

# The Effects of Remittance on Economic Growth in Nepal

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## ABSTRACT

The cross-border movement of workers has increased with the enactment of economic liberalization policy, especially after the 1990s in Nepal and increasing globalization in the world. It opened the door to the Nepalese workers in abroad, making their remittance one of the prime sources of foreign exchange earning in Nepal. Consequently, solving the problem of unemployment, remittance become the major contributor in Nepalese economy accelerating overall economic growth of the country; it is the major source of financial savings and thereby investment and growth. Despite the increasing importance of remittance in Nepalese economy, the overall impact of remittance on economic growth has not been adequately explored yet. This paper analyzes the effects of remittances on the economic growth of Nepal. Previous studies have found mixed results regarding to impact of remittances on economy- i.e. positive effects as well as negative effects of remittance on economic growth. So, this paper examines which effect is predominant in Nepalese context. The multiple regression model (OLS) is employed in the study in order to identify the effects of remittances on economic growth of Nepal. The time series secondary data for 20 years, 2001-2020, are collected from various published sources. This study concludes that there is positive and significant relationship between remittance and economic growth in Nepal. The impacts of other control variables, government expenditure and export trade are also positive for growth. However, expenses made on human capital has lagged effect, making insignificant in short run. The government of Nepal and concerned agencies should provide skill development trainings for the Nepalese migrants to increase their income in host countries. Government should encourage migrants to send remittances only from formal banking channels. It even helps for capital formation, investment and economic growth. It also solves the liquidity crisis and foreign exchange constraints in the nation, promoting the infrastructure development on the nation.

**Keywords:** Labour Migration and Remittance, Economic Growth, Real GDP, Multiple Regression, Human Capital

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## 1. INTRODUCTION

With the increased adaption of economic liberalization policy, increasing globalization and with the coming up of WTO, the cross-border movement of workers has increased. This has encouraged the workers to move from low income and underdeveloped countries to developed, industrialized and emerging economies in search of employment opportunities. This policy has also influenced the movement of outmigration of Nepalese workers basically after 1990s. Nepalese youths go abroad in search of employment opportunities due to economic and non-economic reasons. Even though inflow of remittance is considered good for the recipient nations, there are a number of negative consequences. Mostly income received is largely used for consumption purposes, it has a little impact on long-term economic growth of the country. Historically, migration from the developing countries has been a source to fill up the labour shortage in the developed nations under the guest worker policy during the post-war (World War – II) period. Under this policy, a large number of Turks migrated to Germany, Pakistanis to Saudi Arabia and the Mexicans to United States of America.

Migration of Nepalese people for employment in foreign countries has a long history of around 200 years back. It is believed that such migration started before early nineteenth century when the first Nepalese travelled to Lahore to join the army of Sikh ruler of Punjab, Ranjit Singh. Labour migration started after the Anglo-Nepal treaty of peace and friendship of 1816 which recruited 3000 Nepalese soldiers in British Gurkha Regiment. The signing of a peace and friendship treaty between India and Nepal in July 1950 was a turning point in the movement of Nepalese migrants to India. Nepalese people are recruited to the Indian Army, Police force, civil service and private sectors. Likewise, the oil boom of 1970s has created many employment opportunities to the Middle East Gulf –Countries for unskilled and semi-skilled workers (Shrestha, 2004). With the enactment of Foreign Employment Act 1985, Nepalese people started to migrate beyond India particularly to the Gulf-countries, where the oil boom has created a massive demand for labour. Even in present, the migration to Gulf-countries, Malaysia, South Korea, Japan, and other countries is still rise.

Nepal had implemented economic liberalization policy since 1990s. The total volume of trade is increasing year after in which the volume of imports is increasing rapidly; and there is slow change in export of Nepal. The total trade deficit was NPR 9,076.8 million rupees in 2004 and in 2020, it has reached at NPR 86, 321.0 million rupees (MoF, GoN-2020). Thus, increasing deficit in foreign trade has limited the foreign exchange earnings. There is slow growth of tourism sector in few years, especially due to COVID pandemic, resulting the significant loss in the foreign exchange earnings from tourism. Nepal was food surplus country till 1990s, and now we have shortage of food for ourselves. In this situation, the provision of foreign employment and inflow of remittances have not only helped to minimize the unemployment, but also injected the significant amount of foreign currency in Nepal.

According to the Census year 2001, the population growth of Nepal was 2.25 percent, and 1.35 % in 2011. The most recent growth rate as per 2021 census is 0.93 percent per annum. It shows that there is a still high population growth in Nepal. Every year around 500,000 labour force enter into Nepalese job market in search of employment opportunities. However, very few of them could get employment in Nepal. So, searching job in foreign countries became the ultimate option for large number of unemployed Nepalese people. Even though there are a lot of potentialities in Nepal, due to the failure of Nepalese economy to transform from subsistence agriculture to industry, service, tourism sector, widening the scope of export trade, highly unstable politics, etc. are major reasons for slow growth of employment opportunities in domestic economy (Sigdel, 2010). As a result, in an average 1500 people go abroad every day for jobs in a normal situation. Remittance earned from foreign countries have become a fundamental source of financial inflow in Nepalese economy. Various studies conducted by researchers argued that remittance helps in employment generation, reduces the problem of unemployment, increases the foreign exchange earnings, and thus contributes to accelerate overall economic development. World Bank (2011) found that almost half of all the households of Nepal had at least one migrant in abroad. Remittance received by foreign countries contributed a quarter of the income of all the households and almost two-thirds of the income for those receiving money from abroad. Similarly, World Bank (2012) argues that remittances contribute to growth of output in the economy by increasing the consumption, investment demand, and savings.

According to the World Bank, the top ten remittance receiving countries in 2020 are presented in Table 1.

**Table 1**

*Top Ten Remittance Receiving Countries as of 2020*

S.N.	Country	Remittance ( US \$ billion)
1	India	83.1
2	China	59.5
3	Mexico	42.9
4	Philippines	34.9
5	Egypt	29.6
6	Pakistan	26.1
7	France	24.5
8	Bangladesh	21.8
9	Germany	17.9
10	Nigeria	17.2

*Source: World Bank Data (2021)*

According to the World Bank data, the inflow of remittance and remittance as percentage of GDP in SAARC countries as of 2019 are presented in Table 2.

**Table 2**

*Remittance and its contribution in the SAARC Nations*

S. N.	Country	Amount (US \$ billion)	Remittance as Percentage of GDP
1	India	83.10	2.8
2	Pakistan	26.10	7.9
3	Bangladesh	21.80	5.8
4	Nepal	8.10	27.3
5	Sri Lanka	6.70	7.8
6	Afghanistan	0.86	4.6
7	Bhutan	0.47	1.7
8	Maldives	0.04	0.1

Source: World Bank Data (2021)

The share of Gulf countries in the total remittance inflow to Nepal was 50.3 percent. According to Nepal Rastra Bank, Nepal received a total of Rs 304.97 billion remittance, out of which Rs 153.26 billion was received from the Gulf countries (NRB report, 2020). Among Gulf countries, the biggest amount of remittance was received from Qatar which was Rs 53.93 billion (17.7 percent) followed by UAE at Rs 40.87 billion (13.4 percent), Saudi Arabia at Rs 38.15 billion (12.5 percent), Rs 11.52 billion (3.8 percent) from Kuwait, Rs 8.79 billion (3.8 percent) from Bahrain, Rs 29.66 billion (9.7 percent) from Malaysia in the year 2019 (Kafle, 2020). The country wise inflow of remittance from different host countries to Nepal in the year 2019 is summarized in **Table 3**.

**Table 3**

*Country wise inflow of remittance in Nepal (As of 2019)*

Country	Amount of Remittance (Rs billion)	As Percent of Total
Qatar	53.93	17.7
Malaysia	29.66	9.7
UAE	40.87	13.4
Saudi Arabia	38.15	12.5
Japan	22.87	7.5
South Korea	6.15	2.0
India ( from Formal channel)	43.16	14.2

India ( from Informal channel)	38.00	N. A.
Kuwait	11.52	3.8

Source: Kafle, Laxman (*The Rising Nepal*, 28 Jan 2020).

The year wise inflow of remittance in Nepal, annual percentage change and remittance as percentage of GDP since 2000/01 to 2019/20 are given in Table 4.

**Table 4**

*Remittance, its annual percentage change and as Percentage of GDP*

Year	Amount of Remittance (Rs billion)	Annual Percentage change in Remittance	Remittance as Percentage of GDP
2000/01	47.2	274.6	10.6
2001/02	47.5	0.6	10.3
2002/03	54.2	14.1	11.0
2003/04	58.6	8.1	10.9
2004/05	65.5	11.9	11.1
2005/06	97.7	49.0	14.9
2006/07	100.1	2.5	13.8
2007/08	142.7	42.5	17.5
2008/09	209.7	47.0	21.2
2009/10	231.7	10.5	19.4
2010/11	253.6	9.4	18.5
2011/12	359.6	41.8	23.5
2012/13	434.6	20.9	25.6
2013/14	543.3	25.0	28.0
2014/15	617.3	13.6	29.0
2015/16	665.1	7.7	29.5
2016/17	695.5	4.6	26.0
2017/18	755.1	8.6	24.9
2018/19	879.3	16.5	25.4
2019/20	875.0	- 0.5	22.4

Source: MoF, GON. *Economic Survey, various issues from 2000/01 to 2020/21*

It is real fact that contribution of remittance income earned by Nepal is more than what is shown by official data and information. Few studies were conducted to explore the impacts of remittance on very small aspects. Thus, my study found the research gap in the field of macroeconomic effects of remittances in economic growth of Nepal.

The research question and the main problem to be addressed are: How does remittance income sent by Nepalese workers from host countries contributes for economic growth of Nepal? A comprehensive study is required to explore this issue. Thus, this study aims to identify the macroeconomic effects of remittance on Nepalese economy.

## 2. LITERATURE REVIEW

Literature review is basically a “stock taking” of available literature in one’s field of research or selected topic for research (Wolf and Pant, 2000). The purpose of literature review is, thus, to find out what research studies have been conducted in one’s chosen field of study, and what remains to be done. Literature review, in this research, identifies the various issues related with foreign employment and remittances by various international researchers, institutions, policy institutions, domestic researchers and institutions. The literature review is focused on studies that have examined the effect remittance on economic growth. It will cover both country specific and cross-country studies. The previous studies have found positive and negative relationship between inflow of remittance and economic growth of country.

The summary of review of literatures from international perspectives and Nepal specific studies are summarized in Table 5 and Table 6.

**Table 5**

*Tabular Summary of Review of Literature from International Perspective*

Author/Year	Sample	Variables Used	Methodology	Results
Olayungbo & Quadri (2019)	Twenty SSAC 2000 – 2015	GDP, FDI Remittance., Population., Trade, Inflation	PMG, ARDL	Positive relationship between remittance and growth
Meyer et al., (2016)	Six high remittance receiving nations 1999 – 2013	GDP per capita, Remittance, GCF, Consumption, School enrollment, Pop.	Multiple Regression Model	Remittance has positive impacts on growth
Mannan et al., (2015)	Bangladesh July – Dec, 2013	Real GDP, Inv. Education, Employment	Multiple Regression Model	Strong relationship between household relation to migrant and remittance
Fayissa et al., (2010)	36 African Nations from 1980 – 2004	Real GDP, Remi., Enrollment, GFC, F. Aid, FDI, Trade,	Neo-classical Growth Model	Remittance has positive impact on growth
Singh (2010)	36 SSA Countries 1990 – 2008	N. A.	Multiple Regression Model	Negative relation between remittance & growth
Ziesemer (2009)	Four different countries pooled data	GDP, Remi., Saving, Inv, GFCF, Interest	GMM – HAC	Effects are weak in rich and strong in weaker nations
Ahortor (2009)	31 SSA & LAC 1996 – 2006	Real GDP, Remi., Inv, HC, CPI, BOP, Govt. Exp.	Panel Model GMM	Remittance contributes more on long run
Pradhan et al. (2008)	39 developing countries 1980 – 2004	Real GDP, PCI, Remi., Inv, Trade, Govt. Policy	Multiple Regression Model	Remittance has positive effects on growth

**Table 6***Tabular Summary of Review of Literature from Nepal Specific Studies*

Author/Year	Sample	Variables Used	Methodology	Results
Kaphle (2018)	Nepal 1976 – 2017	Remi., Trade, GDP Growth	Log-Log Econometric Model	Long run relationship between remittance & growth
Uprety (2017)	Nepal 1976 – 2013	Remi., GDP Per Capita, Inv., Consumption	VAR Model	Negative effects of remittance on growth
Pant (2017)	Nepal NLSS – III	Remittance, Education, Consumption,	TEM	Remittance supports indirectly for growth
Dhungel (2016)	Nepal	GFCF, Remi., Enrollment, PCI, Trade	ARDL Bound Testing	Long run relationship between remittance & growth
Sapkota (2013)	Nepal 1996 – 2006	Remittance, Trade	Effect analysis	Slow impact on growth
Neupane (2011)	Nepal 1990 – 2008	Consumption, Inv., Growth, Remittance	Simultaneous equation Model	Positive relationship between remittance & growth

### 3. METHEDOLOGY

As this study is related with time series macro-variables of the economy of Nepal, it is predominantly based upon secondary data. It uses the time series data since the year 2000/01 to 2019/20, they are the extended set of data for 20 years, published by MoF in Economic survey of various issues, data published in quarterly economic bulletin by NRB, publications of CBS and international agencies like the world bank. To identify the impact of remittance on growth, multiple regression model (OLS) is used.

#### 3.1. Empirical Model Specification

This study tries to examine the impact of remittance on economic growth of Nepal. As remittance is the main variable of interest of this study, it will be added to explore its effect on growth of Nepal. Besides it, other important control variables which contribute to economic growth are government expenditure (Govt. Exp.) as a proxy for investment, export (export as percentage of GDP), human capital (HC) measured by years of schooling or enrollment rate or literacy rate, among other. The new growth theory also known as endogenous growth theory puts large importance on the education variable on economic growth, propounded that investment in human capital, innovation and knowledge are significant contributors to economic growth. Human capital such as enrollment rate in the higher education or number of teachers employed in school level education might be the education variables. This study uses enrollment in higher level education for the study. Thus, the economic growth in functional form is written as:

$$\text{Eco. Growth} = f(\text{Rem}_t, \text{HC}_{t-1}, \text{Govt. Exp.}_t, \text{Exp.}_t) \dots\dots\dots (1)$$

Where,

Eco. Growth = Economic growth

Rem<sub>t</sub> = Remittance received at time period t

Govt. Exp.<sub>t</sub> = Government expenditure at time period t

Exp. t = Export as percentage of GDP

HC<sub>t-1</sub> = one period lagged human capital proxied by enrollment in higher education

The linear form of the regression (after taking Log on both sides) equation for growth is :

$$\text{LOG RGDP}_t = \beta_0 + \beta_1 \text{ LOG Remi.}_t + \beta_2 \text{ HC}_{t-1} + \beta_3 \text{ LOG G. Exp.}_t + \beta_4 \text{ LOG Exp.}_t + \vartheta_t \dots\dots\dots (2)$$

In equation (2), RGDP<sub>t</sub> is dependent variable; Remi<sub>t</sub>, Exp. t, G. Exp and HC<sub>t-1</sub> are explanatory variables. Similarly, β<sub>0</sub>, β<sub>1</sub>, β<sub>2</sub>, β<sub>3</sub> and β<sub>4</sub> are the parameters to be estimated and ϑ<sub>t</sub> is stochastic error term. The expected sign of parameters β<sub>1</sub>, β<sub>2</sub>, β<sub>3</sub> and β<sub>4</sub> are positive expecting that economic growth increases due to increase in remittance, export trade, government expenditure and human capital in the nation. The sign of intercept β<sub>0</sub> may be positive or negative.

Depending upon the above objective and research question, the hypothesis set by this study is

$$H0 : \beta_0 = \beta_1 = \beta_2 = \beta_3 = \beta_4 = 0$$

i.e. The inflow of remittance has no any contribution in economic growth of Nepal.

$$H1 : \beta_0 \neq \beta_1 \neq \beta_2 \neq \beta_3 \neq \beta_4 \neq 0$$

i.e. The inflow of remittance contributes significantly in economic growth of Nepal.

### 3.2. Empirical Results and Interpretation

The model shown in equation (2) with the values of empirical findings can be written as :

$$\text{LOG RGDP}_t = 9.6055 + 0.1317 \text{ Remi.}_t + (- 0.0024 ) \text{ HC}_{t-1} + 0.0998 \text{ Govt. Exp.}_t + 0.1755 \text{ Exp.}_t + \vartheta_t.$$

**Table 6**

*Estimation of Parameters*

Variable	Coefficient	Std. Error	t-Statistic	Prob.
LOG(REMITANCE)	0.131714	0.026620	4.947845	0.0002
LOG(HUMAN_CAPI-TAL)	-0.002473	0.031517	-0.078470	0.9385
LOG(GOVT_EXP)	0.099805	0.022793	4.378668	0.0005
LOG(EXPORT)	0.175555	0.094177	1.864097	0.0820
C	9.605510	0.838856	11.45072	0.0000

R-squared	0.985031	Mean dependent var	14.24958
Adjusted R-squared	0.981040	S.D. dependent var	0.252777
S.E. of regression	0.034806	Akaike info criterion	-3.665709
Sum squared resid	0.018172	Schwarz criterion	-3.416776
Log likelihood	41.65709	Hannan-Quinn criter.	-3.617115
F-statistic	246.7737	Durbin-Watson stat	1.283484
Prob(F-statistic)	0.000000		

The empirical results presented in Table 6 show that economic growth rate (RGDP) is positively related to inflow of remittance, government expenditure and export trade. However, the effect of human capital is not significant in short run because its effects could be realized in long run. The estimated coefficient of remittance is 0.1317. It shows that; when inflow of remittance increases by 1 unit then, GDP growth increases by 0.1317 unit, other things remaining the same. Similarly, the coefficient of government expenditure 0.0998 shows that when government expenditure increases by 1 unit, GDP growth rate increases by 0.0998 unit. Likewise, the coefficient of export trade 0.1755 justifies that GDP growth rate increases by 0.1755 unit due to 1 unit increase in export trade, other things remaining the same. This result is statistically significant at 5 percent level of significance. The result summary shows that there is more effects of remittance, government expenditure and export trade on GDP growth.

The value of  $R^2$  is 0.98. It justifies that 98 percent of the overall variation in the model is explained by selected variables of regression model. The value of Durbin- Watson statistics is 1.3, which is nearer to 2. It shows that overall result is tolerable. The empirical results presented in Table 7, Table 8, and Table 9 show that the model is free from multicollinearity, there is no serial correlation among the selected variables and no sever problem of heteroskadasticity as the values of VIF is less than 30, the value of Chi-Square in LM test is 0.23 (only 23 percent), and the value of Chi-Square in heteroskadasticity is only 0.28 (only 28 percent).

**Table 7**

*Multicollinearity Test*

Variable	Coefficient	Uncentered	Centered
	Variance	VIF	VIF
LOG(REMITANCE)	0.000709	1789.909	12.78303
LOG(HUMAN_CAPITAL)	0.000993	2614.726	3.578521
LOG(GOVT_EXP)	0.000520	1045.713	5.389444
LOG(EXPORT)	0.008869	18121.90	6.426598
C	0.703680	11616.77	NA

**Table 8***Breusch-Godfrey Serial Correlation LM Test*

F-statistic	1.101161	Prob. F(2,13)	0.3616	
Obs*R-squared	2.897350	Prob. Chi-Square(2)	0.2349	
Variable	Coefficient	Std. Error	t-Statistic	Prob.
LOG(REMITANCE)	0.001459	0.032928	0.044306	0.9653
LOG(HUMAN_CAPITAL)	0.019975	0.036563	0.546315	0.5941
LOG(GOVT_EXP)	-0.002883	0.022754	-0.126697	0.9011
LOG(EXPORT)	-0.039352	0.122745	-0.320599	0.7536
C	0.199156	1.127559	0.176626	0.8625
RESID(-1)	0.412320	0.321724	1.281595	0.2224
RESID(-2)	-0.284250	0.383568	-0.741067	0.4718
R-squared	0.144867	Mean dependent var	-1.16E-15	
Adjusted R-squared	-0.249809	S.D. dependent var	0.030926	
S.E. of regression	0.034574	Akaike info criterion	-3.622208	
Sum squared resid	0.015540	Schwarz criterion	-3.273702	
Log likelihood	43.22208	Hannan-Quinn criter.	-3.554176	
F-statistic	0.367054	Durbin-Watson stat	1.858960	
Prob(F-statistic)	0.887049			

**Table 9***Heteroskedasticity Test: Breusch-Pagan-Godfrey*

F-statistic	1.255683	Prob. F(4,15)	0.3303	
Obs*R-squared	5.017029	Prob. Chi-Square(4)	0.2856	
Scaled explained SS	3.049692	Prob. Chi-Square(4)	0.5495	
Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-0.024540	0.032175	-0.762687	0.4575
LOG(REMITANCE)	-0.000508	0.001021	-0.497141	0.6263
LOG(HUMAN_CAPI-TAL)	-0.002193	0.001209	-1.814093	0.0897
LOG(GOVT_EXP)	0.000627	0.000874	0.717126	0.4843
LOG(EXPORT)	0.004717	0.003612	1.305954	0.2112
R-squared	0.250851	Mean dependent var	0.000909	
Adjusted R-squared	0.051079	S.D. dependent var	0.001370	
S.E. of regression	0.001335	Akaike info criterion	-10.18740	

Sum squared resid	2.67E-05	Schwarz criterion	-9.938466
Log likelihood	106.8740	Hannan-Quinn criter.	-10.13881
F-statistic	1.255683	Durbin-Watson stat	2.102637
Prob(F-statistic)	0.330264		

## 5. CONCLUSION AND RECOMMENDATION

This study was designed and initiated in order to explore the empirical analysis of the effects of remittance on economic growth of Nepal by using an econometric tool – Multiple Regression Analysis, using the extended set of time series data covering the period of 2000/01 to 2019/20 i.e. 20 years. The empirical results show that remittance is positively and significantly related with economic growth. The impacts of other control variables government expenditure and export trade are also positive for growth. However, expenses made on human capital has lagged effect i.e. not significant in short-run but, significant only in long-run. It is real fact that the investment made in higher education at present will affect growth only in long-run.

Thus, this study concludes that remittance is relatively more stable and predictable source of financial inflow than other sources. It reduces the short term unemployment problem in the economy and contributes significantly for economic growth. Recently, the inflow of remittance in Nepal is around 25 percent as of GDP in recent years. So, Nepalese economy is going to be remittance based economy. It is one of major source of foreign exchange earnings, capital formation and investment in the nation and, thereby, economic growth in the economy.

The finding of this study has some important policy implications. They are given below.

- The government of Nepal and concerned agencies should provide skill development trainings to Nepalese migrant workers in order to get better income in host countries. It helps to earn more, to remit more in the nation and family.
- The government should play proactive role to promote the foreign employment and to explore and identify new destinations in the emerging nations other than Malaysia and Gulf nations.
- Encouraging the migrant workers to send remittance only from formal banking channels which helps to overcome the liquidity crisis in banking sector and foreign exchange shortage as Nepal is recently suffering from it.
- Attractive schemes and interest rates on deposit should be provided for migrant workers. It helps for savings and investment in the economy.
- Government should use the remittance for the fast development of major infrastructures by offering the attractive schemes to the foreign remitters.
- Unnecessary and unproductive use of remittance income should be discouraged with the attractive and high yielding saving schemes. Efforts should be directed by the concerned authorities towards productive use of remittances rather than using more remittance on the purchase of land, houses, jewelry, etc.

- Efforts should be made by Nepal government to explore and expand the job opportunities in the nation in long run. Nepal should not be always depending upon foreign employment. It is only short term solution but not permanent solution.

Remittance generates a number of macro impacts in receiving countries and micro impacts on receiving households. Such impacts are seen in gross domestic product (GDP), foreign exchange reserve, export and import, consumption and investments, financial savings and so on. Moreover, remittance helps the recipient members and households to increase their consumption pattern of both domestic and imported goods, helps to increase the tax revenue of the government. The effects of remittances are stronger in less developed and developing countries like Nepal. If there is excess inflow of remittance or capital outflow, it may lead to increase in money supply, increase in price level or inflation rate in the economy, and thereby reduces the value of money. It is the better source of income for recipients and for governments for poverty alleviation and even for infrastructure development. It does not mean that there are only positive aspects of remittance. Developing countries like Nepal may be highly depending upon remittance, discourages the labour force participation rate, fall in domestic labour supply and, thus, adverse effects on economic growth (United Nations, 2013). Thus, the government of recipient country should make appropriate and productive policy to use remittance to achieve higher growth in the nation.

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