Remittances to India's Rescue Again

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There were growing global uncertainties in the last four months, from September, 2023 continuing into early December as well. They were related to falling inflation in USA consequent to a series of aggressive hikes in its policy interest rate, by the US Federal Reserve (the Fed) to fight inflation. The US Inflation was at its highest (9.1% in June 2022) in 20 years, following the Ukraine-Russia conflict breaking in March 2022. Steady increase in the policy interest rate, known as Fed Funds rate, brought down the American inflation to 3.7%, in September. As part of anchoring inflationary expectations, the Fed indicated in advance there might be only one cut by about 25 basis points or 0.25% in its policy interest rate of 5.5%, which was fixed in August 2023 and continuing since then.

That was sufficient to cause uncertainties, which resulted in a high degree of volatility in short term capital flows to India, Foreign portfolio investors (FPIs) holding shares and short term debt, started to pull out their funds from India, as there was no likelihood of further increase in its domestic interest rate. India's inflation was within the comfort region, 4%-6%, The Reserve Bank of India (RBI) was keeping its policy interest rate (RPO) unchanged 6.50%, since June 2023.

With the Israel-Hamas war, which broke on October 7, attention of central banks all over the world attention is now on fresh disruptions in supplies, likely to cause yet another bout of inflation from yet another war. The Fed formally announced on December 13 that there would be no cut in its policy interest rate, although inflation has further decreased to 3.1% in November. The Fed also confirmed that there will be no cuts before end of 2023 and if at all, there would be three small rate cuts, by 25 basis points each.

Volatility in exchange rate and stock market gyration

The global uncertainties and volatility have already done the damage. A total of US$5 billion of FPI funds have already been taken out of India by the fickle minded, speculative investors in September and October, which was further prolonged into early November. However, as the market had been rife already with bearish rumours that the much- awaited cut in interest rate may not materialize before end of the new year, there was a slow but slight reversal of outflow funds from India in November. It was small, though at just around US$ 620 million. But soon, India's foreign exchange reserves (Forex) started to grow: from US$ 595 billion on November 17 to US$ 598 billion to on December 1 to US$ 607 billion on December 8, and to US$ 616 billion on December 15. As I write this, for the week ending December 22, it was a 20-month high of US$ 615.97 billion, though still below the highest of US$ 642 billion recorded in October, 2021. The conventional wisdom would convey to us as the Forex goes up, the external value of the currency would also tend to rise. But it did not! The market rate, known as spot rate depreciated. It went down to the lowest rate ever: ₹ 83.40/US dollar on December 13. Another strange event also took place. Contrary to usual expectations, as both the NIFTY 50 and BSE Indexes rose by 6%, on the same date, the Indian rupee depreciated.

What is the "reliable indicator" of economic health of a nation? Is it stock market performance or change in external value of domestic currency? Among the two, stock market performance is influenced primarily by sentiments about the pure monetary gains in the future, determined by interaction of bearish and bullish tendencies. On the other hand, external value of the currency is determined by good or poor macroeconomic performance in the immediate past, conveyed through additions to or decrease in Forex for settling external payments in hard currency. The answer to question: Don't rely on stock market reactions and spot exchange rate changes. They are transitory.

Components of Forex

Components of Forex include earnings from exports of primary produce including wheat and rice and coal and minerals, and vegetables and fruits as well as processed agricultural goods like flour and cooking oil and manufactured goods; and manufactured goods, such as textiles and footwear and a whole range of consumer goods. If the countries are on a higher scale of development, exports would include capital goods including machinery and automobiles and transport vehicles. Countries, with no mineral resources of any kind, but happened to have abundant sun shine and surf depend on tourism. They include island nations such as Maldives and Mauritius in Indian Ocean, Fiji in the South Pacific and Jamaica and Barbados in the Caribbean region. Thus, tourism is now one of the most important sources for small island states.

Impact of globalization

With increased globalization, and liberalization of trade and payments, capital besides goods and services, has been mobile in search of higher return. Developing countries are keen to attract capital and entrepreneurial skills to upgrade their development base and improve technology and management. They are the most desirable forms of investment, known as foreign direct investment (FDI). Most of the FDI is from multinational investing corporations (MNCs), whose interests are long term growth in the host economy. They have been contributing to production of consumer goods but also

of machinery and transport of vehicles, not only for local consumption but also for exports The FPIs, on the contrary, are only speculators with short-term gains from buying and selling shares and bonds. They have no interest in country's development.

The latest balance of payments (BOP) data show that the current account deficit (CAD) for first half of FY 2024 (April to November 2023) is negative, though small at 1% of GDP. That is the outgoings (imports of goods and services: IMGS) exceeding the incomings (exports of goods and services: EXGS); it is financed by running down the Forex. The small deficit is due to better performance by services sector dominated by IT sector, thus indicating a diverging trend in manufacturing and services exports. While services exports rose by 5.3% merchandise exports decreased by 6.3%.

Forex is growing more because of rise in FDI inflows due to attractive incentives as well more relaxed, open policies of the government of the day. In addition, tourism in the pre-pandemic years has been a support. Other than FDI in hotels and resorts by MNC contributing to creation of jobs in the formal tourism sector, it has also responsible for increase in informal employment, especially in the high season (October to February). Besides, it has also given rise to new opportunities for part time employment for women in making and selling handicrafts, running kiosks for sale of ethnic meals and operating tour services for visitors. International tourism, however, has yet to return to the level of pre-Covid 19 period.

Remittances, "the unsung hero"

Inward remittances are rising from overseas Indians working in the Middles East and Singapore. Further, from the increasing number of first generation migrants, mainly low skilled workers who have chosen to work and live overseas and send cash to their families who are left behind in home countries, for their maintenance. The remittances from them are regular, weekly or monthly, and understandably in small amounts, which are a great support. Results of a survey on inward remittances by RBI showed four states, Kerala, Karnataka, Maharashtra, and Tamil Nadu are the major beneficiaries. Poverty reduction in the recipient families has been the most notable achievement.

Highly skilled migrants and together with those of second and third generations, called part of expanding diaspora were seen sending funds, not as regular as those of first generation. However, their contributions were sizeable, especially in times of natural disasters, such as earthquakes and floods, in response to calls for aid by affected countries.

Unrequited transfers

These remittances were not in the expectation of any return. These remittances were once called by IMF as unrequited transfers of funds. The term "unrequited" means the absence of any quid-pro-quo element. The remitting persons knew they were for food, shelter, children's education, medical services, and caring for the old, sickly, and the like. They do not expect any return from their regular transfers. However, they are additions to country's reserves. Even in recession periods in advanced countries, the migrant workers, laid off and are looking for jobs but on still unemployment relief hand outs, strive to continue their support. In critical times, when the left behind families are in dire straits, (example, the Kerala floods or the Kutch earthquake), the Indian diaspora rushed funds by stepping up remittances for immediate relief and reconstruction works.

TABLE 1 : Remittances before and after the pandemic 2018-23

Year	Remittances	
	(US$ billion)	Growth rate (%) over the previous year
2018	76.4	10.6
2019	83.2	8.9
2020	80.2	-3.6
2021	89.1	11.1
2022	111.2	24.4
2023	125.0	12.4

TABLE 2 : Top ten remittance receipient countries in 2023

Rank No.	List of Countries	Remittances (US$ billion)
1	India	125
2	Mexico	67
3	China	50
4	Philipines	40
5	Egypt	24
6	Pakistan	24
7	Bangladesh	23
8	Nigeria	21
9	Guatemala	20
10	Uzbeskistan	16

Source: Migration and Development Brief (World Bank 2023)

The World Bank Report on Migration and Development Bried 2023, released on December 19 highlights the role of inward remittances in developing countries. **Table 1** provides inward remittance flows to India during the pre-pandemic (Covid-19) period and the post pandemic periods: 2017-23. The latest figure for 2023 shows India received the maximum remittance

TABLE 3 : Inward remittances and other major inflows as % of FOREX

PARTICULARS	2018	2019	2020	2021	2022	2023*
FOREX (US$ billion)	400	465	590	640	568	607
Remittances (US$ billion)	76	83	80	89	111	125
Remittances (% of FOREX)	19	18	14	14	20	21
FDI (US$ billion)	62	74	81	84	70	NA
FDI (% of FOREX)	16	16	14	13	12	NA
Tourism Earnings (US$ billion)	29	30	7	9	17	NA
Tourism Earnings (% of Forex)	7	6	1	1	3	NA

Source: World Development Indicators Statistica

Notes: NA = Not available *Provisional

which is US $125 billion, It is also the highest so far, placing India first among the ten top recipient nations **(Table 2)**. **Table 3** also shows that percentage of remittances' contribution higher than those of FDI and tourism earnings.

Inward remittances rose in 2023, mainly because of tight labour market in both US, UK and Europe. The presence of strong base of India's highly skilled professionals and workers in US, UK and Singapore was yet another reason behind the high growth rate in remittances: 12.4% in 2023 over 2022. Additional factors are the extensive leveraging of labour retention programs, falling inflation in US and agreement with UAE for bilateral trade in dirhams and rupees, At the same the World Bank has cautioned against the risks lurking around the corner from likely return of inflation. Further, there are risks also from volatility in oil prices and downturns in high-income countries.

Worldwide costs of sending remittance costs to developing countries, however, continue to be high. The average costs are not coming down fast enough from more than 10% for sending US$ 200, which prevailed two decades ago. It is now at around at 6.2%. One of the UN Sustainable Development Goals is to achieve a reduction in the cost to 3% by 2030. Though more use of formal channels is now being used than ever before for ensuring that foreign exchange gets into official kitty, the average cost of the banking channels is still more than 12%. The Indian diaspora keeps their savings in safe and stable countries outside their original homes. The Report recommends introduction of Diaspora Bond Schemes for attracting them to countries of origin.

Governments of India in the past had at different times resisted temptations, often in terms of advice offered by overzealous bureaucrats for mobilising additional resources through a levy or fee on inward remittances. Wise counsel prevailed and reminded them of the Aesop fable of the "Goose that laid the golden eggs" and the idiom "killing the goose that lays the golden egg" which refers to the hasty and certainly a shortsighted destruction of a valuables resource.

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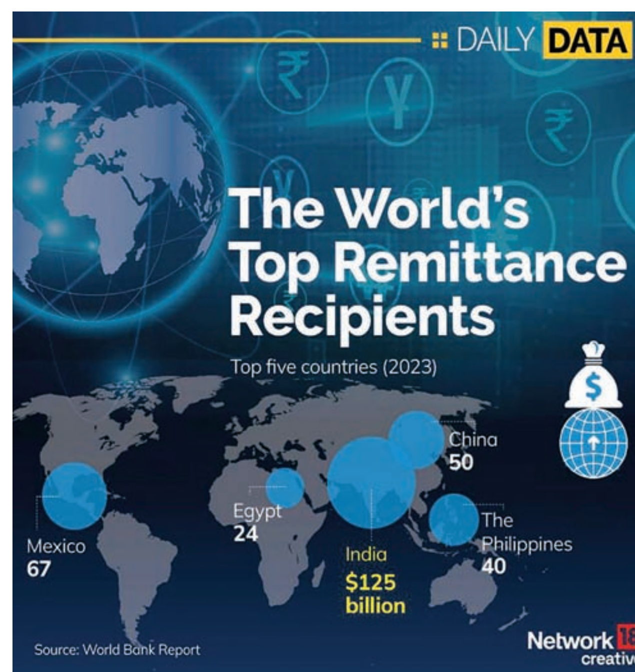

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