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The effect of remittances on the Nigerian economy

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Abstract

This study analyzed the effect of remittances on the Nigerian economy. The study employed secondary data covering the period 1980-2008. Data sources included official publications of the World Bank, Central Bank of Nigeria, National Bureau of Statistics, Journals and other relevant publications. Data collected were analyzed using trend and regression analysis. Results of data analysis revealed that remittance inflow has been on the increase over the past two decades. Also, remittances, per capita income, investment and time were the positive and significant factors influencing output while consumer price index significantly influenced output negatively. It was recommended that remittance receiving countries should provide a friendly economic environment through sound macro-economic policies, including stable exchange rates, basic physical infrastructure, improved market integration, reliable financial and other institutions, transparent legal system and good governance – in essence, conditions that can prime the economy for development and equip it adequately to benefit from this external stimulus.

Keywords: Remittances, Nigeria, Economy

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1. Introduction

International remittances has been recognized as an important driver of the economy of most developing countries. It plays vital roles in poverty reduction, income redistribution and economic development, especially in rural areas. According to Hernandez-Coss and Bun (2006), Nigeria is the largest recipient of remittances in Sub-Saharan Africa. They reported that the country receives nearly 65 percent of officially recorded remittance flows to the region and 2 percent of global flows. The Central Bank of Nigeria (CBN) reported approximately US$2.26 billion in remittances for 2004. The phenomenon of Nigerian emigrants, considered as an escape from hardship on the home front and a depletion of human capital is somehow paying off for the country. This is in view of the revelation that Nigerians abroad grew the economy by a whopping $7billion in the year 2008 and that Nigeria is the sixth highest destination of remittances from its citizens living in the Diaspora (World Bank, 2008; The Nation, 2009).

"Remittances reflect the local labour working in the global economy and have been shown to explain partly the connection between growth and integration with the world economy" (Addison, 2004, p. 5). Remittances enhance the integration of countries into the global economy and reflect the local labour working in the globalized economy.

Remittance has become an important source of revenue both for government through tax and fees and for households. At households' levels, it helps increase income and consumption smoothing (Kannan and Hari, 2002; International Monetary Fund (2005), and Jongwanich, 2007); increase saving and asset accumulation (Hadi, 1999); and improve access to health services and better nutrition (Yang, 2003) and to better education (Edward and Ureta, 2001). Likewise, at village/community level, remittance income can help stimulate local commodity markets and local employment opportunities. Remittances have proved to be less volatile, less procyclical, and therefore a more reliable source of income (for agricultural production and other household uses) than other capital flows to developing countries, such as foreign direct investment (FDI) and development aid (Gammeltoft, 2002; Keely and Tran, 1989; Puri and Ritzema, 1999; Ratha, 2003).

International financial flows of remittances, official development assistance and foreign direct investment for the year 2007 is shown in Table 1 below.

According to Hernandez-Coss and Bun (2006), Nigeria is the largest recipient of remittances in Sub-Saharan Africa. It received approximately US$2.26 billion in remittances for 2004. The phenomenon of Nigerian emigrants, considered as an escape from hardship on the home front and a depletion of human capital is somehow paying off for the country. The World Bank, (2008) and the Nation (2009) noted that recorded remittances from about 20 million Nigerians in the diasporas exceeded $7 billion in 2008 and that Africa accounts for up to $46 billion of the globally recorded remittances. As is the case for other countries in the Region, the figure might not be reflective of the actual contributions of these Nigerians since it could be higher due to underreporting and the prevalence of informal transfer mechanisms which account for 50 percent of total flows to the country.

Table 1. International financial flows: remittances, official development assistance and foreign direct investment (2007)

Country	Remittance inflows (US$ millions)	Remittance inflows per capita (US$)	Remittance inflows as a % of ODA	Remittance inflows as a % of GDP	Ratio of remittance inflows to FDI
Nigeria	9,221	62	451.5	6.7	1.5
Ghana	117	5	10.2	0.8	0.1
Burkina Faso	50	3	5.4	0.7	0.1
Mali	212	17	20.8	3.3	0.6
Côte d'Ivoire	179	9	108.7	0.9	0.4
Cameroon	167	9	8.7	0.8	0.4
Gambia	47	28	65.4	6.9	0.7
Morocco	6,730	216	617.8	9	2.4

However, Nigeria faces immense challenges in accelerating growth, reducing poverty and meeting the Millennium Development Goals (MDGs). It has become necessary and indeed imperative to examine the flows of remittances to Nigeria as well as the potential impact of these remittances on the performance of the economy.

2. Methodology

The study area is Nigeria. Nigeria is one of the largest countries in Africa, with a total geographical area of 923 768 square kilometers and a population of about 150 million (NPC, 2006). It lies wholly within the tropics along the Gulf of Guinea on the western coast of Africa. "Nigeria is bordered by Benin to the west, Niger to the north, Cameroon to the east and the Atlantic Ocean. The terrain varies from coastal swamps and tropical forest in the south, to savannah and semi-desert in the north. The highest points are the Jos Plateau in the centre (1,200-2,000 metres above sea level) and the mountains along the eastern border. The river Niger, the third longest river in Africa, reaches the sea through an extensive Delta of mangrove swamps" (Nigeria Country Report, 2012, p. 3).

The study employed secondary data covering the period 1980-2008. Data sources include official publications of the World Bank, Central Bank of Nigeria, National Bureau of Statistics, Journals and other relevant publications. Data collected were analyzed using trend and regression analysis. The empirical model of the regression analysis followed the works of Giuliano and Ruiz-Arranz (2005) and Ahortor and Adenutsi (2009) and is given by:

$$GDP = f(REM, PCY, HCA, INV, CPI, GXP, EOP, TRN)$$

Where is GDP is the real GDP per capita, REM is a measure of remittances per capita, PCY is lagged real per capita income, HCA is human capital investment proxied by secondary school enrolment, INV is investment proxied by gross fixed capital formation as a percentage of real GDP, CPI is natural growth in Consumer Price Index used as proxy for inflation , GXP is government spending, EOP is economic openness (EOP) which is proxied by the ratio of total exports and imports to GDP and TRN is lagged trend.

3. Results and discussion

3.1. Inflow of remittances

The result of the trend analysis showing the flow of international remittances to Nigeria from 1980 – 2009 is shown in Figure 1. The figure shows that remittance inflow to the country increased rapidly from early 2000 to 2009. This supports the revelation that Nigerians abroad grew the economy by a whopping $7billion in the year 2008 and that Nigeria is the sixth highest destination of remittances from its citizens living in the Diaspora (World Bank, 2008; The Nation, 2009).

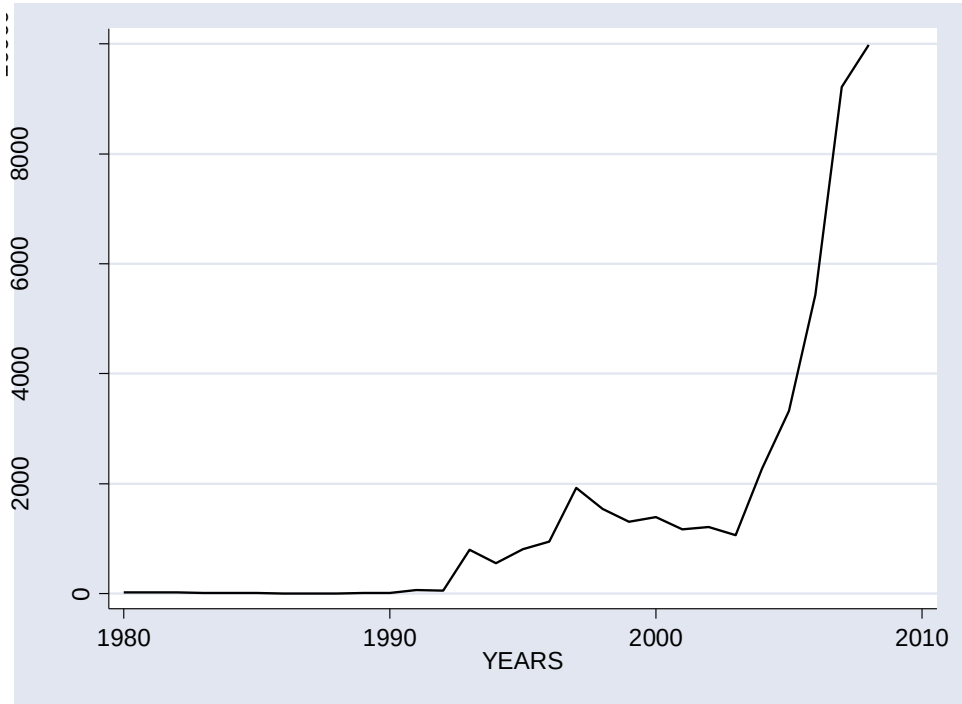

Figure 1. The Flow of Remittance to Nigeria (1980-2008) (Million USD)

For the country therefore, remittances form a crucial source of foreign exchange capable of sustaining her balance of payments. In addition, governments of sending countries have put renewed hopes on migrants as

potential investors in the national economy. The surge in remittances has given rise to a kind of euphoria, with migrant remittances being proclaimed as the newest "development mantra" among institutions like the World Bank, governments, and development NGOs (Kapur, 2003; Ratha, 2003).

3.2. Factors affecting output of the economy

The regression result showing the factors affecting output of the economy measured by the real gross domestic product per capita is presented in Table 2. The linear functional form was chosen as the lead equation as it was the best fit model. The coefficient of multiple determination was 0.9686 which implies that 96.86 percent of the variations in output of the economy was explained by the variables included in the model. The F ratio was (77.24) was significant at I percent and this attests to significance of the regression result or otherwise, that the data fit the model.

Table 2. Factors affecting output of the economy

Variable	Linear	Exponential	Double log	Semi log
Constant	828.292	6.678	7.456	1778.905
	(11.080***	(106.73)***	(6.61)***	-1.02
REM	0.059	2.10E-05	0.152	222.564
	(3.22)***	(1.57)*	(2.14)**	(2.03)**
PCY	0.055	-3.47E-04	-0.07	-39.581
	(4.54)***	(-1.48)	(-0.54)	(-0.20)
HCA	0.1	4.65E-06	0.088	137.018
	-0.69	-0.38	(1.71)*	(1.71)*
INV	0.273	-1.42E-03	0.069	-102.687
	(2.67)**	(*1.04)	(-1.17)	(-1.12)
CPI	-0.447	4.09E-04	-0.018	-55.869
	(-1.60)*	(4.02)***	(-0.17)	(-0.34)
GXP	-0.001	-4.15E-07	-0.133	-187.927
	(-2.18)	(-1.74)*	(-1.20)	(-1.09)
EOP	0.614	6.94E-04	-0.01	-47.487
	-1.44	(1.93)*	(-0.10)	(-0.30)
TRN	7.151	0.011	0.171	223.401
	(1.74)*	-0.95	-1.21	-1.02
R^2	0.9686	0.9599	0.7835	0.7137
Adj.R^2	0.9561	0.9439	0.6969	0.5991
F ratio	77.24***	59.91**	9.05***	6.23***

Remittance was significant at 1 percent and positively related to the economy's output. This implies that the national output increases with increase in the inflow of remittances to the country. This result lay credence to the "view upheld by contemporary development economists that international remittance inflows are one of the major macroeconomic factors that significantly promote long-run economic growth in small-open developing economies" (Ahortor and Adenutsi, 2009, p. 3282).

The table also revealed a positive and significant relationship between lagged per capita income and investment proxied by gross fixed capital formation at 1 percent level of significance. These imply that there would be a 5.5 percent and 27.3 percent increase in output for a unit increase in per capita income and investment respectively.

The positive impact of remittances on per capita income growth in the sampled countries over the study period could be explained by the fact that remittances may be used by recipients for consumption and/or investment. All other things remaining equal, whichever use remittances are put, they are capable of inducing an increase in aggregate demand, leading to a rise in national output and a subsequent increase in real income growth (Ahortor and Adenutsi, 2009, p. 3282).

Consumer price index is negatively and significantly related to output at 10 percent significance level. This result implies that there would be a 44.7 percent decrease in output for a unit increase in the rate of inflation. This conforms to *a priori* expectation as increase in the price productive inputs is a disincentive to investment which leads to reduction in output. Time trend is significant at 10 percent level and positively related to output. This implies that output of the economy increases as the years goes by.

4. Conclusion

This study provides empirical evidence that international remittance inflows are one of the major macroeconomic factors that significantly promote economic growth in a developing economy like Nigeria. Therefore, remittance receiving countries need to provide a friendly economic environment through sound macro-economic policies, including stable exchange rates, basic physical infrastructure, improved market integration, reliable financial and other institutions, transparent legal system and good governance – in essence, conditions that can prime the economy for development and equip it adequately to benefit from this external stimuli. This is particularly important if remittances are to be attracted and used as development capital. The corporate sector, especially banks and other financial institutions, can do a lot to increase the volume and value of official flows by reducing the transaction cost, simplifying transfer procedures and by encouraging through various other means the use of formal financial channels.

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