



FOREIGN REMITTANCES AND THE PERFORMANCE OF THE SUB-SAHARAN AFRICAN ECONOMY

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Abstract

Remittances in the world represent one of the major international capital inflows. Sometimes, they exceed the flow of Foreign Direct Investment (FDI) and Official Development Assistance (ODA). For Sub-Saharan Africa (SSA) countries specifically, little attention has been made in the study of remittances and economic growth. This study investigates the role of Foreign Remittances and the performance of Sub-Saharan African economy. The study adopts a panel econometric technique of pooled OLS, fixed effects model, random effects model, the Hausman test, the dynamic panel data model using the Generalized Methods of Moments System (GMM SYS) for 26 Sub-Saharan African countries in a period of 26 years (1990-2016). Other statistical tests carried out include Descriptive statistics, Heteroskedasticity test, panel unit root test, Wald test, white test and granger causality test. The econometric results of pooled OLS, the static (fixed effects and random effects) and the dynamic panel data models revealed that remittances inflows significantly affect the economy of Sub-Saharan Africa negatively. The granger causality test carried out also revealed a negative unidirectional relationship running from remittances to economic growth. This suggests that higher remittance channeled towards unproductive purposes has invariably led to a fall in economic growth in Sub-Saharan Africa. Therefore, Sub-Saharan Africans should invest their extra funds from remittances inflows in production of goods and services. More so, government should create a conducive environment that will enhance business activities and profit making which has the potency to attract foreign direct investment inflows into the region.

Key words: Remittances, Sub-Saharan African, Panel Data & Dynamic Panel Data Model.

Introduction

Remittance is the transfer of fund by an overseas employee to an individual officially or unofficially in his or her home country. World Bank (2011) noted that these movements of funds may be achieved via formal or informal links. Formal links entails transfer that is done via financial institutions and other related but registered financial agents. Esman, Roseline, Leonard & Lydia (2012) maintains that when remittances come through the formal or official channel, it has the potency to impact positively on the financial sector in terms of weight and breath of the sector, thereby guaranteeing effectiveness and efficiency of the sector. The unofficial links entail transfers in the

form of cash or physical goods brought home by these migrants during festive periods or occasional visits to his or her homeland, funds sent via unregistered money agents using local channels among others.

According to the World Bank (2011) over 50% of the remittances accruable to countries in the Sub-Saharan region are mainly done via the unofficial links. As a result of these, informal channels posed a great impediment and challenge in ascertaining the magnitude of remittance that come into Sub-Saharan regions. Research also reveals that in situations where all fund are remitted via the official channels, it is anticipated that there will

still be some problems, like fund diversions and irregularity of documentations (Barajas, Chami, Fullenkamp, & Garg 2010). The true magnitude of remittances both official and unofficial as well as unrecorded flows in Sub-Saharan African economy, is believed to be significantly large.

World Bank report alluded to the fact that world remittances over the last few years have risen gradually to about \$613 billion in 2017, of which \$72 billion was received by Sub-Saharan African (SSA) countries (world Bank 2017). As a result of continuous migration in the world, the earnings generated and transferred by migrants are becoming one of the major sources of international capital inflows especially in third world countries, both in size and in growth rate.

It is on this note that this paper seeks to examine the direction of causality of foreign remittances and economic growth and its impact on the performances of the Sub-Saharan African economy. The paper is divided into five sections, section one is the background to the paper, section reviewed of related works in the area, section three method of empirical analysis and finally, section five is conclusion and policy implication

Foreign Inflows Profile in Sub-Saharan Africa Economy

Over the years, foreign remittances have been compared with other foreign capital inflows in developing countries, particularly Foreign Aid, Foreign Direct Investment (FDI) as shown in the figure below:

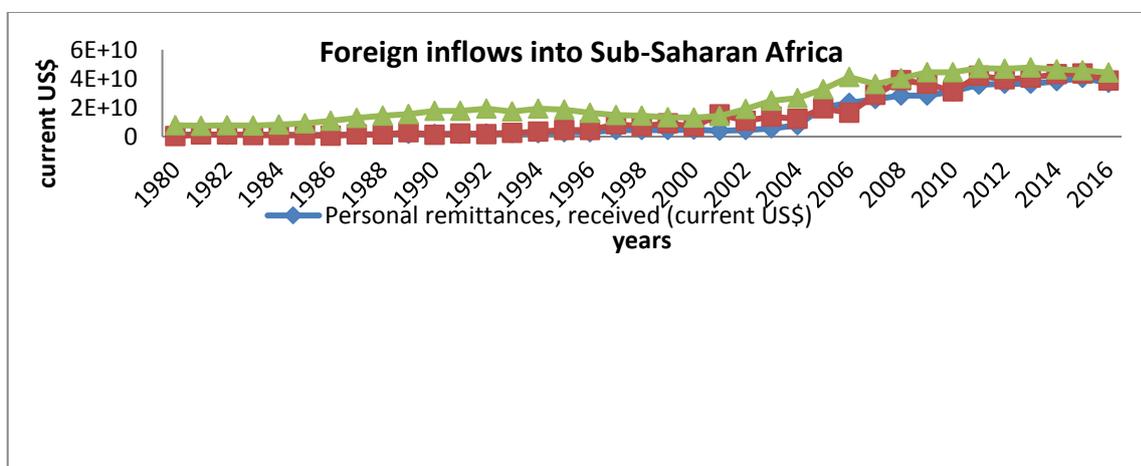


Fig. 1: Foreign inflows into Sun-Saharan African Economy

Source: Author’s Computation from WDI 2016 using Excel

The chart below reveals that in 2007, world remittances were seen to be twice as much as Official Development Assistance (ODA), and that of FDI was about two-third of its inflows to emerging countries. Conversely, remittances have performed poorly relative to FDI & ODA in SSA. However, a close study reveals that, FDI has outweighed remittances for quite an extended time horizon. Despite this observation, remittances remain germane as a source of external finance to the region. From figure 2.1, it was observed that Net official development assistance and official aid has the highest capital inflows for the period under consideration. Foreign direct investment has also increase over time, but has not been stable. From the graph, it was also observed that remittance has been steady and continuous increase of foreign remittances into Sub-Saharan Africa.

Remittance to Sub-Saharan Africa Countries during the global Economic/Financial crisis 2007-2009

The financial crisis that started towards the end of 2007 in the United States of America resulted in devastating economic and social effects on both developed, developing and underdeveloped economies. Remittance inflows to Sub-Saharan Africa were estimated to have declined by a modest 3.7 percent in 2009 (Ratha, Mohapatra, and Silwal 2010). According to Esman et al (2012), the drop in remittance inflows during the financial crisis is linked to 2 factors: (a) inability of migrants to send money home, and (b) loss of job for migrants led to forced return to their home countries.

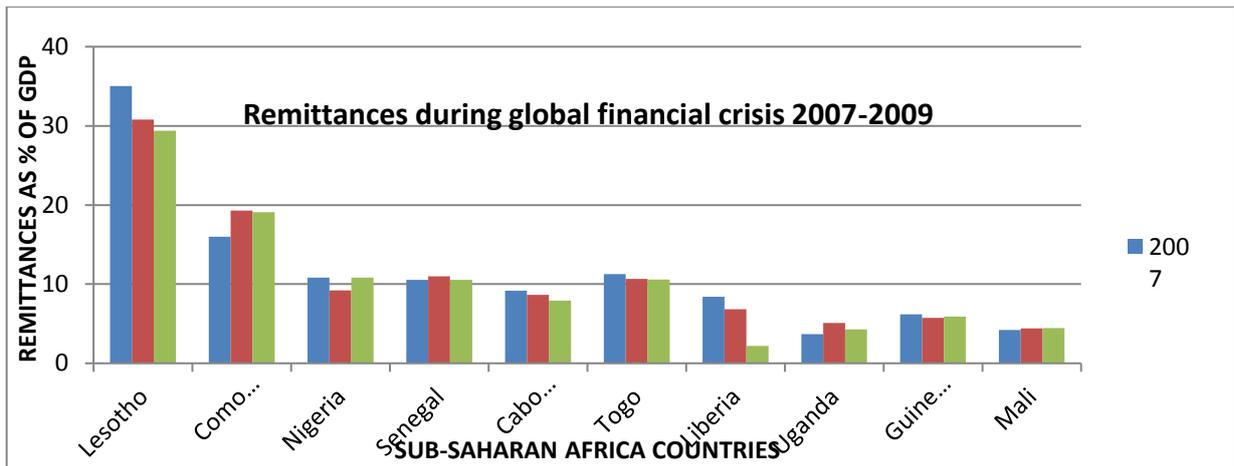


Fig 2: Remittances during global financial crisis 2007-2009

Source: Author's Computation from WDI, 2016

Figure 2.2 therefore shows the flow of remittances as a percentage of GDP to Sub-Saharan Africa countries during the global financial crisis. From the figure, Lesotho is the highest recipient of remittances as a percentage of GDP followed by Comoros, Togo, Senegal, Nigeria, Cape Verde and so on as shown in the figure above. However, during the 2008-2009 global crises, remittance flows to Sub-Saharan Africa remained relatively unchanged, while aid and FDI decreased substantially. Had it not been for remittances, GDP of many Sub-Saharan African countries might have reached below one percentage growth or even contracted. Remittances therefore had proven to be a remarkable source of foreign income for Sub-Saharan Africa countries.

Percentage Share of Regional Remittances Inflows in 2016

The pie chart in figure 2.3 shows the regional remittances in the year 2016. South Asia received the largest remittances inflows of 35% out of the world total remittances. Sub-Saharan Africa is the second largest receiver of remittances in the year 2016. It was observed from the literature that the Education Sector of most Sub-Sahara African countries has increased in size, it has deteriorated in terms of quality and relevance in the society. Also, the cost of living has increased in the region while poverty is at an unbearable level. Due to incessant conflicts, poor government policies and poor infrastructures, the Business Environment in the region has also worsened.

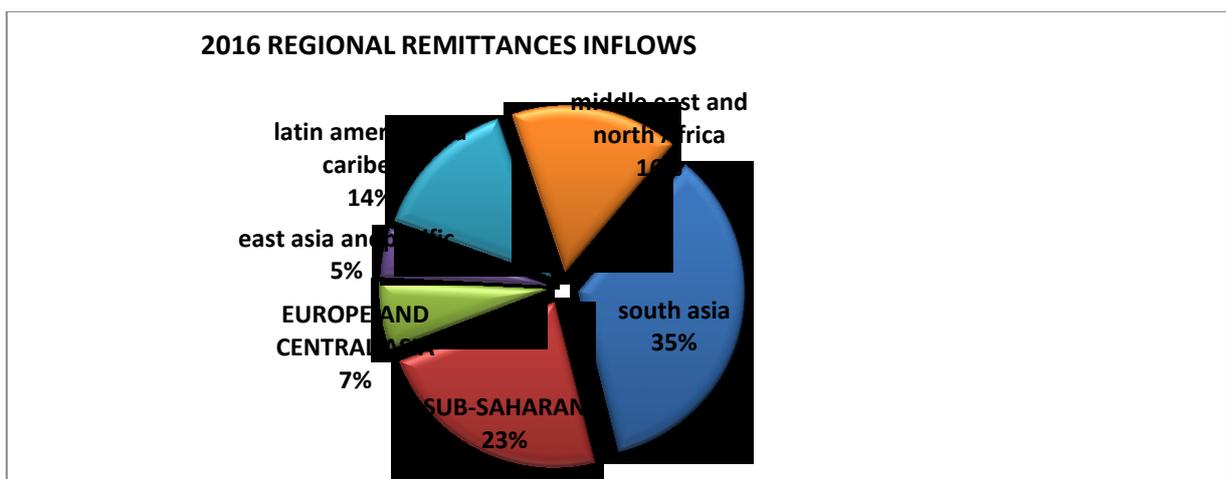


Fig 3: percentage share of Regional Remittance inflows in 2016

Source: Author's Computation from WDI 2016 using Excel

Hence, more and more Sub-Sahara Africans migrate to developed nations for better education, for better standard of living and for better business endeavors. This may explain the increased remittances inflows to Sub-Saharan Africa.

Rank of Remittances to Sub-Saharan African Countries in 2016 (% of GDP)

As a percentage of GDP in 2016, remittances to Gabon ranks highest at 21.5 percent of GDP.

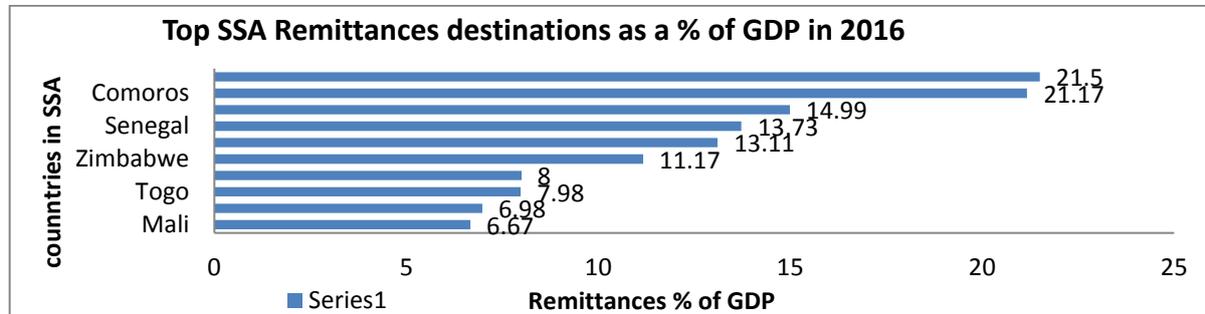


Fig 4 Top SSA Remittances Destination as a % of GDP in 2016

Source: Author’s Computation from WDI, 2016.

Next is Comoros, followed by Lesotho and Senegal with approximately 14 percent of GDP, Capeverd 13.11 percent, Guinea-Bissau and Togo had approximately 8 percent of GDP, while Ghana and Togo had approximately 7 percent of GDP (WDI, 2016)

Literature Review

The remittances and economic growth nexus is faced with severe debate in the literature. The proponents of a positive remittances economic growth link assert that foreign remittances inflows help to stabilize key macroeconomic variables. On the other hand, those against international and remittances argued that remittances inflows reduce hard work and commitment of recipient families thus, affecting economic growth negatively and ultimately the Dutch disease syndrome. For example Iheke (2012) using an error correction mechanism (ECM), on yearly data of 40 years found out that workers’ remittances have a strong, positive and significant impacts on economic growth on the Nigeria economy. Furthermore, Adarkwa (2015) in addendum, also tested the impact of workers remittances on economic growth in four selected West African countries of, Cape Verde, Ghana, Nigeria and Senegal countries after a critical analysis of the relationship between workers remittances and economic growth in these four countries, the results showed that foreign inflows have a positive effect on economic growth in Senegal and Nigeria but had a negative effect on national output in Cape Verde and Ghana.

Oshota and Badejo (2016) examined the relationship between international remittances and economic performance along with labor migration in Pakistan. A yearly time series data was used for

their analysis (from 1975 to 2010). The authors using the multivariate and bivariate cointegration approach showed that international remittances and economic performance in Pakistan are positively related and also the Granger Causality test showed that there is a one way direction of relationship between workers’ remittances and economic growth. The recursive OLS results showed that there is a strong positive relationship between workers’ remittances and consumption and consumption in turn has significant positive effect on economic growth.

Ripon and Rasheda (2018) empirically tested the impact of remittances on reducing volatility of house hold consumption employing a panel data set covering 84 emerging economies from 1980 to 2014. It was found that high migrants’ remittance reduces household consumption volatility in developing countries.

Methodology

In empirically investigating this study we thus present the model of this study following the work of Dietmer and Adela (2016) which was based on the Harris-Todarо migration model and the Horrod-Domar theory of economic growth. With little modification we therefore formulate our model thus:

$$Y_{i,t} = \alpha_0 + \mu_i + \beta_1 X_{i,t} + \varepsilon_{i,t}; \quad \varepsilon_{i,t} \sim N(0, \delta^2 \eta) \quad (1)$$

Where $Y_{i,t}$ = per capita GDP in country i at time t;
 $X_{i,t}$ = Vector of the independent variables including remittance inflows (REM), foreign direct investment (FDI), population growth (POP), Household

consumption expenditure (CONSUM), exchange rate (EXCHR) and broad money supply (M2).

μ_i = Country specific, time invariant effect;

β_i^* = Scalar vector of coefficients of β_1, \dots, β_9

$\epsilon_{i,t}$ = Error term with $E(\epsilon_{i,t}) = 0$ and $\text{var}(\epsilon_{i,t}) = \delta^2 \eta$

Thus with a slight modification we hereby specify the model for the work as thus

$$\text{GDPGRit} = \beta_0 + \beta_1 \text{REMit} + \beta_2 \text{CONSUMit} + \beta_3 \text{FDIit} + \beta_4 \text{POPit} + \beta_5 \text{EXCHRit} + \beta_6 \text{M2it} + \dots \quad (2)$$

A priori expectations

Table 1: A-priori expectations in terms of sign and not their magnitude

Variables	Proxy or definition	Expected sign
<i>GDPGRit</i>	GDP per capita growth (annual %)	$\beta_1 = +/-$ $\beta_2 = +$ $\beta_3 = +$ $\beta_4 = -$ $\beta_5 = +/-$ $\beta_6 = +$
<i>REMit</i>	Remittances received as a % of GDP	
<i>CONSUMit</i>	Household final consumption expenditure as a % of GDP	
<i>FDIit</i>	Foreign direct investment, net inflows (% of GDP)	
<i>POPit</i>	Population ages 15-64 (% of total)	
<i>EXCHRit</i>	Official exchange rate (LCU per US\$, period average)	
<i>M2it</i>	Broad money (% of GDP)	

Source; Authors construction

Estimation Techniques

This research will therefore make use of different econometric techniques in order to obtain a model which yields robust result and best fit for the analysis of the panel data. This includes: the pooled OLS, the static model and the dynamic model. The static model includes the Fixed Effects Model, the Random Effects Model why the Dynamic panel data estimating techniques make use of the Generalized Methods of Moments (GMM). The (GMM) estimator is employed to correct the problem of endogeneity and orthogonality. All the variables in the regression equation are in their natural form, so as to get the direct effect of one variable on the other.

Result and Discussion

Descriptive Statistics

The descriptive statistics considered are mean, standard deviation, maximum, minimum values of the variables, the skewness, the kurtosis and the jarque-bera statistics. The statistics is based on selected 26 Sub-Saharan African countries out of the total of 48 in the region for the time period 1990-2016 due to the unavailability of data on some variables for some of the countries.

The descriptive statistics is used to show the statistical reliability and the nature of the data used so as to ascertain its potency for policy implications.

Table 2: Descriptive Statistics

	GDPGR	REM	CONSUM	FDI	POP	EXCHR	M2
Mean	1.398	3.410	74.468	1.493	52.046	511.460	28.490
Median	1.337	3.090	74.281	1.190	52.007	511.552	26.467
Maximum	5.507	8.040	80.888	6.080	53.898	733.038	43.004
Minimum	-1.415	1.393	68.486	-0.900	50.458	264.691	19.367
Std. Dev.	1.656	1.472	3.340	1.738	1.017	121.581	6.915
Skewness	0.287	1.240	-0.124	0.839	0.122	-0.501	0.627
Kurtosis	2.791	4.632	2.248	3.036	1.858	3.059	2.279
the Jarque-Bera	10.914	257.903	18.331	82.559	39.846	29.552	61.236
Probability	0.004	0.000	0.000	0.000	0.000	0.000	0.000
Sum	981.920	2393.87	52276.7	1048.25	36536.	359044.	20000.
Sum Sq. Dev.	1924.63	1520.90	7823.45	2119.65	726.31	103621	33525.
Observations	702	702	702	702	702	702	702

Source: Author's Computation Using E-views 9

Table 2 therefore presents the summary of descriptive statistics for the variables. Thus from the forgoing, the average values of GDPGR, REM,

CONSUM, EXCHR, FDI, M2 and POP are 1.398747, 3.410077, 74.46835, 1.493234, 52.04611, 511.4600, and 28.49044 respectively.

Their respective maximum values are, 5.507107, 8.040205, 80.88860, 6.080271, 53.89842, 733.385 and 43.00435 respectively. The result also shows that the level of variation is systematically low as shown by the various S.D values of 1.656974, 1.472961, 3.340721, 1.738896, 1.1017894, 121.5811 and 6.915605 respectively.

Therefore, from the result in table 4.1, the probability of the Jarque-Bera statistics of 0.004266 and 0.0000 reveals a normal distribution. Also, the independent variables: Remittance, Consumption, Foreign Direct Investment, Population, Exchange rate and Money Supply all shows that the variables of interest are found to have a skweness and kurtosis matching a normal distribution.

Conclusively, we can say that the standard deviation of each variable is also relatively low (except for Exchange rate), compared to the mean showing a small coefficient of variation. The table also revealed a reasonable range of variation between maximum and minimum values. Kurtosis measures the peakness or flatness of the distributions. This implies that the series for these seven variables does possess flat distributions that are relative to normal. Thus from the forgoing, the Jarque-Bera test statistics as supported by their probability values allows us reject the null hypothesis of no normal distribution of our

variables meaning that the variables are normally distributed.

The study conducts the panel unit root test for the variables because they are time series variables therefore there are need to secure stationarity. Thus based on our result Exchange rate, Foreign Direct Investment and Remittance were found to be stationary at level, while others were not stationary at level but stationary at first difference. However a general level of stationarity at first difference was secured for all variables.

Presentation and Interpretation of the Results of the Static Models (The Fixed Effect and Random Effect Models)

The whole analysis was estimated with GDPGR as the endogenous variable and Remittance, consumption expenditure, foreign direct investment, population growth, official exchange rate and Broad money supply (M2) as the exogenous variables. The null hypothesis of the Hausman test is that the random effects model is appropriate. The results of our computed Hausman test give a probability value of 1.0000; hence, we accept the null hypothesis and conclude that the random effect regression model is efficient. Thus, we choose the Random effect model as our efficient model for interpretation, policy implications and recommendation.

Table 3: The Static Models (Dependent Variable – GDPGR)

Fixed Effect Model				Random Effect Model			
Variable	Coefficients	t-statistics	Prob value	Variable	Coefficients	t-statistics	Prob value
REM	-0.348	-4.209	0.000	REM	-0.348	-750.	0.000
CONSUM	-0.112	-4.052	0.000	CONSUM	-0.112	-294	0.000
FDI	0.395	7.880	0.000	FDI	0.115	726	0.000
POP	-0.532	-3.408	0.000	POP	-0.742	-367.	0.000
EXCHR	0.000	0.178	0.858	EXCHR	0.000	141	0.000
M2	-0.045	-2.402	0.016	M2	-0.889	-341	0.000
C	39.308	4.673	0.000	C	39.308	521	0.000
R-Squared	0.969			R-Squared	0.478		
Adjusted R-Squared	0.967			Adjusted R-Squared	0.469		
F-statistic	684.8			F-statistic	52.89		
Prob (F-statistic)	0.000			Prob (F-statistic)	0.000		
D-W Statistics	2.091			D-W Statistics	2.074		

Source: Author’s Computation Using E-views 9

The static model shows that remittances have a negative effect on the economic growth of Sub-Saharan African Countries as proxy by GDPGR. Showing that remittance inflow into Sub-Saharan Africa negatively impact on the economy of the region. The coefficient reveals that a unit increase in remittance inflows into Sub-Saharan Africa leads to approximately 0.348213unit fall in GDPGR. Also, a negative relationship exists between Household Consumption expenditure (CONSUM) and economic growth (GDPGR). This is contrary to a-priori expectation of positivity in relationship between CONSUM and GDPGR.

Thus a unit increase in CONSUM will lead to a statistically significant decrease of 0.112522 unit decrease in GDPGR.

Additionally, the output shows that foreign direct investment inflows have a positive effect on GDPGR of SSA. This conforms to apriori expectation this positive effect is seen to be statistically significant even at 5% significant level. Therefore a 1unit increase in FDI inflows into Sub-Saharan Africa leads to approximately 0.115697 unit rise in GDPGR.

Population growth (POP) has a negative effect on the economic growth of Sub-Sahara African Countries (GDPGR) and its coefficient is highly significant and passes the test of significance test at the 5% level. Thus a lunit increase in POP will lead to a 0.742236 unit decrease in GDPGR of Sub-Saharan African countries.

The coefficient of determination, of 0.47% of the random effects model, indicates that the explanatory variables (REM, CONSUM, FDI, POP, M2, and EXCHR) accounts for about 47 percent of the systematic variations in the dependent variable (GDPGR). The F-statistic of 52.89161 of the random effects models respectively indicates that the overall regression models are highly significant easily passing the significance test at the 1 percent level of significance as supported by their respectively P-values which is far below 5%. Thus, the null hypothesis of no existing linear relationship between GDPGR and the explanatory variables

can be rejected at the 5 percent level of significance. In addition, the DW Statistics for both models reveals an absence of serial-autocorrelation among the error term.

Presentation and Interpretation of the Results of the Dynamic Model (GMM– Generalized Methods of Moments)

Table 4.3 presents the results of the dynamic panel data model using the GMM SYS estimation technique. The results of the dynamic panel data model show that the one period lagged value of GDPGR positively and significantly affect the growth rate of Sub-Saharan African Countries as proxy by GDPGR. Like both the fixed effect and random effect models, remittances have a negative effect on the GDPGR in Sub-Saharan Africa. Unlike the static models, its coefficient is significant easily passing the significance test at the 5 percent level. A unit increase in remittance inflows into SSA leads to approximately 0.217058 unit decrease in GDPGR in SSA countries.

Table 4: The Dynamic Model-GMM SYS (Dependent Variable – GDPGR)

Variable	Coefficients	t-statistics	Prob value
GDPGR(-1)	0.130	-3.574	0.000
REM	-0.217	-2.907	0.003
CONSUM	-0.052	-2.155	0.031
FDI	0.457	9.294	0.000
EXCHR	0.003	5.304	0.000
POP	-0.113	-0.780	0.435
M2	-0.054	-3.254	0.001
C	11.158	1.420	0.155
R-Squared	0.401		
Adjusted R-Squared	0.352		
J-statistic	668.0		
J-Statistic (Prob)	0.000		
Durbin-Watson stat	2.195		

Source: Author’s Computation using E-views 9

Foreign direct investment (FDI) positively impacts on the growth rate of SSA Countries as proxy by GDPGR. This aligns with the a-priori expectation. Thus a 10 unit increase in foreign direct investment (FDI) will lead to a 45.7761 unit increase in GDPGR in SSA. The effect is large and statistically significant even at the 1 % level of significance.

Finally, in line with the a-priori expectation, official real exchange rate (EXCHR) negatively affects GDPGR. Both the static model and the dynamic model as estimated, presented and analyzed in previous sections are amendable to policy implication. Going by our principal variable remittance inflows (REM), it is obscured that REM has a negative effect on GDPGR both in the static and dynamic model. Therefore inflows of remittance into the region have a negative impact on the GDPGR of the region. This empirical finding is in line with Ratha and Mohapatra (2012)

which alluded to the fact that foreign remittances can have a negative impact on economic growth based on the following reasons (1) remittances can have Dutch-disease effects where they lead to appreciation of the exchange rate and a fall in exports of tradables. (2) Remittances can also reduce the motivation of recipients to work which could adversely affect productivity and output. (3) Some remittance channels could be misused for money laundering and to finance terrorism (Ratha and Mohapatra, (2012) opt cited in Babajide Fowowe Taofik M Ibrahim, (2016)). Additionally, it is also possible that remittances inflow into the region are used basically for altruistic purposes and not channeled into productive activities. Also, families with extra funds from remittances may use these funds to purchase foreign products, hence, increasing importation which in turn leads to a higher exchange rate. It is also possible that increase in this remittance has led to over-dependent on foreign economy and abandonment

of the pursuit of macroeconomic policies, where recipients heavily rely on these transfers, leading to a decrease in labour supply.

In addition, the study has shown that foreign direct investment is positively and significantly related to Economic growth of Sub-Sahara African Nations. Therefore increase in FDI inflows into Sub-Sahara African regions improves the region with its antecedent spill-over effect/benefits. In particular, thus policy towards the increased sustainable increase in economic growth as measured by GDPGR should be driven towards encouraging increased FDI inflows into the country since it is seen to positively and significantly impact on Economic growth.

Another policy implication from other control variables like CONSUM implies that most consumption expenditure by SSA house-holds are imported, hence the level of dependence on foreign product, thus policy measures to boost the productive capacity of the respective nation and also build the faith of the citizens on its product, above all controlled restrictions should be put in place from undue import by SSA nations. From the GMM SYS in specific only population growth is not statistically significant, but all other variables are. Thus SSA countries should put policies in place to increase the level of human capital so that its population growth can impact can have a positive and statistical impact on her economic growth.

Conclusion and Recommendations

The main objective of this study is to investigate the impact of remittances on economic growth in Sub-Saharan Africa. The study covered the period of 1990 to 2016 for 26 Sub-Sahara African countries. The data used were secondary panel data sourced from the World Bank Development Indicator (2016). The natural form of GDPGR per capita which is the dependent variable was used to measure economic growth in Sub-Saharan Africa.

The econometric results of both the static (fixed effects and random effects) and the dynamic panel data models revealed that remittances inflows significantly affect the economy of Sub-Saharan Africa negatively. Other variables that negatively affect economic growth of the region are population growth, household consumption expenditure and broad money supply. Foreign direct investment (FDI) and official exchange rate were found to have positive impacts on Sub-Sahara African economy and their individual effects were also found to be statistically significant. The following policy recommendations were therefore drawn from the findings of this study.

1. For Sub-Saharan Africa to enhance her economy, the various government of the region needs to set up institutions and policies that will encourage and promote foreign direct investment. To encourage foreign direct investment into the region, the governments of Sub-Saharan Africa should (i) create a conducive environment that will enhance business activities and profit making. To do this, maximum security should be put in place in the region. (ii) There should be sincere measures and strong commitment from both the governments and people of the region (SSA) to tackle the issue of incessant crisis (religious, ethnical and political) ravaging the region. This will create peace and stability in the region which is very good for investment and will thus attract foreign direct investment inflows to SSA. (iii) Apart from the exploration, exploitation and exportation of primary products from Sub-Saharan Africa, the region has several lucrative sectors that foreign investors can profit immensely from. International investors are most likely to profit hugely from investing in the manufacturing sector of the region. This is due to the fact that the region has fertile lands, abundant mineral resources and large population which serve as raw materials for manufacturing and large markets for the finished products. Thus, it is the responsibility of the various governments of Sub-Saharan Africa to publicize the various investment opportunities to other regions of the World especially the developed regions (as they have more capital to invest).
2. Remittances inflows were found to negatively affect economic growth in Sub-Saharan Africa. A possible cause may be that remittances inflows to the region are used basically for altruistic purposes and not channeled into productive activities. Also, families with extra funds from remittances may use these funds to purchase foreign products, hence, increasing importation which in turn leads to a higher exchange rate. Sub-Saharan Africans should therefore, invest their extra funds from remittances inflows in production of goods and service and also in the purchase of locally manufactured products as this will enhance the economy of the region. Policies regarding emigration should be put in place to regulate the current inordinate emigration of the region's finest elites to other parts of the world.

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