

## Remittance: Role and Challenges in Nepalese Economy

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### Abstract

*Both developing and developed countries have made a significant study of remittance and labor migration. Developing countries have attained benefits from remittance to uplift economic activities like maintaining household consumption, increasing pattern of saving and investment, receiving foreign currencies for imports, making favorable balance of payments, diplomatic activities, enhancing social and infrastructural development and maintain macroeconomic stability. The study explores the role and challenges of remittance in Nepalese economy. No doubt, Nepal as least developing country attains lots of benefits from remittance and labor migration. Along with such economic and social benefits, remittance generates a lot challenges in economy such as brain drain, trade deficit, shortage of man power, higher labor cost, backwardness of productive sectors of economy and a lot of social problems. The study also points out of effective use of remittance that helps to mobilize internal resource to create employment opportunities in a country with a formulation of proper implementation of necessary policy regarding a proper utilization of remittance.*

**Key Words:** Remittance, Labor migration, Benefits, Challenges, Effective uses

### Introduction

Nepal is a small and least developed country. Gross domestic production (GDP) of Nepal is 3,000 billion and per capita income is 1,004 US \$. There are 21.6 percent people (60 Lakh) under absolute poverty line and there are more than 37 percent people under multi-dimensional poverty line. Average economic growth of Nepal of recent one decade is 4.3 percent (MoF, 2017). Nepal has targeted to be developing country by 2022 and targeted to be middle income country by 2030. Remittance is a very important capital source for developing countries like Nepal. Remittance is significantly higher in low-income and middle income group of countries than in other developing countries (DoFE, 2014). Remittance to low and middle-income group of countries reached a record high in 2017 (World Bank, 2017). Remittance has been crucial for social and economic development of developing countries. The World Bank estimates that officially recorded annual remittance flows to low and middle-income group of countries reached US \$ 529 billion in 2017, remittance flows to low and middle-income group of countries are expected to reach US \$ 550 billion, to become their largest source of external financing. Remittance to South Asia grew 12 percent to US \$ 131 billion in 2017, outpacing the 6 percent growth in 2017 (World Bank, 2017). According to a report released by World Bank, Nepali migrant workers sent

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home US \$ 8.1 billion in 2017 making it the 19<sup>th</sup> biggest beneficiary of funds sent by migrants around the world. The remittance was up to 16.39 percent year-on-year despite a drop in the number of departures. As a share of the GDP for 2017, Nepal is among the top five recipient smaller economies, along with Tonga, Kyrgyz Republic, Tajikistan and Haiti. South Asian countries are in the top 20 list of biggest beneficiaries of remittance with Nepal taking the fourth spot in the region. It is behind India (US \$ 78.6 billion), Pakistan (US \$ 21 billion) and Bangladesh (US \$ 15.5 billion) but ahead of Sri Lanka (US \$ 7.5 billion) in terms of remittance (World Bank, 2014). Employment continues to be the most significant motivation for international migration from Nepal. In the past consecutive fiscal years 2015/16 and 2016/17, the Department of Foreign Employment (DoFE) issued 786,564 permits for foreign employment to over one hundred destination countries (Asia Foundation, 2017). Malaysia and the Gulf countries have been the most attractive destinations, receiving 86.42 percent of all male and female labor migrants in the past nine fiscal years. Of the total 3,554,683 permits issued over that period (including DoFE and EPS), 29.88 percent were for Malaysia followed by Qatar (at 21.57 percent), Saudi Arabia (20.37 percent), United Arab Emirates (UAE) (10.62 percent), Kuwait (2.54 percent), Republic of Korea (1.32 percent), Bahrain (0.86 percent) and Oman (0.63 percent). Malaysia was the top country of destination for Nepali migrant workers in the past nine fiscal years. The data shows that majority of the migrant workers who went to Malaysia, both male and female, engaged in manufacturing factories as a production worker or general labour at 59.52 percent of all migrant workers. Nearly 85 percent of the female migrant workers were listed as factory workers. Majority of Nepalese migrant workers going to Saudi Arabia went as a general labour (Asia Foundation, 2017).

Remittance has been determinant factors in socio-economic development of Nepal since the last two decades. It is one of the largest sources of financial flows to developing countries. It is a steadily growing external source of capital for developing countries. Remittance and foreign employment are interlinked. As labor migration on foreign countries increases, remittance also increases. Remittance can increase the well-being of receiving households by smoothing consumption and improving living conditions. It can facilitate the accumulation of human capital by making possible improved sanitary conditions, healthier life styles, proper healthcare, and greater educational attainment. Remittance can ease the credit constraints of unbanked households in poor rural areas, facilitate asset accumulation and business investments, promote financial literacy, and reduce poverty etc.

To make advanced economy of a country, remittance must enhance productive sectors of the economy. Otherwise, imports increases resulting balance of payments unfavorable, which is witnessed in current economy of Nepal. It ultimately endangers economy of Nepal if the country does not properly utilize resources. High consumption and less production seem to be contradictory in Nepalese economy. Nepalese economy faces economic dependency which was directly experienced after undeclared blocked by India in 2015.

### **Role of Remittance on Nepalese Economy**

Remittance is being common issues within last two decades. From the late 1990s, remittance became a vital source of income (Tahir, Khan, & Shah, 2015). Both physical and human investment have a larger impact on the economic growth in a long-term perspective, while direct consumption on primary goods activate a multiplier effects of aggregate demand which results beneficial to the entire economy. In developing countries, both remittance and foreign direct investment (FDI) are important for accelerating economic growth. Studies

show that remittance and FDI have improved the economic growth of Pakistan economy. This could be the case of other developing countries as well. Migration has long been an important livelihood option for the Nepalese people so that remittance contributes to more than a quarter of the country's gross domestic product at present (Piya, 2016). Remittance is not only helping in maintaining macroeconomic stability, it also has shown some positive impact on microeconomic indicators. At the household level, remittance helps to smooth consumption and increase investment in human and physical assets (Acharya & Leao-Gonzalez, 2014).

Remittance constitutes an important source of foreign exchange for developing countries like Nepal. It is identified overseas remittance achieving a favorable balance of payments and as well as creating a new resources base for the country (Ali, 1981). Migration generates source of income that supports to the family members of migrants that enabling them to invest in education, health and housing. Thus, it helps for improving household living conditions and reducing vulnerability of family members, especially women and children. Remittance increases the diversity of consumption and investment and thereby playing an important role in stimulating the economy. Remittance has a multiplier effects on economy as it is used for investment that stimulates demand for goods and services.

Remittance contributes to the GDP as well as foreign exchange earnings of developing countries at a greater extent. With remittance, an economy can spend more than it produces, import more than it exports, and invest more than it saves (Connell & Conway, 2000). Remittance inflow is a phenomenon with the increased emigration of Nepali workers over the past one decade that has been receiving attention in the Nepali macroeconomic environment. A part from eradicating poverty in the Nepalese rural areas, remittance inflow has also maintained the balance of payment situation (World Bank, 2014).

### **Challenges of Remittance on Nepalese Economy**

Nepalese workers are mostly unskilled and professionally untrained because of which they do not have reasonable wages on the one side and they have to do highly risky jobs abroad on the other side. Furthermore, there is no guarantee of job, wages and other facilities as contracted before. Many of them have lost their life and property in the past in foreign countries. So, there are security problems of migrants that hinder threat to remittance receiving countries like Nepal (Ojha, 2013). Migrant syndrome or braindrain also creates problems in remittance receiving countries. The more the phenomenon creates remittances the more it feeds itself, creating a vicious circle of migration. Logically, this phenomenon affects all the productive sectors of the country, triggering some negative effects, which then hit the whole economy (Oruc, 2011). However, remittance is not devoid of adverse effects. Manpower exports country has many barriers in normal functioning of the economy. A major portion of remittance is used for land-plot purchase, daily consumption, loan repayment and housing. Mostly, remittance is used for normal expenditure (79 percent) while a very small portion (2 percent) is used for investment (Devkota, 2016).

Remittance is used for functioning of general living and only 33 percent of return emigrants invested in the business enterprises in Algeria, Morocco, and Tunisia (Gubert & Nordan, 2011). It is used more for basic consumption, health care, and education for the household members than business investment. Similarly, high remittance-earning people allocate more to housing than to other sectors in Nigeria (Osili, 2004). Through the exchange rate channel, remittance inflows may be so significant in volume as to result in the appreciation of the real exchange rate of the receiving economy. The result in reduction of

foreign trade competitiveness and adversely affects the balance of trade as well as the economic development of the receiving economy (Okodua & Olayiwola, 2013). This could also generate resource allocation from the tradable to the non-tradable sector, known as the Dutch disease.

One of the critical negative effects of increasing remittance inflows in a developing economy is the infection of the Dutch-Disease through reduction in international competitiveness. A continuous and significant inflow of remittance can lead to increase in demand for the domestic currency. Hence, real appreciation of the exchange rate which in turn reduces the international competitiveness of the country's exports whilst imports are made relatively cheaper (Shera & Meyer, 2013). There is a negative correlation between remittance and economic growth and the growth rate of remittance is inversely correlated with the per capita GDP growth. There is a negative relationship between remittance and economic growth as it reduces the incentive to work by the migrant family members (Chami et al., 2003).

Remittance can reduce labor supply and create a culture of dependency that inhibits economic growth. It can increase the consumption of non-tradable goods, raise their prices, appreciate the real exchange rate, and decrease exports, thus damaging the receiving country's competitiveness in world markets. Remittance can be curtailed along with international migration by escalating anti-immigrant sentiment and tougher enforcement practices in host countries, including the US and many in Europe and the Gulf region (Amuedo-Dorantes, 2014).

Migration negatively affects agriculture yield and remittance receiving agricultural households have not demonstrated improvements in agriculture productivity, despite increased household incomes. It points to two important trends; firstly, migration adversely affects agriculture yield by inducing a labor shortage in the sector, and secondly, the remittance-receiving households are not investing such incomes on productivity-enhancing agricultural capital goods and inputs. Therefore, a key development challenge for a highly remittance-dependent agrarian economy like Nepal is to incentivize remittance receiving agriculture households to invest in capital goods and inputs to improve agriculture productivity so that it more than compensates for the yield losses arising from labor migration (Tuladhar, Sapkota, & Adhikari, 2014). Remittance deteriorates GDP per capita growth in Nepal. The main channels of remittance are the consumption and investment that influence economic growth. An increase in inflows of remittance decreases agro-product. The increased demand is met by imports from Indian markets. There is no evidence of association of remittances and investment but they are positively associated with consumption.

However, remittance brings both positive and negative impacts to the socio-economic condition of Bangladesh and the positive impacts are more effective than the negative one. The government of Bangladesh and other relevant associations need to consider with due importance. For government, several rules and regulations favorable to the migrants and remittance flow should be formulated. Several investment opportunities can be created so that the remittance of transnational migrants can be utilized properly (Ahmed, 2014). The main challenges remain how best to assess the impacts of remittance and how to design policies that facilitate the transmission and productive use of remittance flows while taking into account the idiosyncrasies of each country. Possible policies range from easing capital controls to reforming immigration policy.

### **Conclusion and Recommendations**

Nepal is one of the highest remittance receiving countries in the world in percent of GDP. Remittance has both positive and negative impacts to the economy. Remittance plays an important role as sources for household consumption, investment, transforming the structure and dynamics of the overall economy. Remittance has important role to make favorable current account of BoP by providing foreign exchange that can be used for the imports of capital equipment, raw materials, capital formation, investment on education and human capital creation etc. Remittance also contributes to raise the living standard of households and reduce poverty. Remittance can be taken as one of the major sources of capital formation in the context of Nepal. Because a huge amount of capital is needed for enhancement of productivity and accelerating economic development. Remittance has helped improve the social and economic conditions on nutrition, living condition, shelter, education, health care, poverty reduction, social security, and investment activities of the recipient households.

Despite positive effects of remittances, there are a lot challenges due to labor migration. Various challenges in an economy increase like brain drain, imports of luxurious goods, making trade deficit, social and cultural problems etc. Rapid labor migration has also made increased divorce rates in various parts of county that have generated various family issues and social problems in Nepal. Both remittance and imports ratio have been increasing simultaneously over the years. Because, as remittance increased, about 80 percent of it spent on consumption and thereby obviously increases the demand for goods and services. It can be fulfilled either through imports or by expanding domestic production. Due to less industrial development and domestic production, imports of Nepal have been drastically increasing. Similarly, due to less developed agricultural sectors and high consumerism, Nepal's economy is getting problematic. Declining rate of exports and the increasing rate of imports produce a trade imbalance thereby making unfavorable BoP.

Families having increased remittance tend to migrate from villages to urban areas where they spend more on consumption rather than investment in productive sector. This has created various problems in city area for water supply and garbage management. Village areas are facing the problems of youth manpower thereby remaining inactive of agricultural land. Strategic plans and programs for main streaming the incoming remittance to financial system for their productive use is the urgent need in order to avoid any possibility of the country's economy to suffer the Dutch-disease. Going with the current trends of consumption in Nepal, if the remittance is soaked up by consumption only and are not turned into investment in productive sector, the short term boost provided by it in the economy will not be sustainable. Productivity will decline and the economic choices get tougher if the situation is not addressed in time and is stalled being momentarily content with the remittance based income.

The government should develop appropriate training and education programmes to assist returning migrants or remittance receipts in making effective investment decision. Moreover, the appropriate infrastructure should be developed to generate favorable investment environment and be complement investment out of remittance. The capital, skills and technology which migrant workers bring back home country are among the most valuable gains from foreign employment that should be properly utilized by the government. Government has to formulate the policies to encourage returned migrants to be involved themselves in productive activities. So, the government should formulate proper utilization of remittance policy to channelize the amount in productive sector. Then, remittance would create employment opportunities and minimize imports in turn. Policies are needed to

encourage the use of remittance to promote long term growth and income security. Similarly, remittance through official rather than unofficial mechanism has been increased and this should be stopped. The government should encourage migrants to hold their savings in financial assets in the country rather than holding them abroad. It is needed to encourage migrants to become investor in productive assets in the country. To promote investment of remittance in business enterprises is very urgent and there is a need for the government to provide adequate incentives for migrant workers to invest in productive activities in Nepal.

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