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How do Filipino families use the OFW remittances?

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The Philippines is now one of the world's largest recipients of overseas workers' remittances. In fact, the country is the largest recipient of remittances next to India, Mexico, and China.¹ Latest data from the Bangko Sentral ng Pilipinas (BSP) show that from January to September 2007, international remittances from abroad coursed through formal channels have already reached US\$10.477 billion. This is 15 percent higher than that of the estimate during the same period last year.

There are several important questions arising from the continuing surge of overseas Filipino worker (OFW) remittances. Do families receiv-

ing remittances spend more on consumption goods? Do they make investments at all? How can the Philippines harness these inflows for development?

This *Policy Notes*, as based from this author's longer study, looks into these concerns, especially on some of the trends and patterns of the Filipino families' use of remittance income.

Growth of remittance receipts

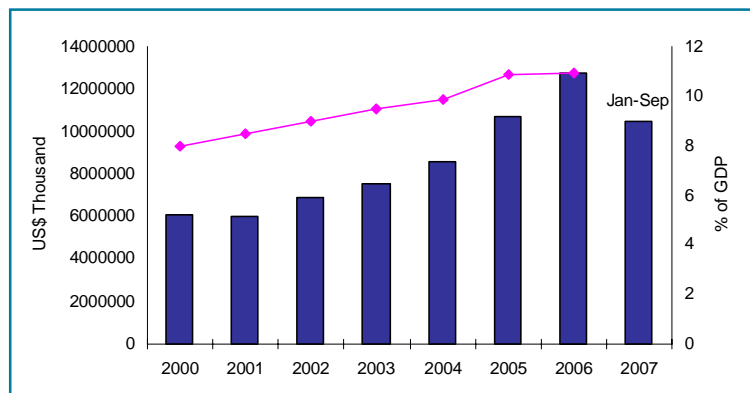
Remittance receipts have been rising at phenomenal rates since 2002. In fact, Figure 1 shows that from 2001 to 2006, remittances

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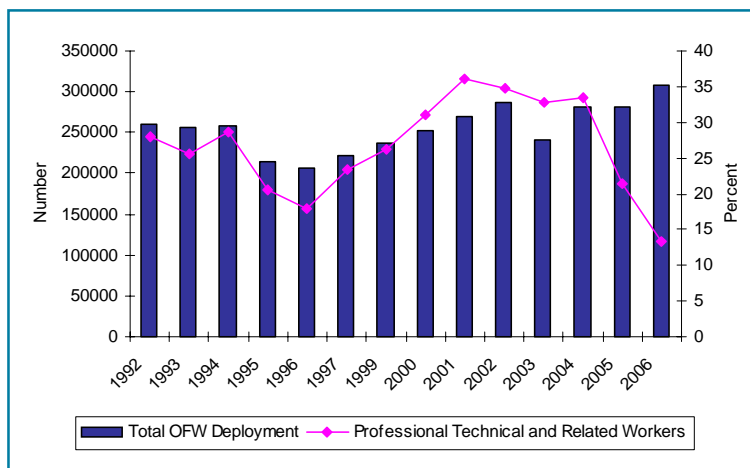
¹ Based on UN International Fund for Agricultural Development estimates for 2006.

Figure 1. OFW remittances in US\$ thousand



Source: Bangko Sentral ng Pilipinas

Figure 2. Total OFW deployment (new hires)



Source: Philippine Overseas Employment Administration

have been growing at an average rate of over 16 percent annually. In 2006, it constituted about 11 percent of the country's gross domestic product (GDP). At the household level, remittance income² constituted, on the average, about 5.8 percent of total family income in 2003. An Asian Development Bank (ADB) study, however, put this percentage at about 80 percent of the beneficiary household's total income. In the same study,

it was found that Filipino workers abroad regularly remitted an average of \$340 a month through bank channels in 2003.³ This indicates how big a role remittance income can play in the country's national development.

Remittances are a direct outcome of labor migration. The Philippines, one of world's largest labor exporters since the 1980s, is sending hundreds of thousands of its labor to various destinations every year. One major concern arising from this is the detrimental effect of the so-called brain drain, an inevitable outcome of skilled labor migration. Official data show that the percentage of professional, technical, and related workers to total OFW deployment has been more than 30 percent during the period 2000 to 2004 and went as high as 36 percent in 2001 (Figure 2). The recent trend, however, exhibits a declining share of professionals in the pool of OFW new hires. Other subjects of debates are the possibilities of migration resulting to inequitable income distribution and to a culture of dependence on remittances.

Amidst these concerns on the possible effects of migration, one topic that is of great interest is how the country can maximize the gains from OFW remittances. Thus, it is an

² Estimate refers to the remittance income obtained from the cash receipts from abroad variable of the 2003 FIES but excludes dividends from investments abroad and pension payments received by Filipino families.

³ As cited in the 2004 ADB study on remittances of Southeast Asia workers.

interesting subject to look at how Filipino families spend their remittance income.

How do Filipino families spend their remittances?

Recent literature on remittances and their impact on the development of labor-sending countries recognize that even without investing these remittances, they can still contribute to the local economy by way of the multiplier effect of consumption done by the families receiving the remittances (Taylor et al. 1996). Investing the money in productive enterprises, however, yields bigger impact on the local economy. In the Philippines' case, the importance of this cannot be overemphasized. The problem of brain drain, as mentioned earlier, an issue by itself that requires in-depth study, gives more reason to investigate how remittances can help the country's economy by being more than just sources of consumption income and a "bump-up" to the country's balance of payments (BOP). Spending remittances on mere consumption has less contribution to local development. In fact, if remittance income induces people to consume more and produce or work less, it is preventing its potential to spur local development and may even produce dependency among migrant workers' families thereby disrupting local production.

The body of literature on this particular topic is divided into two main views. The earlier view is pessimistic, saying that households receiving remittances do not make productive investments. Such households often spend

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their increased income on housing and consumer items such as household appliances. In other studies, remittances and in a sense, migration, had adversely affected local production.⁴ A number of recent studies, however, have challenged these findings. Using bigger samples and sophisticated econometric analyses, they found that remittances induce households to invest in human capital such as education.⁵ Remittance income via exchange rates shocks, as will be seen later in this *Notes*, also influences households to engage in entrepreneurial activities (Yang 2005).

There are only a few recent studies dedicated to this subject for the Philippines. Yang (2005), for one, found that increased remittance income via exchange rate shocks lead to more hours of work in self-employment, greater child schooling and entry into relatively capital-intensive enterprises by the migrants' origin households. An ADB study in 2003 found that beneficiary households of

⁴ These include Lipton (1980), Ferran and Pessar (1991), and Gorges (1990) all cited in Taylor et al. (1996).

⁵ Adams (2005) and Sosa and Medina (2006) found such results.

While there is little evidence of a clear and strong relationship between increased remittances via the peso depreciation and overall entrepreneurial activities, Yang found that increased remittances via exchange rate shocks lead to entry into new entrepreneurial activities. In particular, these activities are in transportation and communication services and manufacturing, both of which require large up-front fixed investments.

remittances consumed highest on food and education. Meanwhile, Tabuga (2007) found that families receiving remittances devote more income on consumption goods and invest more on education, health care, and housing. A closer look at each of these studies further reveals the following points.

Yang (2005) studied the influence of remittances on the entrepreneurial activities of households receiving remittances and on child schooling. He did this by obtaining the panel data sets from the 1997 *Family Income and Expenditures Survey* (FIES) and the 1998 *Annual Poverty Indicators Survey* (APIS) and merged these to the *Labor Force Survey* (LFS) and the *Survey on Overseas Filipinos* (SOF). The idea of this methodology is to obtain those households with OFWs and investigate the effects of changes in the remittance income via exchange rate shocks. In other words, Yang used the peso depreciation during the said period as an exogenous shock to remittances in his model to examine any subsequent effect on the entrepreneurial and human capital investment behavior of the households under study.⁶

While there is little evidence of a clear and strong relationship between increased remittances via the peso depreciation and overall entrepreneurial activities, Yang found that increased remittances via exchange rate shocks lead to entry into new entrepreneurial activities. In particular, these activities are in transportation and communication services and manufacturing, both of which require large up-front fixed investments. In terms of human capital accumulation, favorable shocks in remittances are associated with more child schooling, less child labor, and higher household educational expenditure.

In 2003, the ADB conducted an in-depth study titled “Enhancing the efficiency of overseas workers remittances” wherein market surveys and focus group discussions were done in the Philippines and two major remitting countries, Singapore and the United States. One of the objectives was to determine the use of remittances. Among households where remittances supplement total income, remittances were mostly used for food, household operations, utilities, and education. Aside from these, the usual allocations go to fiestas, special occasions, and savings.

⁶ The methodological importance of doing this is that he addressed the problem of endogeneity often encountered in using remittance income as an explanatory variable in the model. This is due to the fact that remittance income can be endogenously determined by the socioeconomic status of the households. Thus, using remittances to explain entrepreneurial behavior of households doubly reflects the socioeconomic attributes of the households and is an econometric no-no.

The paper by Tabuga (2007), on the other hand, focused on the expenditure patterns of Filipino families and how remittances influence budgets on various commodity groups. Tabuga did a cross-section analysis of the 2003 FIES, thereby providing a nationwide picture of the influence of remittances on family expenditure patterns. In her paper, the presence of remittance income was used as a dummy variable that explains spending behavior of the remittance-receiving families. It tested the influence of remittances on commodity groups such as food, tobacco and alcohol, education, and health care, among others. The importance of looking at the general spending patterns of remittance-receiving families is that it does not make a lot of sense to just look at how households spend remittances because of its fungibility. This means that even if families spend remittances on conspicuous consumption, remittances may have freed other parts of income into productive ventures (Adams 2005).

Based on this study, claims that households receiving remittances may be spending more on conspicuous consumption indeed have some validity. This is shown by the strong and consistent evidence that remittance induces households to allocate more on consumer goods and leisure. However, there are also indications that households might be putting the extra income into better uses. Similar to findings of international research works, remittance induces households to spend more on education, medical care, and housing.

Moreover, remittances also influence families to devote more on durable goods. What is more interesting is that remittances do not tend to induce households to spend more on vices like tobacco and alcohol. They also allocate less on food, particularly those that are regularly eaten outside. Table 1 summarizes the effects of remittances on various items of the expenditure basket.

Implications for policy

The expenditure patterns and investment behavior of remittance-receiving families reflect the general condition of the country, specifically its investment climate. Since remittance-receiving families have tendencies to work more on self-employment activities and enter into enterprises, the government should enhance its role in providing necessary support mechanisms such as sound credit facilities and trainings on entrepreneurship for them to stay in business and expand their enterprises. The Overseas Workers Welfare Administration (OWWA) and National Livelihood Support Fund (NLSF) Project is just one of the government programs with such objectives. This program aims to help OFWs,

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Table 1. Influence of remittances on budget allocation

Commodity Group	Effect/s [*]
Food, particularly food regularly eaten outside	Negative and significant; magnitude of effect increases as budget allocation on food increases
Education	Positive and significant; magnitude of effect increases as budget allocation on education increases
Medical care	Positive and significant; magnitude of effect is very high when the allocation is high
Housing and minor repair	Positive and significant; insignificant when the allocation is relatively very high
Tobacco and alcohol	Mostly negative but insignificant
Consumer goods	Positive and significant; magnitude of effect increases as budget allocation increases
Leisure	Positive; significant in all distributions of the budget allocation except the 0.9 quantile or when the allotment is very high
Gifts	Positive and significant when the allocation is low but negative when the budget share is high
Fuel, transportation and communication, and household operations	Positive and significant; magnitude of effect increases as budget allocation increases
Durables	Positive and significant
Others	Negative and significant; magnitude of effect increases as budget allocation increases

* Please refer to Tabuga (2007) for detailed explanation of the effects. Note that effect in here refers to the direction and significance of the coefficient of the interaction term: remittance dummy and logarithm of expenditure per capita on various distribution of the budget share.

Source: Tabuga (2007)

their families, and organizations gain access to entrepreneurial development opportunities and credit facilities. Moreover, the OWWA provides several education and training programs to OWWA members. It also conducts financial literacy programs in its Pre-Departure Orientation Seminars (PDOS). From 1995 to 2005, the OWWA has benefited more than 24 million OFWs with its range of programs and services.

However, many of the current programs of the government through the OWWA cater only to OWWA members. These efforts must be improved further and expanded to allow as many OFWs as possible to avail of such programs especially those related to entrepreneurship, financial literacy, and investment of their earnings. To echo the ADB study's

recommendation, financial literacy programs extended to OFWs during their PDOS should likewise be extended to their families, especially in the rural areas where many OFWs originate.

At the same time, because remittance-receiving families invest mostly in housing, the government, through the Pag-IBIG Fund, now provides assistance for OFWs and their families in availing affordable housing. The Social Security System (SSS), meanwhile, has also created a voluntary provident fund for OFWs called Flexi-Fund that is designed to enable workers to save hard-earned money while working abroad.

Remittances can also lead to enhanced human capital accumulation as evidenced by greater

child schooling and greater household expenditure on education and medical care by the remittance-receiving families. These efforts, however, must be complemented by the government's aggressive action to improve the quality of education and health services. In this way, OFW families can expect better returns to their investments on human capital. At the same time, the country can expect long-term gains from labor migration and remittances because investments made on education and health care have a greater chance of producing better human resources for the country.

The magnitude of remittances indeed provides immense opportunities for the development of the country. However, remittances should not be treated as a panacea that gives a reason for the government not to pursue policy reforms that ensure long-term economic progress. Current efforts of the government such as legislations designed to provide incentives and privileges to overseas workers and Filipino migrants abroad to invest in the country must be coupled with long-term policy reforms that aim to improve the overall investment climate. Reforms that foster good investment climate entail good governance, sound physical and social infrastructures, peace, and stability.

Remittance income, temporary as it is, is not the solution to the chronic problems of the society but is a potential tool. If the country grabs the opportunities presented by the large inflow of remittances and if more attention is

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focused on pursuing effective reforms to improve the country's economic condition, then the Filipino labor force will not have to seek greener pastures abroad. The problem of brain drain can thereupon be avoided and the country will have a greater chance of achieving progress. 📄

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