

Mammoth remittances

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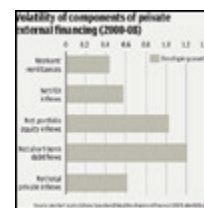
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Poverty estimates published by the World Bank in 2008 reveal that nearly 1.4 billion people in the developing world were living on less than \$1.25 a day in 2005, of which South Asia alone accounted for some 600 million people. This clearly indicates that much more remains to be done in order to ensure that the benefits of economic growth are more evenly distributed to make the goal of eradicating poverty worldwide more achievable.

In this regard, an area that urgently needs to be addressed is that of resource constraints that have severely limited poverty alleviation efforts globally. Most developing countries depend heavily on official sources of external financing such as grants and concessionary loans, which are often referred to as Official Development Assistance (ODA). ODA, which includes debt relief as one of its vital components, is especially important for many of the poorest countries burdened by heavy debt service payments. However, in view of decreasing net ODA disbursements (ODA including debt relief) from donor countries in recent years, it is necessary to consider other types of private sources of external financing that could help developing countries realise their developmental goals.

The World Bank data on net capital flows to developing economies reveals that net Foreign Direct Investment (FDI) inflows and workers' remittances are the most significant component of external financing for developing countries. Over the period 2000-07, on an average, FDI and workers' remittances made up about three quarters of the net total private inflows into the developing countries. Other notable components of external financing comprised of portfolio equity inflows and short-term debt inflows. While both these components have experienced more than a ten-fold rise in recent years, these types of capital flows tend to be highly volatile and hence might be considered rather unstable sources of financing.

It is interesting to note that despite the fact that workers' remittances alone have constituted one-third of net total private capital flows into the developing countries—second only to FDI flows—not much attention has been paid to this source of financing. This, despite the fact that there has been a marked increase in the magnitude of workers' remittances into the developing countries from about \$85 billion in 2000 to about \$280 billion in 2007 and it is estimated to surpass \$300 billion in 2008.



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Among the developing countries, South Asia has, on an average, received about 20% of global remittance receipts by developing countries between 2000 and 2007. In fact, remittance inflows to the South Asian region have actually remained quite resilient even during the global financial crisis. Like most other emerging economies, South Asia too experienced sharp net capital outflows following the global financial crisis. According to available estimates, net private capital inflows, which were \$112 billion in 2007, almost halved to \$66 billion in 2008. As

against this, remittance flows to South Asia actually remained stable with a slight upward bias, rising from \$52 billion in 2007 to an estimated \$66 billion in 2008, the same amount as total net private capital inflows to the region.

A lion's share of these inflows (about 70%) has come into India over the years. The average remittance inflows to India between 1995 and 2007 stood at about \$16 billion. For the corresponding period, the average inflows into Bangladesh and Pakistan were about \$2.7-2.8 billion respectively, while that to Sri Lanka was about half that at \$1.4 billion. While the absolute values indicate India's clear dominance as a host to South Asian remittance flows, this is not surprising either, in view of the fact that India constitutes about 80% of aggregate South Asian output. However, viewed in terms of the share of their respective GDP, Bangladesh actually has the highest share of remittances, about 10% in the year 2007, followed closely by Sri Lanka with a share of about 8%. In comparison, Pakistan and India lag behind with shares of 4% and 3%, respectively.

Apart from the magnitude of remittance flows, another important feature of the remittances component is their relative stability. Computations show that remittances are the least volatile, followed by trade flows, FDI flows and then by portfolio and short-term commercial bank lending. The last two components appear to be the most volatile in all countries and it is not without reason that these components are referred to as "mobile capital".

Beyond measures of volatility, arguably of much greater importance is the fact that, while private capital flows are generally considered pro-cyclical, i.e., capital flows rising at times of growth booms and falling during busts, remittances are generally expected to be counter-cyclical. Thus, remittances could serve as macroeconomic stabilisers during times of economic slowdown, as migrants are expected to increase the amounts of money they remit back home when most needed (i.e., during a downturn in their home country).

As a significant portion of migrants' incomes are being spent in destination countries, this could also provide for the much-needed economic stimulus to spur domestic demand in times of economic distress. Also, in contrast to other types of capital flows, workers' remittances do not create liabilities such as debt servicing in future.

An important area of policy concern that needs to be addressed by all concerned countries, though, is the presence of excessively high transaction costs associated with remittance transfers.

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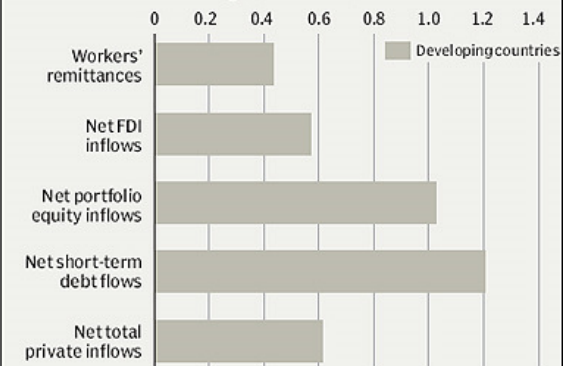
Remittances in select South Asian economies

\$ billion, GDP(%)

Year	Bangladesh		Pakistan		India		Sri Lanka	
	Remittances	GDP	Remittances	GDP	Remittances	GDP	Remittances	GDP
1995	1.20	3.17	1.71	2.82	6.22	1.75	0.81	6.21
1996	1.35	3.31	1.28	2.03	8.77	2.26	0.85	6.13
1997	1.53	3.61	1.71	2.73	10.33	2.51	0.94	6.24
1998	1.61	3.64	1.17	1.88	9.48	2.28	1.02	6.48
1999	1.81	3.95	1.00	1.58	11.12	2.47	1.07	6.85
2000	1.97	4.18	1.08	1.45	12.89	2.80	1.17	7.14
2001	2.11	4.48	1.46	2.02	14.27	2.99	1.19	7.53
2002	2.86	6.01	3.55	4.92	15.74	3.10	1.31	7.65
2003	3.19	6.15	3.96	4.76	21.00	3.50	1.44	7.62
2004	3.58	6.34	3.95	4.03	18.75	2.68	1.59	7.69
2005	4.31	7.16	4.28	3.91	21.29	2.63	1.99	8.16
2006	5.43	8.77	5.12	4.02	25.43	2.78	2.18	7.73
2007	6.56	9.59	6.00	4.20	35.26	3.29	2.53	7.81

Source: Compiled from World Development Indicators, World Bank

Volatility of components of private external financing (2000-08)



Source: Author's calculations based on Global Development Finance (2009), World Bank