

Economic crisis impact on Remittances and Migration level in Albania

Adela Shera, PhD.

Faculty of Economy, University of Tirana, Albania

Ardita Shehaj, MSc.

Inspector, Abuse of dominant position Directory, Competition Authority, Albania

Abstract

Remittances of international migrants as the second largest flow of incomes contribute to the well-being of their households of origin and also have an impact at macro-economic level. Out-migration is an effective means for low-income households to quickly overcome shortages of income. The sustenance of poor households might have been more difficult without such remittances. From a macro perspective, remittances contribute to the equalization of the income distribution among households having out-migrants. Remittances have enforced the Albanian economy since 1992 especially they had a positive and large contribution in consumption level, investment and GDP. But the economic crisis of 2008 has affected large sectors of the population in developed and developing nations and international immigrants have not been the exception because there have been an economic downturn. Remittances in Albania represent the second main source of incomes and this study documents the recent slowdown in workers' remittances, the money that international immigrants send back home. Current data indicates that remittance flows have slowed for all regions of the globe. This paper tries to analyze the impact of the economic crisis on remittances level and also the negative impact of their slowdown in the Albanian economy.

Keywords: Emigration; workers' remittances; financial crisis; foreign direct investments; consumption level

Introduction

Remittances, the money that international immigrants send to their country of origin are a crucial and growing source of external financing in many developing countries. The data have shown that they have grown faster than the private capital flows and official aid until the economic crisis have had a negative impact on them. The world economic crisis began in the years 2007-2008 in USA, which was caused from the banks system at United States of America and also from the uncovered, where the fall of weight of securities has caused the damage of the financial institutions and from the uncovered collaterals of derivate instruments exploded on Wall Street, which bring the biggest economic recession from the crisis of the year 1929 and after. Before the impact of the economic crisis according to the World Bank, total remittances

recorded at the global level have increased from 2 billion USD in 1970 to a record level of 456 billion USD in 2008. This large flows recorded during this year's are due not only have been an improvement in the statistical gathering of this flows but also of the increased migration levels. One of the main reasons that people migrate is the lack of the possibilities for finding a job in the country of origin and therefore remittances have become essential for the survival of the households. Remittance flows, funds received from migrants working abroad, have become enormously important as a source of income in many developing countries (Giuliano and Ruiz-Arranz, 2005; Mundaca, 2005). Remittances have grown from 3 billion USD in 1975 to close to 370 billion USD in 2007 (World Bank, 2008). This dramatic growth has had important implications for poverty reduction (Adams and Page, 2003), economic growth (Solimano, 2003) and financial development (Aggarwal, Demirguc-Kunt and Peria, 2006).

The impact of the economic crisis in the remittances levels is in the focus of many economists and studies because they suggest that remittances are the second largest source of external finance for developing countries after Foreign Direct Investments (FDI), both in absolute terms and as a proportion of GDP. A recent report from the World Bank (2008) indicates that in 2008, migrants sent about 305 billion USD back to their home countries. Recipients of these transfers typically spend the money on necessities such as food, housing, health care and educational expenses (Amuedo-Dorantes et al. 2007; Edwards and Ureta, 2003; Gitter and Braham, 2007). Moreover, remittances have helped receiving countries deal with financial distress and have been an important source of support during humanitarian crises (Savage and Harvey, 2007). Contrary to foreign direct investment, remittances have a direct impact on household incomes and, since there is no need of direct government intervention, remittances are less likely than foreign aid to end up in the hands of corrupt government officials (Kapur, 2004). In addition, remittances also represent a lucrative business for many banks and money transfer agencies in the United States and abroad (Wucker, 2004). The main consequence of the economic crisis has been a slowdown in the flow of these transfers. From 1997 to 2007, remittances flows to developing countries registered an average annual growth rate of about 15%. These flows increased from 71 billion USD in 1997 to 281 billion USD in 2007. However, the growth rate was just 8% for 2008 (compared to 23% for 2007) and the World Bank expects remittances to drop by about 7 to 10% in 2009 (Ratha et al., 2009a).

Remittances have a major importance and essential impact for the majority of the Albanian population and the whole economy since the year 1990s where the country was faced with the emigration of the free labor forces. According to the data remittances in Albania are mostly used in consumption, investment in housing, savings and has a large improvement impact on the standard of living of the country. Remittances are an important source of foreign exchange earnings for Albania since

1992. During the last 17 years Albania received large amounts of remittances and became a main source of financing the great imbalance between the exports of goods and imports of services, by reducing the current account deficit. Inflow of remittances affects economic growth positively improving the balance of payment position and reducing dependence on external borrowing (Iqbal and Sttar, 2005).

In the course of 1992-1997, entered in the form of current transfers USD 2.8 billion, of which 1.9 billion are a contribution of the Albanian migrants. It is estimated that after reaching the climax in 1996, the remittances from expatriates reduced by half in 1997 because of the pyramid schemes phenomenon. In spite of that, another recovery of these remittances in similar was shown on the following years. During 1991-2001 period, emigrant remittances have continually increased and have represented about 10 to 22% of GDP. In the year 2001, according to an assessment by the Bank of Albania remittances amounted to about 620 millions US dollars, or about 15.1 per cent of GDP, from 150 millions of US dollars or about 22 per cent of GDP in the year 1992. The Bank of Albania reports that Albanian emigrants' remittances reached 1,028 million USD in 2004, which is about 13.5 per cent of official GDP (see Bank of Albania, 2005). During the years 2005-2008 remittances have shown an increase but with the economic and financial crisis they have a slowdown in their level. This sudden decline of workers' remittances flows have generated significant negative impact in the economy and also in declining of the consumption level, investment etc.

Related Literature

Different studies have shown that remittances represent an important and vital source of incomes in the country of origin. They have a direct impact on the household consumption, budgets levels and their personal incomes (Rapoport and Docquier, 2006). Several studies are focused in exploring the economic consequences of emigration through the impact of remittances on the household decisions as regards to the emigration flows and labor supply. The level of remittances that the emigrants can earn in the destination country can have a negative impact in the labor market in the country of origin and can cause the brain drain of the labor forces.

Konica and Filer (2009) has done a previous study on Albania by who use survey data from 1996 and point to two offsetting effects of remittances on labor force participation. This effect causes the increase of the labor supply of the households who have an emigrated members in their family, because they have to compensate the loss in their monthly incomes. On the other hand we can have the opposite effect because the remittances can be higher than this loss in the income level so the emigrants family members can choose not to offer more labor hours.

The findings of Konica and Filer (2009) also suggest that migrants' higher earnings abroad contribute to the development of household-owned businesses in Albania. In particular, members of households with returned migrants in Albania are more likely to be employed in a household business. While the findings of Konica and Filer (2009) are representative of several studies suggesting that the negative effect of remittances on female labor force participation is a response to higher incomes from abroad, the direction of causality between migration, remittances and labor supply remains to be established. It is unclear whether the migration decision as well as the decision to send remittances is not, in fact, influenced by lack of employment opportunities at home. According to the theoretical and analytical studies workers' remittances are mainly used for consumption purposes, investments in fixed capital and in small business. So remittances are seen as compensatory transfers between family members who lost the labor forces of their family, but the level of this earnings can depend on the level of the emigrants qualifications and skills.

Nevertheless, Stahl and Arnold (1986) argue that the use of remittances for consumption may have a positive effect on growth because of their possible multiplier effect, also, remittances respond positively to the incentives of investment opportunities in the home country. Many emigrants invest their savings in small businesses, real estate or other assets in their own country because they know the local markets better than in their host countries, or probably expecting to return in the future. We have to mention the importance and strong relationships in the Albanian families which are a vital factor and has a positive effect in the remittances level of the emigrants. In about two-thirds of developing countries, remittances are mostly profit-driven and increase when economic conditions improve back home.

Several studies have shown the positive impact of remittances in the economic growth, economic development and reducing the poverty by increasing the incomes in the country of origin, improvement of the living standards of the country, development of the education and health conditions [Calaro (2008); Jongwanich (2007); Stark and Lucas (1988); Taylor (1992); Faini (2002); Gupta et al.(2009)]. However Chami et al (2003) find that remittances have negative impacts on economic growth of recipient country because a significant flow of remittances reduce labor force participation and work efforts which lowers output. Thus, the impact of remittances on economic growth and development of recipient country has been controversial

In case of Albania, a number of studies have been undertaken at micro as well as macro level that directly or indirectly focused on the impact of remittances on growth (Burney, 1987; Arif, 1999; Adams, 1998; Malik et al, 1993; Nishat et al, 1993; Burki, 1991; Kozel and Alderman, 1990; Amjad, 1986; Nishat and Bilgrami, 1991). The general conclusion of these studies suggest that remittances have positive effects on economy of Albania in terms of aggregate consumption, investment, reduction in current account deficit, external debt burden

and improve education/skills of the households. Furthermore, labor migration is considered to be a useful source of foreign exchange earnings (Naseem, 2004). Siddidui and Kemal (2006) explored the Impact of decline in remittances on welfare and poverty in Albania. This massive inflow of remittances contributes in reducing current account deficit, increasing foreign exchange reserves, stabilizing exchange rate and reducing poverty. Economic crisis of 2008 has shown a decline in the level of remittances and it can be measured and seen in the most important variables that we mentioned and this whole situation shows the importance that remittances has in the economic situation of the origin country like Albanian case and also the negative effects of their decline in the standard of living of the country.

Economic impact of the Crisis in Albania

The crisis have shown and started to reflect its negative impact in different sectors of the Albanian economy and several performance indicators were dropping. Since the year 2009 there has been a decline in terms of economic performance. The real sectors have started to reflect the further drop in demand, fluctuation of the exchange rate and difficulties in financing. During this years Albania suffers from the high public debt as a result of the public loans with high costs, while the unemployment rate has increased and the remittances flows have fallen. The economic crisis have caused an economic slowdown and an important impact on the macroeconomic stability of the economy. According to the country report, the fiscal deficit which hovered around to 3% of GDP up to 2007, climbed to 7.1% by the end 2008 (IMF, 2010). It has been a slowdown in the growth of budget revenues, while the inflows of FDI have shown an increase mainly due to the increase of the privatization deals.

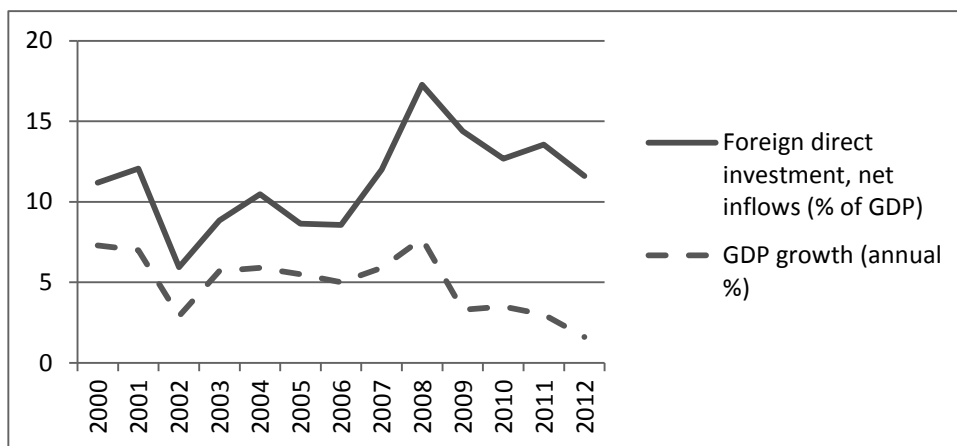


Figure 1: Foreign direct investments in % of GDP¹

¹ Source: World Bank Database 2013

The economic crisis have caused a weak growth, the rapid expansion of public investments (mostly on infrastructure expenditures), large borrowing to finance the high public debt (close 60% of GDP). The widening of the current account deficit from 13.7% in 2008 to 15.7% of GDP by the end of 2009, added another weak spot in the country's macroeconomic conditions (IMF 2010). The unemployment level have increased where by the end of 2009 the registered unemployment rate had increased to 13.8%, from 12.7% in 2008 (INSTAT, 2010). According to the Bank of Albania report the economy continued growing during 2011, the growth rate of GDP in real terms was estimated below 3% (Bank of Albania, 2011), which was lower than the rate of 3.9% in 2010. Growth was supported mainly by "external demand (reflected in the increase of export-related industries and tourism activity-related services) and a slight fiscal stimulus throughout the year" (IMF, 2011).

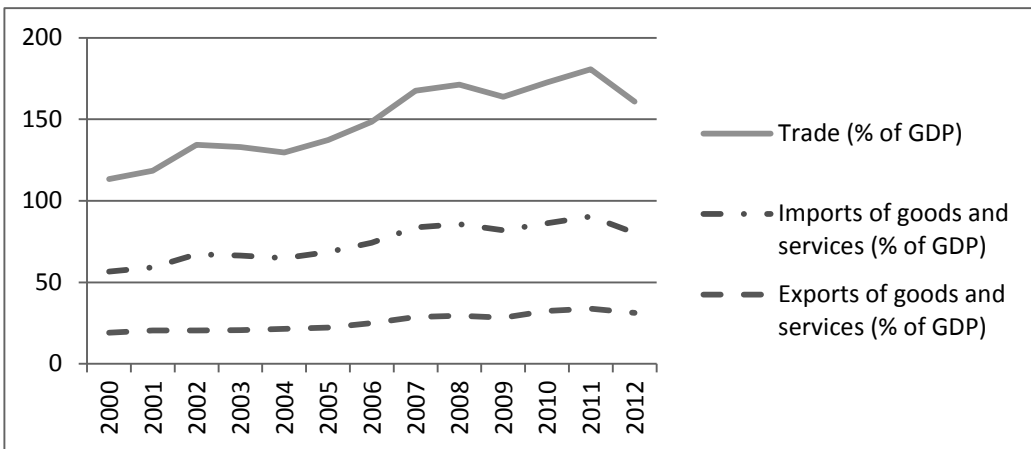


Figure 2: Imports and Exports Of goods in % of GDP²

Albania even after the crisis continues to be an important, oriented economy, the country's export base remains small while the imports are higher. In 2011, the exports are 2 billion USD and imported 5.39 billion USD; exports averaged 15% of GDP and imports 41% of GDP. Trade volume in 2011 increased by approximately 16%, with exports increasing by 22.6% and imports by 13.6%. Although the export/import coverage ratio improved in 2011, the trade deficit worsened by 9% year-on-year. The EU remains Albania's main trading partner, providing 64.1% of Albania's imports and receiving 72.5% of exports as of December 2011. Trade with Italy and Greece continues to represent the largest share of EU trade, with a combined 41.1% of imports and 58.3% of exports in 2011. Other major trading partners include Turkey, China, and Germany. Trade with the United States continues to account for an insignificant part of Albania's trade volume, focusing on a narrow range of goods and products. In 2011

² Source: World Bank Database 2013

total imports from the U.S. accounted for 1.5% of total imports, while the level of Albanian exports to the U.S. was insignificant. Major imports from the U.S. include food (mainly meat), transportation equipment (vehicles), machinery, and computer and electronic equipment, while the main exports to the United States are agricultural products, footwear, and textiles.

From the other side, the total expenditure and the consumption level have shown a decline from 29.3% in 2010 to 28.6% in 2011, while the total revenue relative to GDP declined from 26.2% in 2010 to 25.1% in 2011, resulting in an increase of the overall fiscal deficit of 3.5% from 3.1% in 2010 (Bank of Albania, 2012). According to the official data, the total public debt as a percentage of GDP was 58.9%, an increase from 57.8% in 2010. Such figures reflect the narrow space for fiscal stimulus and the need for a more prudential fiscal policy.

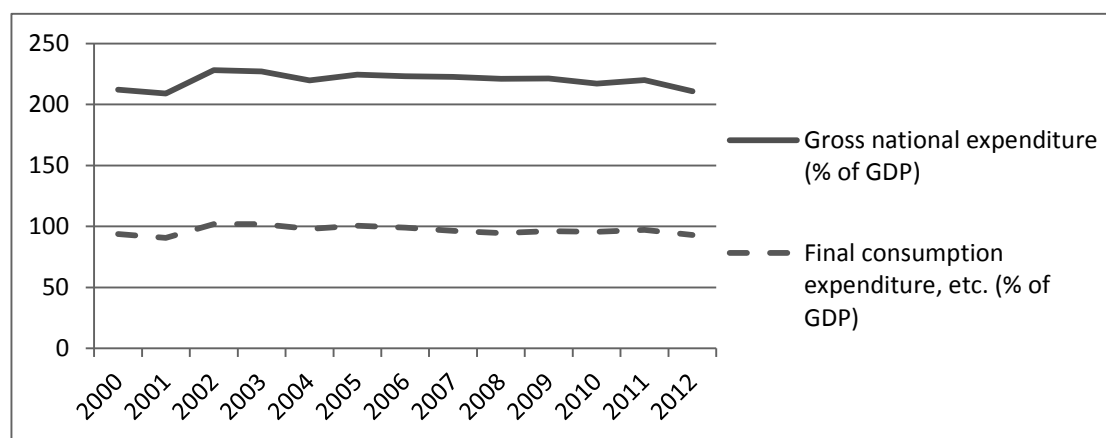


Figure 3: Consumption and Expenditure level in % of GDP³

As we mentioned before remittances are mostly used for consumption and investment, as a result of the economic crisis after the year 2010 there have been decline in this levels. During 2011, domestic consumption and investments remained weak, reflecting the prudential behavior of consumers and investors and also the uncertainty caused by international financial market developments. According to the Bank of Albania (BoA), the total deposits increased by 10.4% in 2011, while credit to businesses increased by 17.9%. The inflation rate averaged 3.5% during 2011, in line with the BoA inflation objectives. Prudential monetary policy continued during the year, particularly in the first half of the year because of high food and commodity prices. The weakening of the inflation pressure in the fourth quarter of 2011 (and in the beginning of 2012) and also the need for a stimulus to growth, forced the BoA to decrease the base (policy) interest

³ Source: World Bank Database 2013

rate to the lowest historical level, 4.25% (another decrease occurred recently in July 2012). However, BoA has continued to provide liquidity at an increasing maturity and at an extended range of collateral to the banking system. One of the main negative consequences of the economic crisis is on the level of remittances.

Impact of Economic crisis on Remittances level

For the first time Albania had an experience with the remittances inflows after the collapse of communism, where has shown a high dependency on them. Since then they have helped many families to fulfill their consumption expenditures, improve their standards of living, while at the same time financing the significant imbalance between the export of goods and the import of services and alleviate poverty. The value of remittances have played a crucial role in helping the families during difficult economic times, ensuring financial source of incomes, and providing incurrence. Several studies have been carried out in recent years to identify the impact of the economic crisis in Europe on the families receiving remittances. While the banking sector is usually thought of as being immune from the crisis in Albania, it is widely believed that the major channel affected by the crisis in Albania is the decrease in the level of remittances sent to the country. According to Central Bank of Albania estimates, remittances by Albanian migrants reached 1,304.5 million USD by 2007 rising from 150 million USD in 1992 (increasing by 870% over 15 years). After 1990, the value of remittances ranged between 10 and 22% of Albania's GDP (almost the size of an economic sector), and were higher than exports, net foreign direct investments and official development aid. These effectively covered almost half the trade deficit, representing the main foreign financial source, and one of the main factors determining the extroversion of the Albanian economy. The most recent survey from the Bank of Albania in 2009 suggested that almost 64% of annual remittances are sent to rural areas in Albania to help with daily expenses (World Bank predicts that almost 35% of Albanians would be living in poverty without them).

Data from the World Bank shows a fall in the absolute value of remittances (WB, 2010). The value of remittances sent to Albania was the highest in 2007 at the wake of the global crisis but it has fallen consistently thereafter. The data shows that in 2011 the value of remittances sent to Albania was around 692 million Euros or 27% lower than in 2007, thus indicating that the sustainability of this source of finance is questionable. According to the data obtained from the World Bank, the importance of remittances as a percentage of GDP has fallen consistently in the past five years. The latest data for 2011 shows that remittances accounted for only 7.3% of GDP or were more than 6% points lower than in 2006 (WB, 2011).

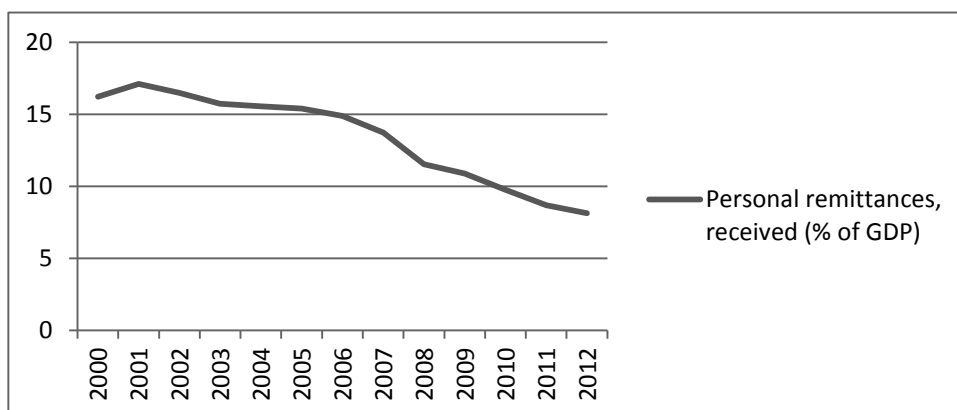


Figure 4: Remittances level in % of GDP⁴

During the last two decades, the phenomenon of migration has been at the very core of the political, economic and social changes occurring in Albania. By the end of 2011, about 1.4 million people or about one third of the Albanian population was estimated to be living abroad, mainly in Greece and Italy (WB, 2011). Smaller numbers are spread throughout different European countries (UK, Germany, etc) as well as USA, Canada and Australia. While, more than 20% of the population migrated internally (WB, 2007), no other country of Central and Eastern Europe has been similarly affected by international and internal migration, and within such a short timeframe. Migration has turned Albania into ‘a country on the move’, as characterized by Carletto et al., (2006) or into a ‘sort of laboratory for studying new migratory processes’, according to a description by Russell King (2005).

The economic crisis has caused a decrease in the emigration outflow of Albania, because of the high level of unemployment due to the lack labor demand in the country of destination. The savings level have shown a decline Comparing 2009 to 2008 data, the average annual savings accumulation of Albanian migrant HHs effectively decreased by 12%. Remittances constitute an important driver of Albania’s domestic demand. The decrease in the flux of remittances would lower the standard of living for many households, cause serious hardship for many and negatively influence some macro-economic indicators. According to the econometric models estimations by the World Bank (2010) suggest that for the overall economy (excluding agriculture) a 10% decline in remittances would lead to a 3.6% reduction in domestic demand. For several years the construction sector has been a vital and important contributor to the Albania’s GDP and the data shows that the decline of remittances due to the economic crisis has resulted in sharp contractions evidenced in Albania’s construction sector over the

⁴ Source: World Bank Database 2013

previous years. In fact, Albania's GDP growth remained positive throughout the crisis but has shown a decline in their values. Also the economic crisis has a negative impact in the poverty reduction with a lost in 4 percentage points. One of the main effects of the economic crisis is the return of emigrants that can cause the increasing rate of unemployment and higher labor supply. We have to pointed out if the return of emigrants include the high skilled and qualified ones so there will be an increase in the human capital investment of the country which can have a positive impact on the economic growth. On the other hand the return of emigrants can have a positive effect in the transfer of accumulated savings and opening new business because they wish to invest and wish to invest their financial, human and social capitals in Albania. is where a part of the family (parents, children, women) return to Albania.

Remittances are used primarily to support basic daily needs (food, clothing, etc.) of receiving HHs, and thereafter to improve living conditions (buying furniture, home equipment, etc), and lastly to expand or build a new house. A part of remittances are also used to organize important household/social events (such as weddings, baptisms, funerals, etc.), while a small component might be deposited in the bank system or, more likely, saved in cash at home. Only small parts of remittances are used to invest in economic activities, mainly in micro-enterprises within the service sector. Consequently, remittances have improved the living conditions of many families in Albania but have had a limited role in sustainable development or job creation. 12% according to the ALSMS 2002 and 11.8% according to 2007 ETF study.

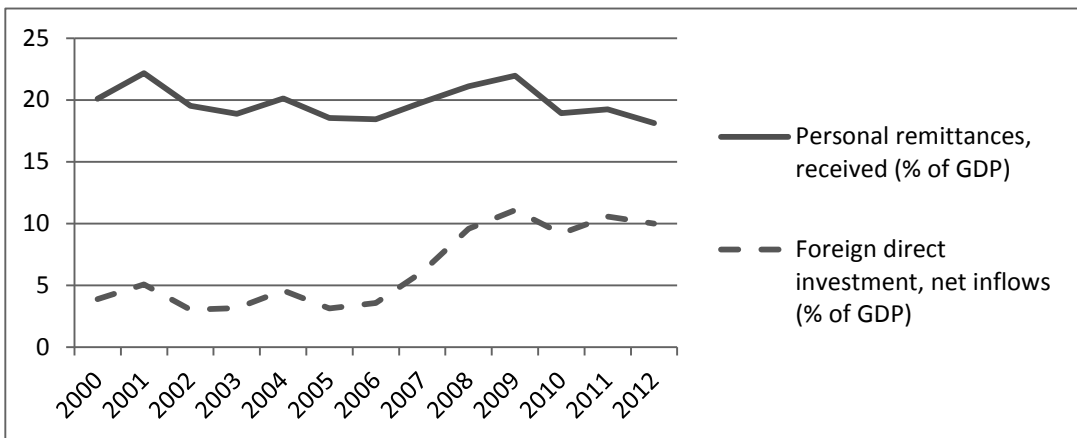


Figure 5: Remittances and FDI flows⁵

FDI in Albania are considered as one of main contributors on the economic growth of the country. Our GDP and export growth rates were the fastest growing in South East

⁵ Source: World Bank 2013

Europe from 1997 to 2009 (Dragusha, Bejleri & Puhi (2010)). While most countries in South-East Europe suffered from sharply declining FDI inflows in 2010, Albania received an increased amount. After 717 million EUR in 2009 (according to data that were revised by the Bank of Albania since the publication of the Albania FDI Report 2010 and UNCTAD's WIR11) inflows in 2010 amounted to 793 million EUR. In 2010 Albania had the second highest amount of FDI inflows among SouthEast European countries, after Serbia. The decline of remittances have a negative impact even in the Foreign Direct Investments inflows The FDI decline in 2011 reduced Albania's share both in global and in regional inflows. Although the value of FDI flows to Albania is modest due to the small size of the host economy, its relative importance for the Albanian economy is rather high.

Remittances inflows in Southeast Europe

Southeast Europe as one of the most relevant remittance recipient regions in the world the economic crisis had a negative impact in lowering their inflows. The high level of remittances is due to the large flows of emigration - based mainly in the motives for emigration: economically determined, as well as the strong family ties which the emigrant population still maintains with the country of origin. The most important recipients of remittances, among the Southeast European countries, are: Moldova, Bosnia and Herzegovina, Albania, Serbia, Bulgaria, Romania, and Republic of Macedonia. The total amount of remittance inflows (compensation of employees, workers' remittances and migrant transfers), or of current transfers, net (defined in accordance with the BOP definition), is one of the most important items of the balance of payments, and they largely contribute into providing sustainable balance of payments, especially for covering the deficits in the foreign trade. According to the data the remittances levels as a share of GDP in some countries it reaches 34,7% (e.g. Moldova in 2006). With the exception of Bosnia and Herzegovina, where the data shows a decreasing trend over time (as a result of GDP growth in recent years, and low coverage of remittances flows), all other countries have stable remittance inflows over the period 2000-2008 (Albania, Serbia and Bulgaria), or a continual trend of growth (Romania, Moldova and Republic of Macedonia). Remittance inflows declined in 2009 in almost all of the analyzed countries (with the exception of Serbia and R. Macedonia), due to the global crisis that caused remittance inflows in developing countries to fall by 5.2%.

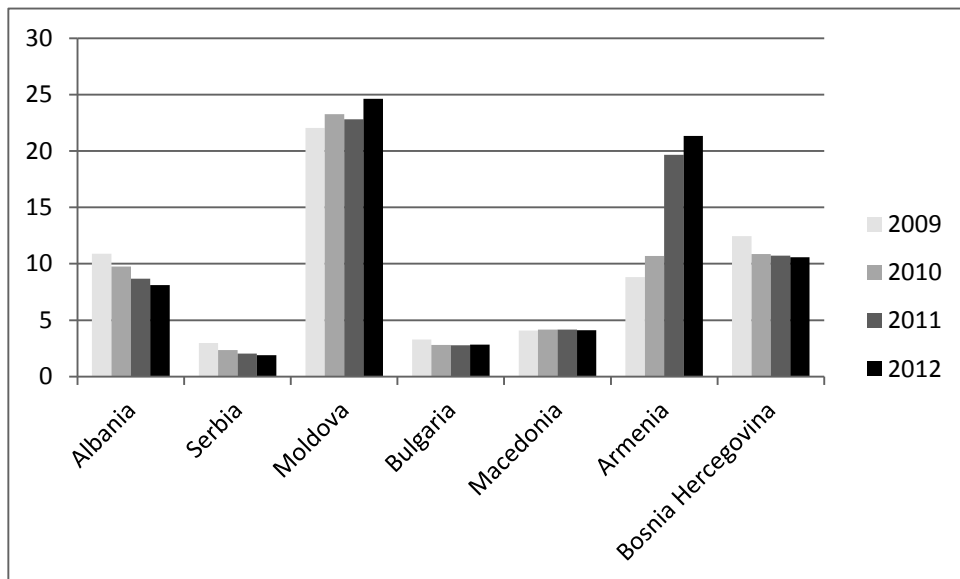


Figure 6: Remittance inflows as a share of GDP-selected countries from Southeast Europe (2000-2012) (in %)⁶

Remittance inflows in 2009 had an effect on reducing the current account deficit by almost 4 times in Moldova, 2 times in Serbia, and almost 2 times in Albania. On the other hand, it is obvious that remittances, when they are mostly spent on imports, can by themselves create trade deficits. Even in that case, it is clear that such deficits are self-financing and pose no threat to balance of payments stability. Another way to show the importance of remittance inflows is to compare them with other types of capital flows. Only in Bulgaria and Romania, remittance inflows are ranked behind foreign direct investment as a source of external funding. In other four countries (Albania, Bosnia and Herzegovina, Macedonia and Moldova) remittances are significantly larger than other types of capital flows. This is in line with international experience, which confirms that poorer and smaller countries receive relatively larger remittances. Inflows from portfolio investments are negligible by size, indicating a high level of underdevelopment of the secondary stock exchange markets in these countries.

However, despite their positive contributions to foreign exchange earnings and national income, remittances could also have their downside. Extensive and continuing inflows of remittances sometimes can lead to a significant appreciation of the real exchange rate and therefore a loss in the relative export competitiveness of price sensitive tradable goods. Although the empirical evidence of negative effects from remittances on terms of trade and growth are limited, usually these negative effects exist in

⁶ Source: World Bank data, Central bank of Serbia, Central bank of Moldova and Central bank of Albania (2013).

cases of small and open economies which are, at the same time, large remittance receiving countries. For example, one IMF report finds the significant appreciation of the exchange rate in Moldova as a result of the extensive remittance inflows (IMF, 2005). Lucas (2005) argues that Albania greatly benefited from remittances as a source of foreign exchange and as a safety net for the poor people, but this has also postponed the depreciation of its currency and thus potential export growth.

The main interests of the central bank in the recipient countries is how to capture the remittances inflows, but the main interest of the researchers is how to capture the basic influences and consequences of these flows, or what are their effects in general. The most important influence of the remittance flows, on which most of the discussions has been led, is whether these flows are inflationary, and whether they generate relative price changes, causing reallocation of domestic resources (MPRA Paper, May, 2010).

Regardless of the possibility of remittances causing negative effects in the recipient countries, most researches would agree that the positive effects of remittances are far more important than the negative ones. Therefore, the analyst and the policy makers are interested very much in the stability and sustainability of the future remittance flows. Knowing these characteristics is particularly important for better utilization of the potential future inflows, especially in the episodes of economic and financial crises.

Conclusions

Remittances are the most important and vital source of incomes for the country of origin, where their outcomes and effects are reflected in the main economic indicators such as consumption level, investment level, living standards' levels, poverty alleviation etc. To most citizens of sending countries remittances are the most important resource available in the struggle to survive. In Albania the remittances inflows has had a crucial impact in the whole economy and represent the second largest inflow of income. But like other countries in the region, Albania was also affected by the economic crisis and after the year 2008 there has been a decline in their level. Its limited integration into global markets and especially the low level of development of financial markets has kept the country relatively isolated from the financial meltdown. The impact on remittances is likely to be an important transmission mechanism of the effects of the global financial crisis on developing countries. This paper has provided a theoretical and data analyses that shows the impact of the economic crisis on remittances levels. These estimates are based on estimated variables derived from carefully specified of the determinants of remittance outflows and inflows. The study suggests that the economic crisis is likely to have some negative impacts on remittances levels

and indirectly by the impact of their decline on GDP level, consumption, FDIs, unemployment rate etc.

Recommendations for policymakers:

- Encourage remittance receipt through formal channels:
 - Improving access to banking for remittance senders and recipients, which can also reduce costs associated with remittance transfers.
 - Strengthening competition in the remittance service provider industry to reduce money transfer costs.
- Strengthen financial, legal, and regulatory frameworks that govern financial flows and facilitate transparency and competition within the banking sector.
- Incentivizing remittances use for entrepreneurship and enterprise activities.

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