Africa's remittances:

Levering service policies for sustainable economic development

Abstract

Given the rising inflows of remittances to Africa, this essay argues that migrants' monies are the continent's best resource to spur stable economic development. The essay begins by conducting a literature review to explain the advantages of remittances over other financial flows. Next, the essay refers to African-focused research, as well as to macro-level indicators from the Sub-Saharan region, to reveal a steady counter-cyclical inflow of remittances since 2002. Policy recommendations include the need to focus on diaspora-engagement, migration reform, and reduction of transfer service costs. The conclusion offers suggestions for future research and links the essay to WTO's objectives.

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I. Introduction

Africa's steady economic growth over the past decade has given reason for optimism, but the continent is yet to fully utilize one of its most abundant financial resources: remittances from international migrants. The purpose of this essay is twofold: 1) compare remittances to other financial flows to Africa; and 2) explain how African as well as migrant-hosting countries can enact more efficient service policies relating to the transfer and investment of migrants' monies.

Given both the rising inflows of remittances to Africa and the inherent advantages of this type of inflows over others (e.g., aid), the essay argues that remittances are the continent's best resource to spur sustainable development at the macro-level, and to ensure genuine income stability and poverty reduction at the micro-level. In support of its thesis, the essay resorts to a literature review and data analysis. Given the succinct length of the essay, the analysis focuses exclusively on African's Sub-Saharan region in the 2002-2012 timeframe.

The essay is divided into four parts. The first part summarizes the current theory, literature and policies relevant to remittances, especially in the African context. The second part reveals the most up-to-date data on Africa's socio-economic indicators. The third part conducts an analysis of data for Sub-Saharan African countries. Policy recommendations are included in the conclusion.

II. Context

1. Theory

Despite the often technical definitions, remittances may be defined simply as "money transfers by migrants to their relatives or other persons in countries of origin."[i] The theoretical explanation of remittances flows relates to migrants' micro-level remitting behaviour, which is based on the "motivations to remit." The motivations can be divided into three categories: altruism, self-interest and household obligations.[ii] Altruistic remitting is based on non-beneficial, charitable help for those in need. Self-interested remitting is based on a expected benefit for the sender, be it symbolic (e.g., prestige) or material (e.g., inheritance).[iii]

Household motives stem from the new economics of labour migration theory, which stipulates an agreement, be it implicit or explicit, between the remitter and other household members.[iv] The agreement binds the remitter to send money as part of a shared household income; remittances may also be a form of repayment for help (e.g., funding for travel) that the sender

received from the household. In practice, it is difficult to detect the main motivation, since more than one may be involved.

2. Empirical Literature

Most studies in the remittances literature focus on the impact of the inflows. The studies typically utilize multinational datasets to empirically test the effect on macro-level indicators. So far, most conclusions regarding impact on GDP growth have been cautiously optimistic.[v] In Sub-Saharan Africa (SSA), remittances are found to have a "poverty-mitigating effect, and promote financial development."[vi]

Yet, some studies find the impact on growth to be smaller than expected, which may be due to an "illusionary" increase in remittance flows,[vii] or only a limited potential impact in "fragile states" that lack the necessary market conditions.[viii] Also, even in countries with the right conditions, remittances may have negative implications, including the Dutch disease, increased inequality, "dependency", "public moral hazard" or funding of terrorism.[ix]

Nevertheless, a view has emerged that remittances may have an equal or even better developmental impact than foreign aid. In many developing countries, remittances already surpass the volume of aid and foreign investment combined.[x] "Aid optimists" view remittances as a compliment to aid, whereas critics point to aid's drawbacks such as volatility, selectivity and corruption.[xi] The two main differences between remittances and aid stem from the fact that since they accrue to private households rather than the government: 1) remittances are less prone to corruption or mismanagement by central authorities; but 2) they are rarely used for large-scale developmental projects.[xii]

In regards to the motivations, evidence from South Africa suggests that self-interest applies to single individuals whereas household motives apply to married ones.[xiii] Furthermore, the central debate in the literature is whether remittances are pro- or counter-cyclical; most authors favour the latter argument.[xiv] In addition, a key macro-level determinant of remittances are "shocks", which are expected to result in an altruistic "insurance effect" that increases remittances. For example, remittances were found to increase after a hurricane and heavy rainfall.[xv] However, they were found to decrease when a national currency weakens, thus indicating the role of financial self-interest.[xvi]

Also, migrants may still remit even if their primary reason for going abroad was not economic. In countries undergoing conflict, as is the case in some African countries, migrants may depart hastily for security reasons rather as a part of a family income strategy.[xvii]

3. Policies

Although remittances policies are strongly influenced by migration policies, it is beyond the scope of this essay to address the latter in detail. Instead, three types of policies relating to remittances merit mention: diaspora-engagement policies; labour-migration policies; and remittances-transfer policies.

The role of diasporas in the economic development of home countries has grown to become a separate genre in migration studies.[xviii] Depending on the relation between a diaspora and its home country (i.e., government), the diaspora can promote or boycott the country's growth by sending or withholding remittances; at the same time, the home country can appeal to the diaspora for help, or be indifferent or even antagonistic. For example, the large volume of remittances from the Somali diaspora exemplifies both its's attachment to the home country as well as the government's successful engagement strategy with citizens abroad.[xix]

Despite the evermore "free" global market in trade and capital flows, there remain strong barriers to the flow of people. Given the administrative barriers and high costs of migration outside of Africa, most African migrants take part in South-South migration within the continent.[xx] While most migrant-sending countries have embraced remittances as a contributor to economic growth, the perception of such financial outflows in migrant-receiving countries remains controversial. Although migrant-receiving countries may benefit economically from the arrival of the often required and usually cheaper labour, migration remains a sensitive political issue. Populist discourse often portrays migrants are intruders, and remittances as proof migrants' lack of integration or an ingredient to corruption or terrorism in the foreign countries.[xxi]

Transfer policies typically remain the purview of the private sector, unless national governments are concerned that remittances are being used for funding criminal or terrorist activities; such concerns may have negative, discriminatory impact on remitters.[xxii] Transfer costs impact remittances not only by reducing the value of migrants' income that is received by the household, but also by diverting a portion of flows into informal channels, which pose accounting issues for central authorities and financial risks for the senders. It is commonly acknowledged that

at least a quarter of remittances is transferred by unofficial channels.[xxiii] Since women tend to remit smaller amounts than men, but more frequently, high costs disproportionally disadvantage women.[xxiv]

III. Data Analysis

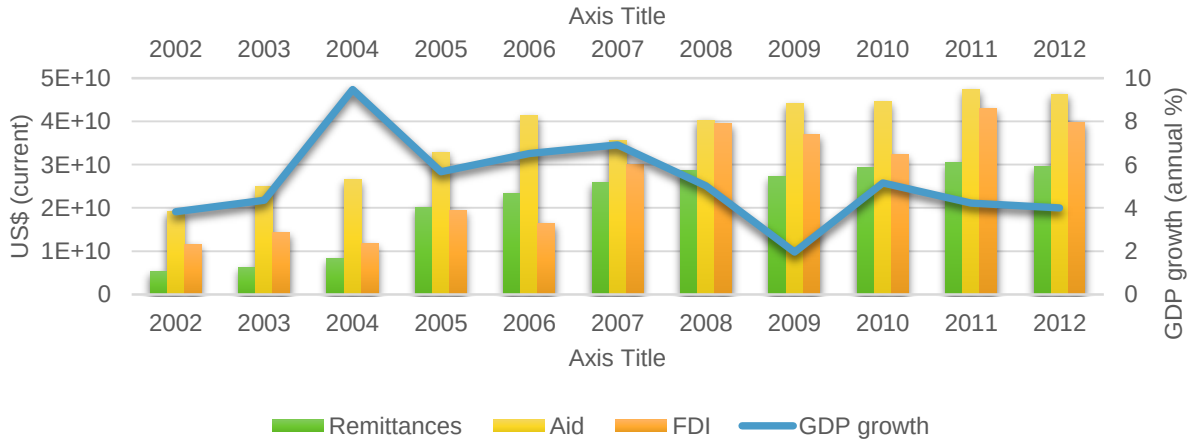
Africa's GDP grew close to six percent annually between 2002 and 2008, fell to just three percent in 2009, but is predicted to recover to five percent by 2016.[xxv] This growth, however, is yet to be enjoyed by 388 million "poor" who subside on less than US$ 1.25 a day. [xxvi]

In (SSA), GDP growth steadily reached 3.8 percent in 2002, peaked at 9.5 percent in 2004, fell to 1.9 percent in 2009, and finally recovered to 4.0 percent in 2012.[xxvii] Unfortunately, 42.7 percent of SSA population subside at less than US$ 2 day. [xxviii]

In the same timeframe, remittances to SSA grew six-fold from US$ 5.2 billion in 2002 to US$ 29.5 billion in 2012.[xxix] In comparison, aid to SSA only doubled from US$ 19.1 billion in 2002 to US$ 46.3 billion in 2012, remaining stagnant since 2009.[xxx] Also, foreign investment tripled from US$ 11.5 billion in 2002 to US$ 39.8 billion in 2012.[xxxi]

However, during the 2008-2009 global crisis, remittance flows remained almost unchanged, while aid and FDI decreased substantially. Had it not been for remittances, GDP of many African countries might have reached below one percentage growth or even contracted. Overall, the crisis not only proved Africa's vulnerability to fluctuating commodity prices and financial flows, but also highlighted for the first time the continent's reliance on remittances as a stable, counter-cyclical source of income.

Table 1. Sub-Saharan Africa



Although the "global average total cost" of sending remittances decreased slightly - from 7.68 percent to 7.52 percent in second quarter of 2015 - there remain regional disparities, especially in Africa.[xxxii] Among the G20 nations, South Africa is the country *from which* it is the most expensive (15.19 percent) to send remittances, and it is the second country *to which* it is the most expensive to send remittances (8.98 percent), after China (10.18 percent). Overall, Sub-Saharan African is the most expensive (9.78 percent) region *to which* to send remittances. The high costs result in a diminished developmental impact of remittances in SSA.

IV. Policy recommendations

In order to reap remittances' benefits, African countries need to further improve three policy areas. First, they need to more closely engage African diasporas, especially those in developed countries, which may have income to send back to home countries, but are facing administrative hurdles (e.g., underdeveloped banking system) or financial risks (e.g., unstable investment climate). Appeals to the diasporas should be made both by direct information campaigns abroad, and by genuine market reform (e.g., currency stabilization) at home.

Second, African countries need not only to establish more effective migration policies domestically (e.g., passport issuing), but also more closely engage with migrant-receiving countries to ensure the proper entry and treatment of migrants abroad. The current migration crisis in Europe has exemplified the seeming helplessness of African authorities in face of large-scale migrant flows, including human trafficking; also, it has revealed a severe lack of coordination between countries of Africa and the European Union in their migration management efforts.

Third, also with cooperation with migrant-hosting countries, African nations need to reduce remittances transfer costs, which are often unregulated by central authorities and are thus set arbitrarily high by monopolistic service providers.[xxxiii] Improved service policies should include a set maximum service fee, less arduous documentation for senders, and more service point outlets in home countries. Anti-monopoly and anti-corruption initiatives have the potential to bring down costs and improve service efficiency.

V. Conclusion

The increase of remittances inflows to Africa has outpaced those of aid and FDI, and may soon surpass both flows in absolute numbers. Given the reviewed advantages of remittances -

especially over aid - and their counter-cyclical nature, migrants' monies are the most stable and direct resource for economic development for African countries. At the macro-level, remittances lead to growth thanks to spending on consumer goods, agriculture and housing, which generates a "spillover effect" throughout the economy.[xxxiv] At the micro-level, remittances improve recipients' standard of living by raising incomes above the poverty level, and by increasing spending on healthcare and education. The implementation of the recommended policies inevitably requires the establishing government agencies focusing on diaspora engagement, migration management and remittances streamlining. However, the huge developmental potential of remittances justifies the cost of running such agencies.

Future research should explore at least three areas: 1) impact of remittances on micro-level indicators; 2) impact of home countries' service policies and market conditions on remittances flows; and 3) impact of host countries' service as well as migration policies on remittances flows. Improvements in data collection and dissemination would allow for more in-depth analysis using statistical methods.[xxxv]

Given the spread of information technology and the internet in Africa, there is potential for more households to have access to quick and inexpensive access to financial resources, which they can use for immediate needs and long-term investment as they see fit. In this sense, remittances are not only the most effective, but also the most democratic, financial resource available. Since the WTO's objectives include "raising the standards of living for Members, ensuring full employment, large and steadily growing volume of real income […] while allowing for the optimal use of the world's resources",[xxxvi] then remittances should be the integral means for achieving those objectives in Africa.

Word count (excluding footnotes & works cited): 1984

[i] IOM 2013. According to the World Bank, "Personal remittances is the sum of personal transfers and compensation of employees. Personal transfers, a new item in the Balance of Payments Manual 6th Edition (BPM6), represents a broader definition of worker remittances. Personal transfers include all current transfers in cash or in kind between resident and nonresident individuals, independent of the source of income of the sender (and regardless of whether the sender receives income from labor, entrepreneurial or property income, social benefits, and any other types of transfers; or disposes assets) and the relationship between the households (regardless of whether they are related or unrelated individuals)." (https://datahelpdesk.worldbank.org/knowledgebase/articles/114950-how-do-you-define-remittances) Accessed Oct. 27, 2015. For further elaboration of remittances' definitions, see Alfieri & Havinga (2006), Chami et al. (2008) and IMF (2011).
[ii] Lucas & Stark 1985; Taylor 1999; Clarke & Wallsten 2003; Goldring 2004; Das 2012
[iii] Naiditch & Vranceanu 2011; Reeves 2012
[iv] Stark 1978 & 1991; Lucas & Stark 1985; Schiff 1994; Taylor 1999
[v] Adams & Page 2003; Ratha & Mohapatra 2007; Chami et al. 2008; Özden & Schiff 2006; Combes & Ebeke 2010; Combes al. 2012; Das & Serieux 2010; Ukueva 2010; Das & Chowdhury 2011; Javid et al. 2012; Salahuddin 2013
[vi] Gupta et al. 2009
[vii] Clemens & McKenzie (2014) attribute the recent increase in recorded remittances to improved accounting methods.
[viii] Impact of "state fragility" on the developmental potential of aid, investment or remittances is an emerging topic in the literature (Fagen 2006; Lindely 2007 & 2009; McGillivray & Feeny 2008; Lum et al. 2013).
[ix] Abdih et al. 2008; Wouterse 2008; Dhungana 2012; Mascarenhas & Sandler 2013
[x] WB 2014
[xi] "Optimists" include Adelman (2003), Combes et al. (2012) and Hundson Institute (2012). Critics include Boone (2006), Easterly (2003), Grabel (2008), Nielsen et al. (2011) and Brückner (2013).
[xii] Rosenzweig 2005
[xiii] Gubhaju & Jong 2009
[xiv] Ratha & Shaw 2006; Chami et al. 2008; Grabel 2008
[xv] Clarke & Wallsten 2003; Yang & Choi 2007
[xvi] Lueth & Ruiz-Arranz 2007
[xvii] Ratha & Shaw 2006; Lindley 2007 & 2009
[xviii] Newland, & Patrick 2004; Brinkerhoff 2009; USAID 2009; Lum et al. 2013
[xix] Lindley 2007
[xx] Bakewell 2009
[xxi] Horst et al. 2014
[xxii] Horst et al. *ibid.*
[xxiii] de Haas 2005; Ratha 2005
[xxiv] IOM 2013
[xxv] African Development Bank Group 2015
[xxvi] Africa. Poverty headcount ratio at $1.25 a day. 2012 data. (http://databank.worldbank.org/data/views/reports/ReportWidgetCustom.aspx?Report_Name=POV_REG_1&Id=be849c9d&tb=y&dd=n&pr=n&export=y&xlbl=y&ylbl=y&legend=y&isportal=y&inf=n&exptypes=Excel&country=SSA&series=SI.POV.NOP1,SI.POV.DDAY&zm=n) Accessed Oct. 29, 2015.
[xxvii] Sub-Saharan Africa (all income levels). Annual percentage growth rate (annual %) of GDP at market prices based on constant local currency. (http://data.worldbank.org/indicator/NY.GDP.MKTP.KD.ZG) Accessed Oct. 29, 2015.
[xxviii] Sub-Saharan Africa. Poverty headcount ratio at $1.90 a day (2011 PPP) (% of population). (http://data.worldbank.org/topic/poverty#boxes-box-topic_cust_sec). Accessed Oct. 29, 2015.
[xxix] Sub-Saharan Africa (all income levels). Personal remittances, received (current US$). (http://data.worldbank.org/indicator/BX.TRF.PWKR.CD.DT) Accessed Oct. 29, 2015.
[xxx] Sub-Saharan Africa (all income levels). Net official development assistance and official aid received (current US$). (http://data.worldbank.org/indicator/DT.ODA.ALLD.CD) Accessed Oct. 29, 2015.
[xxxi] Sub-Saharan Africa (all income levels). Foreign direct investment, net inflows (BoP, current US$). (http://data.worldbank.org/indicator/BX.KLT.DINV.CD.WD). Accessed Oct. 29, 2015.
[xxxii] World Bank Group 2015
[xxxiii] International Fund for Agricultural Development. "Africa: market and financial access." (http://www.ifad.org/remittances/maps/africa.htm) Accessed Oct. 29, 2015.

[xxxiv] Serino & Kim 2011; IMF 2014

[xxxv] So far, World Bank's database offers very limited information on Africa's countries. (http://data.worldbank.org/)

[xxxvi] "Background - 10th WTO Ministerial Conference, Nairobi, 2015." (http://mc10nairobi.org/en/mc10-nairobi/background) Accessed Oct. 29, 2015.

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