

Role of Foreign Remittances in Poverty Reduction: A Case of Poverty-Ridden Kyrgyzstan

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Abstract

Remittances have always been an important source of external finance for the low-income and middle-income developing countries. In Kyrgyzstan, remittances have provided a phenomenal support to the economy. The remittances from Russia to Kyrgyzstan accounted to 29 % of their GDP in 2020. There is a strong need to investigate the impact of foreign remittances upon poverty reduction for Kyrgyzstan, which is the second leading recipient country of the foreign remittances in the Central Asian region. This study has empirically investigated the impact of remittances on poverty in Kyrgyzstan by taking the variables like remittances, poverty size, capital formation, per capita GDP, savings, and unemployment for the period of 2008-2019. Ordinary least square regression was applied, and the results show an insignificant relationship between foreign remittances and poverty reduction. The reason is that remittances in Kyrgyzstan are not pro-poor as mostly the workers from the rich families have migrated to Russia.

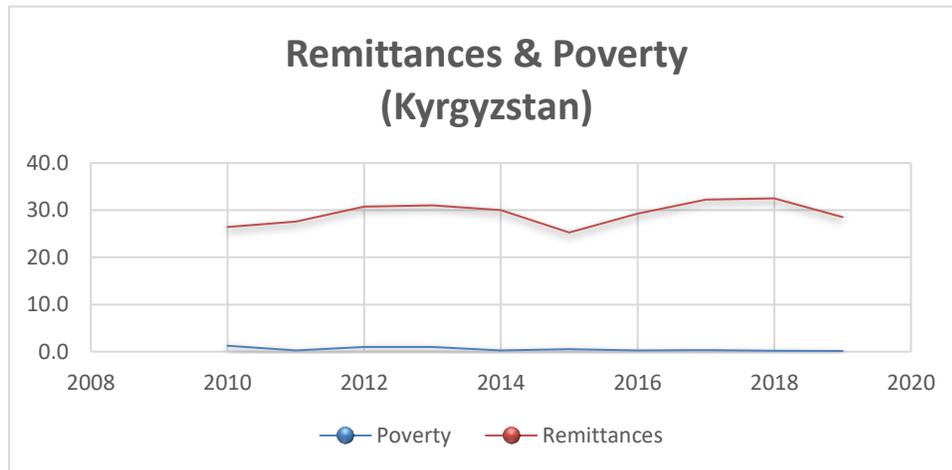
Key Words: foreign remittances, poverty reduction, Kyrgyzstan, Russia, central Asia.

1. Introduction

A sharp rise in the number of remittances experienced over the recent years has grabbed the attention of many sociologists and the economists. According to the estimates of the United Nations, at the beginning of the 21st century, it was estimated that approximately 3% of the world's population is living as immigrant workers. The rapidly developing world has seen immense technological evolution and such advancements have continued to broaden the gap between the developed and the developing countries, thus further exacerbating the poverty. Consequently, the people from developing countries immigrate to developed countries by leaving behind their families and to earn better livelihood for themselves as well as for their families. The purely selfless intention of providing for their families and immigrating to the developed countries has led to an increase in the remittances being flowing out of developed countries into the developing countries.

The increased demand for labor, minimum wage laws, and labor protection laws in developed economies they all act as incentives for the people who fail to find adequate opportunities at their home countries. The money earned by the immigrants is sent back to

home in the form of remittances with the purpose to finance the consumption expenditures of the family members in their home countries. Moreover, the importance of remittances can be evaluated by the fact that according to the World Bank, more than 30% of the total GDP is contributed by remittances for countries such as Tonga, Somalia, and Lebanon (2020). Furthermore, 9.6% of the Philippines' GDP and 9.9% of Pakistan's GDP is contributed by remittances being sent to these countries by their overseas residents. However, these key statistics have failed to record the portion of remittances that are sent through illegal means. The reason being the citizens who migrate illegally do not have the means to afford the legal process of migration but are provoked when they see their peers succeed and elevate their financial status by working abroad and supporting their families back home (Gerber & Zavisca, 2020). The practice may seem feasible once they succeed in crossing the borders but not all of them are able to obtain work permits upon migration. The remittances received by the recipient economies can greatly contribute towards rapid economic development as most of the households tend to invest some proportion of their remittance income in startups or small-scale businesses. Although the primary use of income is to spend on necessities, not much is left to make such investments in businesses under normal circumstances. However, an increase in the disposable income of such individuals prompted by a rise in remittances eases the liquidity restraints for them and allows them to take entrepreneurial risks without putting themselves into jeopardy (Amare & Hohfeld, 2016). Apart from fulfilling their necessities of life, the families of migrants spend remittances on several other things including consumer goods, educational attainment, and small businesses, etc. This results in a rise in demand for goods and services due to which remittances tend to have an increasing impact on the overall aggregate demand in the economy which ultimately leads to increase in output and production, hence to a greater GDP (Ryazantsev, 2016). The boost that occurs in expenditure on health, education, and other investment schemes by the migrant families significantly contribute to breaking the shackles of poverty.



In the case of Central Asia, economists like Murodova (2018) holds an affirmative view that a strong positive relationship exists between the remittances and poverty reduction. A vast number of studies exist confirming the poverty alleviation effect of remittance specifically on Central Asian countries like Tajikistan, Uzbekistan, Kyrgyzstan (Batsaikhan & Dabrowski, 2017; Ulrika, 2020). Moreover, Azam, Haseeb, et al. (2016) also conducted a study on 12 countries of Europe and Central Asia and found a positive relationship between remittances and economic growth which ultimately led to poverty reduction. The republic of Kyrgyzstan contributes the second-largest share of remittances next to Tajikistan in Central Asia. According to the estimates of the World Bank (2019), remittances received by families residing in Kyrgyzstan amounted to 2.7 billion US dollars in 2018. In addition, the Republic of Kyrgyzstan also indulges in making the attempts to promote labor migration to developed countries like the Russian Federation. For instance, the government of the Kyrgyz Republic has laid the foundations of the State Committee for Migration and Employment (SCME) in different regions of Russia with the intention to facilitate the migration process for the Kyrgyz migrants (Sagynbekova, 2016).

The existing literature reveals that the empirical investigation between the foreign remittances and poverty reduction has not gained much attention till date. Therefore, it is important to investigate the empirical effects of the foreign remittances upon poverty reduction for Kyrgyzstan which is the second leading country in contributing the foreign remittances in the region. This study has investigated the relationship based on the annual data for all variables available on World Bank development indicators. This study has contributed in various ways. Firstly, this study is the latest study that investigates the relationship for the period of 2008-2019. Secondly, this study adds into existing knowledge regarding the relationship between foreign remittances in poverty reduction. Finally, this study provides practical implications for academicians, investment managers, poverty related organizations and practitioners. The study reports an insignificant relationship between foreign remittances and poverty reduction in Kyrgyzstan. The study has highlighted various implications for both academic and practitioners at the conclusion section.

The reminder of the paper is based on following sections. Section 2 talks about the existing literature review, Section 3 refers data and methodology. Section 4 explains results and discussion. Finally, section 5 explains conclusion, future directions and implications for quarter concerned.

2. Literature Review

A vast number of studies have investigated the impact of remittances upon poverty reduction and have confirmed the underlying relationship. For instance, Azam, Shahbaz, et al. (2016) termed remittances as an ‘anti-poverty device’ as they confirm the strong positive impact of remittances on poverty alleviation in their study of 39 countries taken from all categories of the income distribution. The results were robust for all categories which further indicates the significance of the positive relationship between remittance

influx and poverty reduction. Imai et al. (2016) enriched the literature further by contributing their input based on the findings of cross-country panel data confirming the hypothesis that remittances stimulate economic growth and poverty reduction in the home country. Similarly, a strong positive relationship was observed between remittances and poverty alleviation in case of Sri Lanka (Karunaratne & Dassanayake, 2018). Le and Nguyen (2019) also asserted that not only international migration but migration within the country from one region to another can also have impact upon poverty alleviation.

However, many economists argue that while remittances prove to have a decreasing impact upon the severity of poverty, it can have much larger repercussion for the economy as well. Several studies confirm the ability of remittances to bring about a significant reduction in the poverty incidence of an economy, albeit giving rise to several adverse effects as well. As discussed above, remittances inculcate an income effect into the minds of the receivers whereby they experience an increase in their disposable income, and hence their consumption level rises. However, a major drawback that the income effect entails is the decrease in the labor force participation of the country (Abduvaliev & Bustillo, 2020). The rationale behind this phenomenon is that people no longer feel the need to work as all their consumption is financed through the remittances. Another moral hazard posed by the inflow of remittances is the deterioration of the government's fiscal policy as the households no longer persuade the public sector to introduce revamping policies aimed at economic growth and development (Combes et al., 2015). Easton and Montinola (2017) also emphasized that remittances empower governments to reduce their expenditures on the public as their financial needs are fulfilled through remittances. Such dependency on part of households and the public sector can have adverse effects on the overall financial health of the families as well as upon the future of the entire economy.

Imai et al. (2016) explained the direct effect of remittances is reflected in the increased disposable income for migrant families allowing them to finance their consumption as their budget constraints are relaxed to a certain extent (Arif et al., 2019). While the remittances directly help the migrant families to escape poverty through an increase in income, economists claim that poverty alleviation can be achieved indirectly as well. The inflow of remittances paves the way for economic growth in the home country as it leads to increased output growth and productivity (Taylor & Castelhana, 2016). Thus, improvement in economic conditions has positive implications for the financial health of poor citizens of the respective country. Another school of thought argues that remittances only allow home economies to get rid of transitory poverty while the evil of chronic poverty continues to wreak havoc on the individuals for the years to come (Prokhorova, 2017b; Wagle & Devkota, 2018). Researchers argue that the increase in consumption induced by remittances is temporary in nature; remittances cannot help in fighting the intergenerational poverty that has existed in families for centuries. Moniruzzaman (2020) stresses that the only way to break the vicious cycle of chronic or structural poverty is to invest some proportion of the remittance income on land purchases or children's education.

On the other hand, Talba et al. (2017) argue that the rise in consumption is merely an illusion, remittances only instill a temporary sense of comfort in the minds of the migrants' families. This is primarily because the remittances received by families are used to fuel the present consumption and, in most cases, almost all the funds are spent immediately with nothing left to save or invest in profitable ventures. If instead, the households were to save a proportion of the remittances, they can be considered as key contributors of foreign currency reserves for both the households and the government which can greatly aid the economy's development (Shah & Majid, 2018). However, such practices are hardly ever executed by the households which is why the benefits obtained from remittances are short-lived and do not prove to be beneficial in the long run. There is no concept of contingency planning in Central Asia both at the household and the state level due to which a vicious cycle of dependency on remittance income continues until the migrants eventually return home.

Although the increase in income induced by remittances can lead to greater educational attainment on part of these migrants' children, many economists argue that such investments may not always be fruitful. The intuition behind this failure in investment is the rising demand for international labor in the developed countries who try to attract laborers from developing countries to make up for the lack of skillset that exists in the local laborers of that respective country. As a result, many educated people emigrate to these countries due to which the investment made on their education goes to waste as the returns can no longer be enjoyed by the home country (Adeyemi et al., 2018). One of the major attempts made by developed countries to facilitate migration includes the implementation of 'Resettlement Program Compatriots in Russia' by the Russian government with the intention of alluring the required labor from Central Asia. Abduvaliev & Bustillo (2020) claimed that this policy contributed a great deal in captivating many skilled labor migrants from countries like Tajikistan, Kyrgyzstan, and Uzbekistan. This helps explain why the Central Asian economies rank among the top remittance-dependent countries around the world. Human capital plays a vital role in the economic growth of any country (Nawaz & Ganic, 2021). Lipková et al. (2020) found that the main countries of Central Asia have a dependency of about 30% on the funds received by the migrants living abroad.

Moreover, some studies suggest that the true impact of remittances is more vulnerable to the economic conditions that prevail in the host country rather than the conditions of the home country (Azizi, 2021; Imran et al., 2020; Liu et al., 2020). Vargas-Silva and Huang (2018) demonstrated their findings based on two hypothetical datasets to study the impact of economic conditions in both home and host country. The results indicate that remittances are more receptive to the changing economic health of the donor country than the recipient country. The intuition behind this theory is the fact that the source of income for these migrants and their families are now the employers of the host country. Therefore, the economic conditions of the host countries are directly reflected in the wages earned by both the local and the foreign workers in that country. The fact that developed economies face

the same obstacles and challenges as do the developing nations. People move to richer countries in hope of earning a better lifestyle but what they fail to realize is that there is an equally likely chance of those economies deteriorating in which case they might be at the risk of either losing out on the earnings they make in those countries or completely losing their jobs (Mehedintu et al., 2019).

Owing to the rising trend in migration among Central Asians, the eventual increases in remittances received are inevitable. Over the past decade, migration has become so common that people from the Kyrgyz Republic also emigrated to countries like Russia, Kazakhstan, Turkey, and many others. The universal factors driving people out of their countries to more developed ones include skyrocketing unemployment rates, low earning potential of the jobs available, if any, poverty-ridden economy, and many others. However, the critical factors specific to Kyrgyzstan that majorly contributed to the rising trend of migration are poor economic conditions and the ethnopolitical tension that stem from ethnic conflicts and political instability of the state (Nurdinova et al., 2019). This helps explain the prevalence of migration and the upsurge of remittances in the Kyrgyz Republic over the past two decades. The republic of Kyrgyzstan contributes the second-largest share of remittances next to Tajikistan in all Central Asia. According to the estimates of the World Bank (2019), remittances received by families residing in Kyrgyzstan amounted to 2.7 billion US dollars in 2018.

Lim and Morshed (2015) asserted that this rapid increase in remittances is not due to the increase in the funds sending by the existing migrants but because of increase in labor migration from Kyrgyzstan. The theory implies that when a developing economy experiences negative income shocks, it does not result in increased remittances. Rather, it gives rise to more people emigrating out of the country in the hope of accessing better earning opportunities. This helps us to explain the rise in remittances induced by the deteriorating economic health of the home country. Moreover, this phenomenon also debunks the theory that the altruistic nature of migrants compels them to leave their country and to provide their families with a better living standard (Kumar et al., 2018). However, the assumption that remittances flowing into the country can be saved and contribute to foreign currency reserves does not hold for economies such as Kyrgyzstan. Kyrgyzstan being one of the poorest countries of Central Asia uses up almost all its foreign remittances to fulfill its consumption needs. Owing to this, a very small proportion of the population can save remittances or to spend them on luxuries. There is very little diversity in the places from which Kyrgyzstan receives its remittances. Kazakhstan and Russia are the two main contributors where the remittances flow in from hence leaving it prone to the risk of fluctuations in its remittances depending on any kind of instability in both host countries (Hagedorn et al., 2017).

Sagynbekova (2017) shared further that those Kyrgyz nationals residing in Russia are mostly employed in the real estate, transport, and utility sector while the other sectors like industrial and agricultural remain reserved for migrants coming from other parts of the world. In addition, among migrants from of Central Asia, the citizens of Kyrgyzstan are

treated with most respect in Russia. The preference of Kyrgyz over nationals of other states can be attributed to the numerous agreements that are in action between the governments of both countries, for instance, the Facilitated procedure of citizenship acquisition whereby obtaining citizenship in Russia is further simplified for Kyrgyz national as compared to others like Uzbeks and Tajiks, etc. (Ryazantsev, 2016). Such agreements in place along with other education and training facilities provided by the government hints at the attempts made to encourage migration from the Kyrgyz Republic to countries like Russia. These efforts are primarily intended to support the continuous inflow of remittances without any hassle to ensure that the objective of poverty alleviation through remittances is realized up to its full potential. The existing literature explained above determines that there is a dire need for examining the empirical relationship between the foreign remittances and poverty reduction, due to the rare attention given so far.

3. Data & Methodology

To investigate the relationship between foreign remittances and poverty reduction in case of Kyrgyzstan, set of variables have been considered in this study. Foreign remittance has been considered as dependent variable whereas poverty reduction has been considered as independent variable. Further, the poverty reduction is measured based on various proxies that include gross domestic product, capital formation, unemployment, and poverty size (Prokhorova, 2017a; Zotova & Cohen, 2016). The annual time series data has been taken for the time ranging from 2008 to 2019. The data has been extracted from the World Bank Development Indicators being available on the website of World Bank. The explanation of variables is provided below in Table 1.

Table1: Variables Description and Data Source

Variable	Variable Abbr.	Description	Data Source	Data Frequency
Remittances	REM	The foreign workers contribution into country economy by sending money to the country reserves.	World Bank Development Indicator	Annual
Poverty	PV	The poor life standards of people residing in any country. The standards include education, health, and social life.	World Bank Development Indicator	Annual
Capital Formation	CF	The contribution into country economies based on the capital goods, assets, transportation tools etc.	World Bank Development Indicator	Annual
Gross Domestic Product	LNGDP	The overall wealth generated by the country based on the contributions of goods and services related activities.	World Bank Development Indicator	Annual
Unemployment	UNEMP	All active seekers for jobs but are unable to find out any opportunity. However, they are still a part of the labor force of that country.	World Bank Development Indicator	Annual
Savings		Savings of the country after expenditures and consumptions.	World Bank Development Indicator	Annual

Starting with preliminary empirical analysis, we applied various data filters for measuring the data reliability and for assessing the normality in dataset (Gujarati et al., 2012; Kennedy, 2008). The basic preliminary analysis results include the Pearson correlation test

for multicollinearity, unit root test for stationarity, Bruesch-Pagan/Cook-Weisberg for heteroscedasticity and the Wooldridge test for autocorrelation (Gujarati et al., 2012; Kennedy, 2008). The un-tabulated results for unit root test for stationarity, Bruesch-Pagan/Cook-Weisberg for heteroscedasticity and the Wooldridge test for autocorrelation indicates that the basic linear assumption of linear regression is fulfilled. As a baselines regression for examining the relationship, this study has adopted the growth poverty model in the light of Nahar and Arshad (2017). The regression equation for the model is as below.

$$\text{Log RMT}_t = a_0 - a_1 \text{Log PV}_t - a_2 \text{Log GDP}_t + a_3 \text{CF}_t + a_4 \text{Unemp}_t + \varepsilon_t \quad (1)$$

The components of equation have already explained in detail in Table 1.

4. Results and Discussion

The study starts basic analysis with descriptive statistics of our dependent and independent variables. The Table 2 reports the values for the descriptive statistics.

Table 2: Descriptive Statistics

Variable	Mean	Std. Dev.	Min	Max
Remittances	.52	.421	.1	1.3
Poverty	29.366	2.426	25.272	32.506
Capital formation	32.895	3.643	25.473	36.757
Ln GDP	6.909	.082	6.78	7.018
Unemployment	7.715	.769	6.72	8.64
Savings	-5.562	7.075	-15.906	1.142

Note: Std. Dev. Represents the standard deviation values, Min reflects minimum values and Max reflects maximum values.

The descriptive statistics in Table 2 is based on the mean, median, standard deviation, minimum and maximum values. The values report there is no issue of data normality, and the data set appears to be normal. After running the descriptive statistics, we ran Pearson pairwise correlation for assessing the issue of multicollinearity among the variables.

Table 3: Pairwise Correlations

Variables	(1)	(2)	(3)	(4)	(5)	(6)
Remittances	1.000					
Poverty	-0.199	1.000				
Capital formation	-0.268	0.492	1.000			
Ln GDP	-0.767	0.367	0.545	1.000		
Unemployment	0.714	-0.340	-0.455	-0.950	1.000	
Savings	-0.490	-0.065	-0.377	0.451	-0.613	1.000

The results in Table 3, reports no issue of multicollinearity among the variables. Furthermore, to reconfirm the results reproduced in Table 2, we ran the variance inflation factor test in addition to Pearson Correlation test. The un-tabulated results confirm that there is no issue of multicollinearity among the variables. Moving forward to our baseline’s regression model of growth poverty model. We started from Ordinary least square (OLS) regression technique. The results of OLS have been reproduced below in Table 4.

Table 4: Ordinary Least Square Regression

Remittances	Coef.	St.Err.	t-value	p-value	[95% Conf	Interval]
Poverty	.294	4.3	0.07	.949	-11.644	12.232
Capital Formation	.323	.949	0.34	.751	-2.312	2.959
LNGDP	1.462	61.417	0.02	.982	-169.058	171.982
Unemployment	-.177	9.419	-0.02	.986	-26.33	25.975
Savings	.029	.62	0.05	.964	-1.691	1.75
Constant	10.01	499.79	0.02	.985	-1377.628	1397.649
Mean Dependent Var	29.366		SD Dependent Var		2.426	
R-squared	0.260		Prob > F		0.902	
F-test	0.281		Bayesian Crit. (BIC)		55.855	
Akaike crit. (AIC)	54.039					

The results in Table 4 based on OLS technique indicates that the relationship between the remittances and the poverty reduction is insignificant. Even in greater depth, we found there is no significant relationship between foreign remittances and poverty, capital formation, LNGDP, Unemployment, and Savings in context of Kyrgyzstan. The results are in line with prior literature. Akmolodov and Budaichieva (2012) identified that most of foreign remittances in Kyrgyzstan are mainly used for consumption purposes not for the investment. It was also identified that most of these foreign remittances are spent on importing foreign goods, which resulted in trade deficit and the reduction in poverty did not take place. Furthermore, the level of dollarization in comparison to Kyrgyzstan currency is also one of the main reasons for having an insignificant impact on poverty reduction by the foreign remittances. Similarly, Atamanov and Van den Berg (2012) also identified that the foreign remittances have not any significant contributions in terms of farm land families in Kyrgyzstan.

5. Conclusion

The labor migration is an important aspect of Kyrgyzstan's economy and most of Kyrgyz labors migrate to Russia because of common language and the geographical proximity. About 20% of Kyrgyz population is living on less than USD 1.2 as per the figures of 2019 by World Bank. As a result of the pandemic, Kyrgyzstan's poor population is projected to increase by another 10%, resulting in about 1.9 million poor people in the country. (World Bank, 2020). This study has empirically investigated the impact of remittances upon the poverty of Kyrgyzstan. The results of the study show that remittances have insignificant relationship with poverty in case of Kyrgyzstan. The reason is that remittances in Kyrgyzstan are not pro-poor as mostly the workers from the rich families have migrated to Russia. In recent years a new trend has also emerged that migrants are migrating along with their entire families to Russia, thus choosing to settle there forever. According to data on Central Asian migrants, 40 percent of migrants live in Russia for two years and 25 to 30 percent stay longer. In addition, 33 percent of male migrants and 50 percent of female migrants are accompanied by their spouses (Caspian Policy Center Brief, 2021). The results of this study are quite aligned with the findings of Kumo (2012), who had also found the insignificant relationship between remittances and poverty in case of Tajikistan. In general, the importance of remittances in reducing the poverty of any country cannot be denied. The immigration of labors to the advanced countries also helps the poor and the developing countries in building the technical and behavioral skills of their labors (Kireyev, 2006). Finally, the future studies can investigate the impact of COVID-19 upon remittances and poverty. Generally, it is believed that COVID-19 has resulted into massive unemployment of migrants (Aysan et al., 2020), thus leading to a fall in remittances and increase in the poverty level.

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