care and nutrition, or consumption. It has been proved that there is long-term benefit of human capital development. Even if the remittances are spent on consumption they may spur local economic activity through multiplier effect.

Third, remittances have **impact on financial development**. Remittances enable low income households to access formal financial services. Remittances serve as collateral for small business start-up capital for individuals previously excluded from the formal sector. Evidences show that remittances promote financial deepening.

Fourth, remittances tend to be **more stable than capital flows**. Remittances are less volatile than most other sources of foreign exchange earnings. In countries affected by political conflict, they often provide an economic lifeline to the poor.

Fifth, Remittance flows also tend to be counter-cyclical. While capital flows tend to rise during upswings of economic cycles, and decline in bad times, remittances tend to be countercyclical relative to recipient countries' economies. They tend to rise when the recipient country suffers an economic downturn following a financial crisis, natural disaster, or political conflict. It is because migrants transfer more funds during hard times to help their families.

III. POTENTIAL COSTS OF REMITTANCES

Major defects of remittances are as follows:

First, if remittances are large, the recipient country could face the **risk of real exchange rate appreciation**. It may make its economy less competitive internationally. This can hurt export competitiveness in the recipient country.

Second, remittances, especially from skilled workers have been associated with **brain drain**. This is a cause of concern. Countries receiving remittances incur costs if the emigrating workers are highly skilled, or if their departure creates labour shortages. A brain drain can impair a developing country's capacity to harness modern agricultural and industrial technology.

Third, some argue that remittances can also **create dependency**. It may reduce recipients' incentive to work, and thus **slowing economic growth**. This along with shortage of skilled workers in the country may hurt the economic growth of the country in the long term. IMF in 2005, in one of its studies, showed that the remittances were negatively correlated with growth, that is, higher the receipts from remittances lower will be the growth rate. John Lyons said in an article that "Though remittances fuel some spending, there is not much evidences that they have added to sustained growth. Instead, the infusions of outside cash often distort the local economy and may diminish the long-term prospects for gains."

Fourth, remittances may also have human costs. Migrants make significant sacrifices. They have to remain separated from families, and incur risks to find work in another country. They may have to work extremely hard to save enough to send remittances. Many Nepalese workers are suffering hardship in gulf countries. It is often heard that many Nepalese girls in foreign employment have been the victim of sexual abuse.

To cut the arguments short, in the words of IMF economists Sanjeev Gupta and others (2007), "The bottom line is that remittances cannot be a substitute for a sustained, domestically engineered development effort. Moreover, large-scale migration may hurt domestic labour markets in specific sectors, particularly when those leaving are mostly skilled workers." However, no economists seem to be of opinion that migration should be stopped because of it being the lifeline of the poor residing in the poor countries, and also the largest source of foreign income for financing a country's development.

IV. TRENDS IN FOREIGN EMPLOYMENT OF NEPALESE YOUTH

Unemployment, particularly that of youth and educated, is increasing rapidly in Nepal. According to Nepal Living Standard Survey (NLSS), 2.9 percent of the population aged 15 years and above were unemployed and 74.3 percent were employed. The percentage of youth unemployed was 15.0. The size of the young population of the age group 15-29 years is estimated to have reached 6.5 million or more than 25.0 percent of total population (MOF, 2008). Most of them are without job.

The conflict in the country negatively affected industries and factories. Due to this, several industries and factories were completely closed, few were partially closed and, even the industries in operation could not operate in optimal capacity. As a result, a number of workers working in these industries and factories lost employment. Besides, due to the government's effort to create a small and efficient administration, new opportunities for employment could not be created. This added fuel to the fire of increasing number of unemployed. Due to the high poverty and the lack of employment opportunities in the country, and relatively very high real wages abroad Nepalese going abroad for employment has been increasing rapidly since last few years. However, there has been no reduction in the number of unemployed.

Table 1 shows the destination of foreign employment and total number of people gone for foreign employment.

Table 1: Destination of Foreign Employment

(Up to Fiscal Year 2007/08 Mid-March)

S. N.	Country/Region	Total Number	Percent
1.	Malaysia	4,12,181	36.5
2.	Qatar	3,22,944	28.6
3.	Saudi Arabia	2,16,798	19.2
4.	UAE	1,35,248	12.0
5.	Kuwait	13,374	1.2
6.	Bahrain	9,011	0.8
7.	South Korea	6,441	0.6
8.	Hong Kong	3,853	0.3
9.	Oman	2,892	0.3
10.	Other countries	8,065	0.7
	Total	11,30,807	**100.0**

Source: MOF/ GON, Economic Survey, 2007/08

During the FY 2005/06, 7, 73,592 numbers of persons were given permit for going for foreign employment. A total of 2, 04,533 persons were given permit in FY 2006/07 and 1, 52,682 persons up to mid-March 2008. Thus, the total number of persons issued permit for foreign employment totaled 11, 30,807 up to mid-March 2008. This is the data of persons going abroad only through institutional channel. There are many more going abroad through informal channels.

The trend of Nepalese going for foreign employment shows that the maximum number of 4,12,181 (36.5 percent of the total) have gone to Malaysia, followed by 3,22,944 (28.6 percent) to Qatar and 216,798 (19.2 percent) to Saudi Arabia. Similarly, 135,248 (12.0 percent) Nepalese have gone to the UAE, 13,374 (1.2percent) to Kuwait, 9,011 (0.8 percent) to Bahrain, 2,892 (0.3 percent) to Oman, 3,853(0.3 percent) to Hong Kong, 6,441 (0.6 percent) to South Korea and 8,065 (0.7 percent) to other countries. Israel and Macau have emerged as new destinations. A new trend is that women are also going for foreign employment through both formal and informal channels.

V. CONTRIBUTION OF REMITTANCES TO NEPALESE ECONOMY

It is, thus, obvious that due to the lack of opportunities at home and lucrative income abroad youths seeking foreign employment is increasing rapidly in the country. Since last few years remittance has been playing crucial role in Nepalese economy. Remittances have been the lifeline for the poor of Nepal as well. Table 2 shows the contribution of remittance to Nepalese economy.

TABLE 2: CONTRIBUTION OF REMITTANCE TO THE ECONOMY

Fiscal Year	Amount (Rs. In million)	As percent of GDP
2002/03	54203.3	11.0
2003/04	58587.6	10.9
2004/05	65541.2	11.1
2005/06	97688.5	14.9
2006/07	100144.8	13.8

Source: MOF/ GON, Economic Survey, 2007/ 08

Foreign employment has been able to bring large amount of remittance inflow to the country. It was Rs. 65541.2 million in 2004/05 which increased to Rs. 100144.8 million in 2006/07. The ratio of remittance as percentage of GDP was 11.1 percent in 2004/05 which was 13.8 percent in 2006/07. This amount is only transfers recorded in balance of payments. Unrecorded flows through informal channels are believed to be many times higher than recorded flows, and on this basis some believe that remittances contribute about 25 percent of GDP. Remittances contribute highest amount to the total foreign exchange earning, (table 3).

Table 3 presents the share of remittances in total foreign exchange earning.

Table 3: Share of Remittance in Total Foreign Exchange Earning

(Rs. In million)

Fiscal Year	Total foreign exchange earning	Foreign exchange earning as remittance	Remittance as percent of total foreign exchange earning
2002/03	98681.8	41630.0	42.2
2003/04	102643.2	56629.8	47.0
2004/05	123268.5	61784.8	50.1
2005/06	157297.3	92748.6	59.0
2006/07	179967.2	107417.4	60.0

Source: NRB, Quarterly Economic Bulletin, Mid-January 2008.

Table shows that the share of remittance in total foreign exchange earning was 42.2 percent in fiscal year 2002/03, which has been increasing every year and reached 60 percent in fiscal year 2006/07.

The poverty level declined in the country by 11 percent during 1996 – 2004 periods despite poor economic growth. Economic growth rate was mere 3.4 percent during the Tenth Plan period against the target of 6.2 percent. Target of the Tenth Plan was achieved in first 3 years and population below poverty line dropped to 31 percent. One of the causes of remarkable fall in poverty is attributed to the increasing inflow of remittance.

Remittance has helped family members back home to meet their basic necessities. However, the family members have been spending on consumption at a rate higher than growth in income. This has resulted into an increase in import which has led to further deterioration in foreign trade balance. It has also fuelled the increase in price level in recent years. The increase in imports has increased government revenue. Remittance has helped the government to maintain balance of payment in favourable position. Foreign exchange reserve of the banking sector has remarkably increased. This has increased the deposits of commercial banks and other financial institutions. This has, in turn, given incentive to commercial banks to maintain lower interest rates on deposits. The number of commercial banks and other financial institutions has increased as there is money floating around in the country.

Due to the enormous benefits of foreign employment to the country the governments of Nepal have been making plans to promote it. Despite this, some economists of Nepal are critical of this policy. As Raghab D. Pant (2008) holds, "This is the equivalent of promoting alcoholism to boost beer sales, or thinking that an epidemic is good for medical sector." It is because the country is exporting the able manpower that is essential to carry out development works in the country. It has lessened the need to increase domestic investment in order to increase employment opportunities within the country and to have sustained economic growth and poverty reduction.

Thus, Nepal will also have to experience both the costs and benefits of foreign employment. However, a country like Nepal has no better alternative right now than issuing permit to its youths to go abroad for work due to the dearth of employment opportunities in the country. Due to the worst investment climate existing in the country there is no hope in generating large employment in opportunities in the country for few years to come. Besides, the country might not be able to bear the potential costs of unemployment that generally come in the forms of crime, robbery, kidnapping, prostitution, and above all the social and political insatiability. According to the World Bank (1984) crime is tied primarily to poverty and social disorder, but tends to increase wherever there are large cohorts of young people who are unemployed. Likewise, J.S. Uppal (1979) had long before warned, "If unemployment persists, these disillusioned persons can become a potential danger to political stability, being highly susceptible to subversive elements in the society."

VI. POLICY IMPLICATIONS

Above mentioned facts indicate that sending most productive youths for foreign employment is not a policy choice but a compulsion on the part of the government of Nepal. However, the Government of Nepal needs to take measures to use remittances productively. For this the policy makers will have to take into mind the following things:

- Try to increase remittance flows from the formal channels. For this, the government will have to make effort to reduce transaction costs by making remittance service providers fix low remittance fee. Greater competition brings prices down. Hence, the entry of new market players can be facilitated.

- In order to use remittances more effectively recipient households should be brought into the formal financial sector. The recipients' propensity to save is also high. So, the policy makers should make effort to channel these saving into productive uses.
- Banks can promote investment from remittances by bundling financial services like savings products and entrepreneurial loans for households that receive remittances. Banks can use the flow of remittances as collateral for small business loans. The government can encourage the banks to do this.

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