



Remittances and relative concerns in rural China



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ARTICLE INFO

Article history:

Received 16 June 2015

Received in revised form 18 December 2015

Accepted 18 December 2015

Available online 29 December 2015

JEL classification:

C90

D63

Keywords:

Positional concerns

Remittances

Subjective well-being

ABSTRACT

The paper investigates the impact of remittances on the relative concerns of households in rural China. Using the Rural to Urban Migration in China (RUMiC) dataset we estimate a series of subjective well-being functions to simultaneously explore relative concerns with respect to income and remittances. Our results show that although rural households experience substantial welfare loss due to income comparisons, they gain well-being by comparing their remittances with those received by their reference group. In other words, we find evidence of a “status effect” with respect to income and of a “signal effect” of similar magnitude with respect to remittances. This finding is robust to various specifications, alternative reference group definitions, controls for the endogeneity of remittances and selective migration, as well as the use of migrants’ net contribution to household income.

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1. Introduction

For the past three decades China has been experiencing an enormous movement of workers from rural towards urban areas. Recent estimates show that about 155 million people have left their rural residence to work in urban areas (Cai, Du, & Wang, 2011). Due to *hukou* restrictions, migrants’ spouses and children are often left behind in villages, making remittances a crucial source of income to “compensate” for the migrant’s absence.¹ Estimates suggest that migrants sent about US \$30 billion to rural areas in 2005 (Gong, Kong, Li, & Meng, 2008). Such large cash flows have important and complex effects not only on the welfare of family members left behind, but also on the development, income distribution and welfare of rural villages (e.g., Acosta, Calderon, Fanjzylber, & Lopez, 2008; Howell, 2014). This paper investigates how remittances affect the relative (or positional) concerns of rural households using subjective well-being (SWB hereafter) as a proxy for the experienced utility (Kahneman & Sugden, 2005; Kahneman, Wakker, & Sarin, 1997).

An emerging strand of the literature has put forward the idea that individual subjective welfare does not only depend on the absolute level of income but also on relative concerns, that is, on how individuals compare their income with that of other

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¹ *Hukou* is China’s household registration system. Migrants from rural areas possess a rural *hukou* and they are typically unable to obtain an urban *hukou*. However, they are allowed to reside in a city as long as they are employed and can remain up to six months after unemployment.

relevant people (Clark, Frijters, & Shields, 2008; Senik, 2008). The effect of relative concerns has been analyzed using SWB data from existing surveys (e.g., Clark et al., 2008; Ferrer-i-Carbonell, 2005) or by collecting experimental data (e.g., Akay, Martinsson, & Medhin, 2011; Carlsson, Johansson-Stenman, & Martinsson, 2007; Solnick & Hemenway, 1998).² Both approaches suggest that the relative income substantially affects individuals' welfare. In the non-experimental approach, the role of relative concerns is captured by introducing the average income of individuals in the relevant reference group as an additional control variable in SWB regressions conditional on individuals' absolute income and other characteristics. Evidence from developed countries suggests that the reference group's mean income negatively affects well-being. Such a result is compatible with the presence of a status effect reflecting feelings such as envy (Clark et al., 2008; Luttmer, 2005).

Yet, empirical studies from less developed or transition countries report small, sometimes positive impact from relative concerns (see for South Africa: Bookwalter & Dalenberg, 2010; Kingdon & Knight, 2007; Ethiopia: Akay & Martinsson, 2011; Akay et al., 2011; China: Akay, Bargain, & Zimmermann, 2012; Appleton & Song, 2008; Knight & Gunatilaka, 2010; Knight, Song, & Gunatilaka, 2009; Poland: Senik, 2005, 2008; Russia: Ravallion & Lokshin, 2000; Senik, 2004).³ One possible explanation of the positive effect is the presence of altruistic feelings towards other members with which the individual interacts, e.g., in the local community. Another explanation is that the incomes of other people act like a *signal effect* (or a “demonstration effect” or “tunnel effect” as coined by Hirschman & Rothschild, 1973) for the individual's own income potential and prospects, thus resulting in positive feelings (Senik, 2005).

By investigating the effect of the remittances received by those in the reference group (*relative remittances*) on individuals' SWB, we build upon and bring together the literature strands on relative concerns and remittances. The remittances literature focuses mainly on the absolute effect of remittances on well-being, particularly in relation to income inequality and poverty (see e.g., Acosta et al., 2008; Akay, Giuliatti, Robalino, & Zimmermann, 2014). Remittances are expected to be positively associated with the well-being of individuals left behind since they represent an additional (or substitutive) income source. In addition, however, remittances may change the income distribution and the relative income position of households within the village. That is, remittances might change the reference group's income position, thereby triggering a “status” or a “signal” effect to the extent that individuals might also be concerned with the remittances received by other households.

Our analysis, based on the Rural to Urban Migration in China (RUMiC) dataset, provides novel and striking results on rural households' relative concerns with respect to both rural income and remittances. The first result is that the definition of income matters when identifying relative concerns in a regression framework. A measure of the overall household income alone might not be able to identify the true effect. Second, we show that while a status effect among rural households exists, the magnitude and significance of the estimated effect depends on the model specification. Third, by decomposing the overall household income into the part pertaining to remittances and the part pertaining to activities carried out in the village (henceforth: rural income), we find that rural households experience both status and signal effects at the same time. In particular, households exhibit a strong status effect with respect to rural income and an equally strong signal effect with respect to remittances. This result suggests that these two effects may be neglected when analyzing relative concerns using aggregate income measures. Fourth, results are very stable across heterogeneous groups and overall insensitive to the definition of the reference group. Last but not least, we take into account the role of selectivity into migration by both estimating selection equations and calculating the counterfactual income and expenditure distributions pertaining to migrants.

The paper is organized as follows: Section 2 provides information about the data and descriptive statistics. Section 3 outlines the econometric approach. Sections 4 and 5 report the results from our baseline and additional models, respectively. Section 6 concludes.

2. Data

2.1. The RUMiC dataset

We employ data from the Longitudinal Survey on Rural to Urban Migration in China (RUMiC), which consists of three distinct surveys: the Urban Household Survey (UHS), the Rural Household Survey (RHS), and the Migrant Household Survey (MHS).⁴ Our paper is based on the first wave of the RHS. Data were collected at the beginning of 2008, with most information (e.g., migration, income) referring to 2007.⁵ The RHS covers the 9 largest migrant sending provinces of China (Anhui, Chongqing, Guangdong, Hebei, Henan, Hubei, Jiangsu, Sichuan, and Zhejiang), and 82 counties (counties are the administrative level above villages and below provinces), as depicted in Fig. 2. The survey was conducted using random samples from the household income and expenditure surveys carried out in rural villages by the National Bureau of Statistics of China, thus constituting a representative sample for these provinces.

The dataset has rich information about demographic and socio-economic characteristics of household members, including questions on physical and mental health, life events, and social networks. We supplement the main dataset with two ancillary modules collected in parallel to RUMiC: the *income-expenditure household* module, which contains information on income,

² The second approach to investigate the positional concerns is based on tailored survey experiments constructed to explicitly identify the relative concerns. This method allows for identifying positional concerns both for income and consumption of specific goods, such as cars and holidays (see, e.g., Akay et al., 2011, 2013; Alpizar, Carlsson, & Johansson-Stenman, 2005; Carlsson et al., 2007; Solnick & Hemenway, 1998, 2007).

³ See also the comprehensive survey by Clark and Senik (2010).

⁴ For an extensive description of RUMiC, see Akgüç, Giuliatti, and Zimmermann (2014).

⁵ The global economic crisis has affected both migration and return decisions. At the end of 2008, around 23 million migrants returned to their rural villages (National Bureau of Statistics of China, 2010, www.data.stats.gov.cn). Hence, the data used in our paper refer to a time period before the crisis. However, we have also checked the robustness of our results by using the waves collected in 2009 and 2010.

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