Migration, Money Remittances and their Effects on Household: A Synthesis of Literatures

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Abstract

Migrant remittances are a steadily growing external source of capital for developing countries of which Nigeria belong. While foreign direct investments and capital markets flows fall sharply in the last years due to recession in the high income countries, migrant remittances continued to grow. Remittances may indirectly affect household income through changes in the labour supply of those remaining behind; relaxation of working capital constraints that expand income from entrepreneurial or farming activities; and multiplier effects on household income factors that determines money remittances are multifaceted. These factors that have been articulated by myriads of studies are elucidated in this paper. Consequent upon various outcomes as articulated in this paper, it was recommended that policy measures that frees billions that go to transfer companies in form of profit to get to migrants household should be pursued.

Keywords: *Remittances, Determinant, Altruism, Money, Migrant household, Literature Review.*

1. Introduction

Remittances to developing countries have dramatically increased over the past few years. According to the World Bank's Global Economic Prospects (2006), remittances to middle and low-income countries amounted to about 30 billion Dollars in 1990. Fifteen years later, they are estimated to have reached about 170 billion dollar, implying annual growth rates that are well above 10 percent. Remittances now account for about 30 percent of total financial flows to the developing world and provide significant foreign exchange earnings. The dramatic increases in remittances observed at the global level over the past few years has been mirrored in Nigeria. In fact, officially recorded remittances flows to the country have increased tremendously since central Bank of Nigeria (CBN) began collecting data on remittances in 2002, CBN reported approximately US $2.26 billion, $2.66 and $3.56 in remittances for 2004, 2004 and 2006 respectively. These figures probably under-estimates the tremendous rate of increase in international remittances to Nigeria, in as much as large amount of such income enters the country in a way that is not counted. To buttress this, IMF (2005). Statistics showed while total remittances to Nigeria Via formal channel in 2005 were $2.6 billion; fund remitted through informal channels exceeded $3 billion. Although this estimate is likely to be on the high side, it never-the less highlights the fact that a collapse in remittances appears unlikely in the near future. In other words, the assumption that remittances are here to stay at least in the short run is realistic.

Some evidence indicates that remittance flows have positive macro-economic effects in recipient countries. Large remittances flows improve a country's credit worthiness for external borrowing and hence, enhance that country's credit worthiness for external borrowing and hence, enhance the country's access to International capital markets. Moreover. Some financial Institutions in developing countries have been able to tap into international capital markets under relatively favourable conditions through securitization of future flows (Acosta et al 2007).

Given the nature, magnitude, and evolution of remittance flows, development practitioners now view remittance as having potentially important role to play in supporting the development effects of recipient countries. Remittances can support these efforts through two main channels. First, remittances could flows to the neediest groups of the population and therefore, directly contribute to poverty reduction. Even if these flows are fully consumed, a concern of many development practitioner, they could have significant positive welfare effects. Second, with imperfect insurance and financial markets, remittances could contribute to increased investment in human and physical capital. For example, they could remove some of the financial constraints to investment faced by household and small-scale entrepreneurs. Similarly, remittances can provide insurance and, therefore, allow households and entrepreneurs to pursue riskier asset accumulation strategies. In this regard, remittances could help raise the country's long-run growth potential through higher rates of capital accumulation.

In practice, however, other effects may counter balance these potential positive impacts. For examples, if important costs are associated with the act of migrating, migrants may not come from the lowest quintiles of the income distribution and therefore, remittances may not flow to the poorest people. Thus the location of the recipient households in the income distribution and the magnitude of the corresponding flows are taken into account.

Remittances can also negatively affect returns on capital. For examples remittance can exert pressure on the exchange rate and lead to a real appreciation, which all other factors being equal, would lower the profitability of the tradable sector. Similarly remittances may raise reservation wages and negatively affect labor supply (Rodrigues and Tiogson 2001). In both cases, remittances would affect the investment incentives of households and entrepreneurs and would lower the rate of capital accumulation.

In general, researchers and policy makers have tended to take a rather pessimistic view of how remittances are spent or used and the impact of these remittances on economic development. For example, Chami *et al* (2003) reports three stylized facts: first that a "significant proportion, and often the majority", of remittances are spent on consumption; second, that a smaller part of remittance funds goes into saving or investment; and the third, the ways in which remittances are typically saved or invested in housing, land and jewelry – are not necessarily productive to the economy as a whole.

This paper contributes to the existing literature in that it articulates findings of previous works with an attempt to synchronise theories on remittances and key channels of how remittances affect household economy and economic growth. Apart from the fore-going, the rest of the paper is structured as follows: Section 2 elucidates the determinants of money remittances while the indirect effects of remittances on household income and welfare are discussed in section 3. The paper ends with conclusion and recommendations.

2. Determinants of money remittances

The level of migrants' remittance flows depends on both the migrants' ability, i.e. their income and the savings from income, and their motivation to remit savings back to the home country. Of course, the willingness to remit is also determined by the duration of migration (how long do migrants intend to stay abroad, temporarily or permanently?), the family situation of migrants (single, married, with or without children?), and network effects (do migrants move alone, with family members, and do they keep attachments to those left behind?) (For the growing importance of network effects see Munshi, (2003). One way of looking at the determinants of remittance flows is by analyzing the motives that migrants have to remit money. The literature distinguishes between pure altruism, pure self-interest, informal agreements with family members left in the home country and portfolio management decision. As Stark (1991) points out, no general theory of remittances exists. The studies that analyse this phenomenon provide useful descriptive evidence and results from empirical research, but they only explain it partly, and are characterized by certain geographical, socio-cultural and temporal limitations.

Pure altruism

One of the most intuitive motivations for remitting money back home is what has been characterized in the literature as "altruism": the migrants' concern about relative left in the home country. Under an altruistic model, the migrant derives satisfaction from the welfare of his/her relatives. The altruistic model advances a number of hypotheses. First, the amount of remittances should increase with the migrant's income. Second, the amount of remittances should decrease with the domestic income of family. And third, remittances should decrease over time as the attachment to the family gradually weakens. The same should happen when the migrant settles permanently in the host country and family members follow. Empirical evidence from Botswana gave support top the first prediction. A 1% increase in the migrant's wage, ceteris paribus, induced increases in remittances ranging from 0.25%, at low wage levels, to 0.73%, at high wage levels. However the correlation between remittance levels and home incomes was found to be insignificant. Thus, altruism was found to be insufficient for explaining the motivations to remit, at least for Bostwana (Lucas and Stark, 1985). Altruistic motives to remit were found also in recent studies on United States immigrants. Households with children at home are approximately 25% less likely to remit than households without children present. In addition, immigrants with minors left in the country of origin are more than 50% as likely to remit money home (Lowell and de la Garza, 2000). In Nigeria however, works on altruism are quite scarce.

Pure self-interest

Another motive for remitting money to family members in the home country may be pure self-interest. First, a migrant may remit money to his/her parents driven by the aspiration to inherit, if it is assumed that bequests are conditioned by behavior. Second, the ownership of assets in the home area may motivate the migrant to remit money to those left behind, in order to make sure that they are taking care of those assets. Empirical evidence from Kenya and Botswana shows that wealthier parents received a larger share of migrant earning through remittances (Lucas and Stark, 1985). However it cannot be clearly discerned whether the motive was to inherit or to ensure the household took care of the migrants are motivate to remit for reasons of self-interest, and in particular for asset accumulation and investment in the home areas (Brown, 1997). Third, the intention to return home may also promote remittances for investment in real estate, in financial assets, in public assets to enhance prestige and political influence in the local community, and/or in social capital (e.g. relationship with family and friends). Empirical evidence from the Greek migration experience shows that per migrant, remittance flows from Greek migrants in Germany were much higher (experiencing a “return illusion”) than from Australia and the United States (experiencing a “permanent settlement syndrome”) (Glytsos, 1997). United States immigrants exhibit the same remittance behavior: each 1% increase in the time spent in the United States decreases the likelihood of remitting by 2% and immigrant’s political lobbies in the United States are half as likely to remit as the rest (Lowell and de la Garza, 2000). Canada, a country that receives mainly permanent immigrants, registered a similar experience, with immigrant households spending just a modest portion of their budgets on remittance. On average, 2 to 6 % of their total household expenditures were devoted to this category (DeVoretz, 2004).

Implicit family agreement: co-insurance and loan

Household arrangements, particularly within an extended family, may be considered more complex in the real world, and certainly more balanced as under the two extremes: pure altruism” and enlightened self-interest”. In this model remittance determination is placed in a family framework of decision-making, with remittances being endogenous to the migration process. For the household as a whole, there may be a Pareto-superior strategy to allocate certain members as migrants, and remittances should be the mechanism for redistributing the gains. Two major sources for potential gains are taken into account: risk-spreading and investment in the education of young family members. In this context, the intra-family understanding is seen as an “implicit co-insurance agreement”, respectively as an “implicit family loan agreement” (see Agarwal and Horowits, 2002 for an empirical case study). The implicit contract between migrant and family is safeguarded against being breached by the family specific assets, i.e. credit and loyalty, but also by self-seeking motives of the migrant, i.e. aspiration to inherit, investment in assets in the home area and maintenance by family, and the intention to return home with dignity.

In the implicit co-insurance model, it is assumed that in a first phase, the migrant plays the role of an insuree and the family left at home the role of the insurer. The family finances the initial costs of the migration project, which in most cases are substantial. It is expected that the potential migrant is unable to cover all the expenses alone. The high extent of uncertainty related with the implementation of a migration intention may be minimized by the financial support from home. In turn, the migrant can act also as an insurer for the family members back home in a second phase of the migration process.

This is expected to be possible when the migrant has already a secure employment, high enough earning and has positive expectations about further income. By receiving remittances, the family will then have the opportunity to improve its consumption, to undertake investment projects including much more risk and thus reach a higher level of utility. Evidence from Botswana shows that families with more cattle receive significantly more remittances in periods of drought (Lucas and Stark, 1985).

The loan agreement model was theorized as displaying a "three waves" shape. In a first stage, remittances are assumed to be the repayment of an informal and implicit loan contracted by the migrant for investment in education and migration costs. In a second stage, they are loans made by migrants to young relatives to finance their education, until they themselves are ready to migrate. In this phase, the amounts remitted are expected to diminish in aggregated numbers because not all migrants are expected to give a loan to family members. Then, in the third stage, before returning to their original country, migrants invest accumulated capital at home, therefore the amount of remittances increases. Later, the next generations of emigrants repay the loan to the former emigrant-lenders, who may have retired in the home country. Given the nature of the loan, remittances cannot consequently be reduced over time-as the co-insurance or altruistic theory predicts – and are mainly used for consumption purposes. Empirical estimations for Botswanan's rural to urban migration showed that migrants' years of schooling, and the years of schooling of their own children, are positively and significantly correlated to remittances, given support to the loan agreement hypothesis, Empirical support was found as well from Tonga and Western Samoa, due t the regularity of remittance flows (Poirine, 1997). However, survey data on migrants from the theses countries in Sydney provide no evidence that in situations where parents have invested more in a migrant's education, they will remit more than otherwise (Brown, 1997). Recent empirical studies also reject the loan agreement hypothesis. A 1998 marketing study of Latino households in the United States showed that migrants' education has a strong impact on remittances, with each additional year of education reducing the likelihood of remitting by 7% (Lowell and de la Garza, 2000). The results of another study with macroeconomic data from over 30 developing countries are suggesting the same behavior of migrant workers. These results are striking, suggesting that brain drain flows are not compensated by remittances (Faini, 2002).

The migrant's saving target

Another way to model remittance determination is to assume that the migrants' goal is to return home with a certain amount of savings – the saving target.[4] Thus, remittance flows during the migrants' stay abroad result from a bargaining process between the migrant and his/her family. The claim of the family left at home on the migrant's income is considered as the demand side and the ability of the migrant to remit, i.e. income and the savings from income, as the supply side for remittances. The migrant has an interest in reaching the saving target and to minimize the drains from the income (i.e. consumption expenses in the host country and the money remitted to the family). Therefore the expectations of future income are continuously being revised and a nexus of inter-related factors are adjusted, including the length of stay, the intensity of work, and the flow of remittances for the family's consumption. On the other hand, the family is regarded as having as its goal an income (including remittances) larger than that of the neighbors, in order to justify the decision to send some family members abroad. Thus, the amount of order to justify the decision to send some family members abroad. Thus, the amount of remittances depends on the migrant's income, the per capita income in the home country and the bargaining power of the two parties. Empirical evidence for the support of the saving target hypothesis was found for Greek-German migration in the period 1960-1982, and for migration from seven Mediterranean countries (Algeria, Egypt, Jordan, Morocco, Syria, Tunisia and Turkey), the remittances being positively correlated to the per capita income in the host as well as in the home country (Glytsos, 1997, 2001).

In a recent paper, Lucas (2004) summarises the answers to the question whether migration for permanent settlement results in lower remittances than temporary migration. Temporary migrants might have higher incentives to remit to those left behind than permanent migrants (Galor and Stark, 1990). Morever, the longer migrants stay abroad, the lesser are the bonds to the sending economy and the lower are the remittances (Merkle and Zimmermann, 1992). On the other hand, migrants are better paid the longer they live in the destination country. Thus they could (if they wish) remit more. Lucas (2004, p. 13) concludes that remittances may initially rise, then decline with duration of stay, which "would suggest an optimal length of stay to maximize remittance flows, balancing greater earning power against diminishing attachment".

Portfolio management decisions

Most of the current literature on the determinants of remittances is concentrated on the individual motives to remit, rather than on macroeconomic variables. To be sure, aggregate remittance flows will reflect the underlying microeconomic considerations described above, which determine individual decisions about remittances. Nevertheless, it is reasonable to expect that there are some macroeconomic factors, both in the host and home country, which may significantly affect the flow of remittances. Migrants' savings that are not needed for personal or family consumption may be remitted for reasons of relative profitability of savings in the home and host country, and can be explained in the framework of a portfolio management choice. In contrast to remittances for consumption proposes, the remittance of these kinds of savings have an exogenous character related to the system of migration, and are expected to depend on relative macroeconomic factors in the host and home country, i.e interest rates, exchange rates, inflation, and relative rates of return on different financial and real assets.

Relying on such assumption, governments of migrant sending countries used to implement incentives schemes, i.e. premium exchanges rates, foreign exchange deposits with higher returns, etc. in order to attract remittances from their Diasporas. However, contrary to the conventional belief, empirical results for Turkey of the period 1963-1982 illustrate that neither variations in exchange rates (reflecting the governmental intention to attract remittances by premium exchanges rates), nor changes in the real interest rates (reflecting the government intention to attract remittances by foreign exchange deposits with higher interest rates) turned out to affect the amounts of remittance flows. The flows of remittance towards Turkey depended more on political stability rather than economic returns. An environment of confidence in the safety and liquidity of savings was much more important than options of possible higher returns (Straubhaar, 1986).

According to some scholars, microeconomic factors are more significant in determining remittance flows in the long run, while portfolio considerations are presumed to have only a short-term effect, essentially by shifting remittances around the long-term trend. In addition, the macroeconomic environment – especially in the home country – may substantially influence the choice of the channel for transferring the money. Therefore, this issue can become crucial for the amount of officially recorded transfers. Inflation in the home country was found to have a negative impact on remittances, perhaps reflecting uncertainties from the perspective of the remitters (Glytsos, 2001). Similarly, remittances became volatile in the Philippines following the financial crisis at the end of the 1990s, and suffered a decline as the economy slipped into crisis in 1999 and 2000 (Ratha, 2003).

It should be pointed out that these numerous hypotheses trying to explain migration decision and remittances are not mutually exclusive. In fact, it may be the case that remittances are driven by all of these motives at the same time, each one explaining a part of the remittance amount or period of remitting practice. One of the elements can predominate over the others for a period or for a sample of migrant workers, and their roles can be later interchanged. This implies the complexity of the remittance phenomenon and its determinants, and explains the challenges of developing a universal theory.

Since systematic research on the determinants of workers' remittances was undertaken in the 1980s, there has been a recognition that an important part of the money remitted back home by migrant workers flows through informal channels. An unstable macroeconomic environment in the home country was assumed to be a significant reason for choosing informal remittance mechanisms by the migrants. However, systematic research on transfer mechanisms has been carried out only in the last years. Here the focus has been on: i) the typology of the transfer mechanisms, ii) the comparative cost transfers through different mechanisms, and iii) the choice of the transfer means and money transfer market evolutions.

3. Remittances and indirect effects on household income

Remittance may indirectly affect household income through changes to the labor supply of those remaining behind; relaxation of working capital constraint that expand income from entrepreneurial or farming activities; and multiplier effects on household income. Unfortunately, the evidence on each of these channels is quite limited, so this paper is constrained here to identifying important areas for additional research.

Remittance may affect labor supply

Remittances may tend to reduce the supply of labor provided by remaining household members, who may take a portion of the remittance gain as leisure. This income effect is generally not a concern, because it represents part of the welfare gain from remittances. By contrast, remittances may change the return to supplying labor, for example, if the migrant conditions the remittance on low household income. Such a *substitution effect* will reduce the welfare gain from remittances by distorting household labor decisions.

However, it is difficult to separate income and substitution effects of remittances on the labor supply of those remaining behind. Looking at the overall effect, a rise in remittances reduced labor force participation in Managua, Nicaragua, but increased self-employment (Funkhouser 1992). Remittances were estimated to reduce the participation rates of remaining household heads in a number of Caribbean countries, although the direction of causality was hard to establish (Itzigsohn 1995). Yang (2004) points to more encouraging labor-supply effects than the standard model when he determined that remittances reduce the supply of child labor but increase that of adult labor.

Remittance provide working capital

There is some evidence that remittances provide working capital to households that lack access to credit markets. For example, migration to South Africa's mines initial reduced agricultural production in countries of origin, because labor was removed from the farm (Lucas 1987). However, over time production rose with migration, perhaps due to remittance-funded capital investment and a greater willingness to take risks with agricultural production, owing to the more diversified sources of family income. Remittance had a small negative effect on household income for Mexico in 1982, but a large positive effect for 1988 (Taylor 1992). One possible explanation is that over time development of migrant networks allowed migration form poorer households that are more likely to be credit constrained. The effect of remittances on household income depends on both the liquidity of household assets (which determines their value as collateral) and on the availability of inputs that complement entrepreneurial activity (Taylor and Wyatt 1996). The role of remittances in relaxing household credit constraints in rural cropping income in China dominated the direct loss of productive labor from migration, so that internal migration increased per capital household income (excluding remittances) by 14 to 30 percent (de Brauw, Taylor, and Rozelle 2001). Mishra (2005) found that a 1 percentage point increase in remittance inflows in 13 Caribbean countries increased private investment by 0.6 percentage point (all measured relative to GDP).

Remittance may ease credit constraint because a stable stream of remittance income may make households more creditworthy in the eyes of formal sector financial institutions. Remittance receipts that increase when the household receives an adverse shock may be even more important in relaxing credit constrains, since they increase the lender's confidence that they will be repaid even if things turn out badly for the household. This creditworthiness effect deserves careful empirical investigation, given the increasing interest in channeling remittances through formal financial channels.

Remittances may have multiplier effects

Some studies have found that remittances have a multiplier effect, whereby the increase in domestic income is some multiple of the remittance income. For example, each dollar sent by Mexican migrants to the United States was estimated to boost Mexican GDP by $2.90 (Adelman and Tylor 1992). Such multipliers will occur if output is constrained by insufficient demand. However, in many developing countries sustained underemployment is likely to have supply-side causes, for example, government policies that increase the cost of hiring and firing workers, so that increased demand will ultimately result in higher inflation rather than increased output.

Nevertheless, there may be greater scope for sustained multiplier effects at the regional level. The local spending of remittance income will generate further income for other local households, which in turn is likely to cause local inflation for non-traded goods and possibly a small increase in national inflation. A national government with a formal or informal inflation target is likely to respond to any increase in the national inflation rate by tightening monetary policy, thereby leading to an offsetting effect would be multiplier effects at the local level but not at the national level. Indeed, the local gains come partly at the expense of the region that do not receive the remittance but the forced do suffer the tighter monetary policy.

Remittance also may have multiplier effects in the context of increasing returns, typically as the expansion of one sector increases the optimal size of other sectors. Although such income-expanding feedback loops could be present at the national level, they are gain more likely to be relevant at the regional level, because expanding regions attract labor and capital from elsewhere in the economy. The bottom line is that remittance-induced multiplier effects cannot be ruled out-especially at the regional level-but our current empirical understanding of their importance is quite limited.

Remittances can lead to investments in education and health

Some of the clearest evidence for remittance-induced investments comes from work on human capital. The dramatic depreciation of the Philippine exchange rate during the Asian financial crisis increased remittances for Filipino migrants (because from the migrants' perspective, exchange-rate depreciation raised the relative price of their own consumption in the destination country compared with consumption by household members back home), leading to greater child schooling reduced child labor, and increased educational expenditure in origin households (Yang 2004).[28] In El Salvador, remittance are estimated to reduce the probability of children leaving school by 10 times the effect of other sources of income in urban areas and by 2.6 times in rural areas (Cox Edqards and Ureta 2003). They speculate that remittances have a disproportionate influence on schooling expenditures because the migrant has made it a condition for financial support. Mexican children in households with migrants completed significantly more schooling, with the largest impact (an additional 0.89 years of schooling) for girls in households where the mother has a low level of education (Hanson and Woodruff 2003).

Health status is both an important component of human capital and a central element of well-being in its own right. Unfortunately, the effect of migration on the health of family members remaining behind-notably children-is poorly understood. Migration from Mexico is associated with lower (by 3 percent) infant mortality and higher birth weights of children left behind (Hildebrandt and McKensie (2005). The positive health effects come through increased access to health-related knowledge as well as through increased household wealth. Notwithstanding these encouraging outcomes, the authors caution that the impact of migration on child health is quite nuanced, the migration on child health is quite nuanced, with migration associated with lower measures of preventive health care such as breast-feeding and vaccinations. De and Ratha (2005) find that in Sri Lanka, remittance income has a positive and significant impact on the weight of children under five; this results is especially strong for female-headed households. However, the health impact of absenteeism of one of the parents is negative.

Remittances can encourage entrepreneurship

There has been a marked shift from the belief that migrants are unlikely to establish new business enterprises in their countries of origin (either upon return or through remittance financing) to the view that migration encourages entrepreneurship. Large receipts of remittances from the United States are associated with a greater likelihood of productive investment in Mexico (Massey and Parrado 1998).[31] A survey of 6,000 small firms in 44 urban areas in Mexico shows that remittances are responsible for almost 20 percent of the total capital in urban micro-enterprises (Woodruff and Zenteno 2001). The share rises to one-third for the 10 states with the highest rates of United States-bound migration. Remittances also appear to ease credit constraints on new Business formation in the Philippines (Yang, 2004). The effect of exogenous increases in remittance income on the probability of entering into entrepreneurship is larger for low-to-middle-income household, which are the ones most likely to face credit constraints.

4. Conclusion and Recommendation

Remittances may indirectly affect household through various factors embedded in this paper namely – labour supply, provision of working capital, expansion of income from farming/entrepreneurial activity, multiplier effects etc. The evident provided in body of the work may be insufficient but it evident remittance impact positively on household income generally.

The different hypotheses attempting to explain remittance motivations – pure altruism, pure self –interest implicit family agreements, the migrant's saving target and portfolio management decisions – complement each other. Some or all of these motives together may simultaneously drive remittances, each one explaining a part of the amount remitted or a period of remitting practice. One motive can predominate over the other for a period or for a sample of migrants with same characteristics, and their roles can be interchanged. This illustrates that the remittance phenomenon is a very complex one, and explains the difficulties in developing a universal theory of remittance determination.

A significant part of the money remitted by international migrants goes to the transfer companies as profit rather than to the migrants' families in developing countries. A reduction of the costs of remitting money to the level charged by the financial institutions with the cheapest transfer services (such as commercial banks), would free up several billion each year for poor households in Africa. This can be achieved by two set of policies in remittance-sending countries. First policies that target fair competition and efficient markets for remittance transfers. For instance ensuring transparency in pricing and greater consumer awareness about migrants to open bank accounts and thus give access to cheaper transfer services.

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