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Extending a Lifeline or Cutting Losses? The Effects of Conflict on Household Receipts of Remittances in Pakistan

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Summary. — I examine the causal effects of long-term exposure to conflict, measured at the micro level, on households' receipt of remittances, among households residing in areas affected by the 2010 floods in Pakistan. Using a dataset of 7802 households, representative of all flood-affected areas of Pakistan in 2010, I employ IV estimation to overcome the endogeneity of conflict exposure and remittance receipts, and control for a range of confounding factors. I find that, contrary to the literature from country-level case studies, long-term exposure to conflict reduces households' likelihood of receiving any remittances at all, as well as the average amounts of remittances received. However for households in the lowest food consumption expenditure quintile, conflict has a positive effect on the likelihood of remittance receipts, which provides evidence for the existence of heterogeneous effects as well as a significant micro–macro gap in understanding the causal effects of conflict on remittance receipts.
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Key words — remittances, conflict, South Asia, Pakistan

1. INTRODUCTION

In recent years there has been a sharpening focus on the role and potential of remittances in spurring growth, promoting development and establishing new terms of North-South, and also South-South economic engagement. Estimated to have surpassed 250 million in 2015, the growing global migrant worker population is responsible for remittance flows to developing countries as high as US$ 436 billion in 2014 (World Bank, 2015). For several countries, including Pakistan, international remittance receipts far exceed inflows of foreign exchange from other sources such as Overseas Development Assistance (ODA) and Foreign Direct Investment (FDI; *Source:* Ahmed & Zarzoso, 2013).

Remittance receipts are especially crucial for Fragile and Conflict Affected States (FCAS). While remittances amount to less than a third of FDI inflows globally, in FCAS countries they are 1.5 times the value of incoming FDI (World Bank, 2016). While remittances account for 0.8% of global GNI, they amount to, on average, 4.0% of the GNI in all FCAS, and are as high as over 20% in Liberia, Haiti, and the Gambia.

While even the proponents of remittances caution against viewing them as a panacea or as a replacement for development assistance and aid programs (Ratha, 2007; Savage & Harvey, 2007), in FCAS remittances can be a very effective complement to these flows due to several reasons. Remittances flow directly from migrant workers to recipient households without incurring the heavy administrative and bureaucratic costs that state-run cash transfer programs do (even as the logistical costs of transferring and receiving money may be significant). Remittance receipts, unlike FDI flows, are also often counter-cyclical (Ahmed, 2012); they tend to increase in times of economic crisis, and thus help retain foreign exchange reserves to secure financial stability at the macroeconomic level. At the household level, remittances can respond to idiosyncratic or covariate shocks, including financial, humanitarian and political crises; affected households often draw on outside assistance when the local means of livelihood and survival are hit (Yang, 2005). Further, remittances are used by households not only for financing consumption, but also for investment purposes. Such investments from external receipts into the local economy can improve productivity, and accelerate economic activity, beyond its multiplier effects on the local economy from increases in consumption demand financed by remittance receipts (Ahmed, 2000; Lindley, 2007; Maimbo, 2006).

The causal effects of violent conflict on the receipt of remittances, particularly at the household level, remain unclear. Violent conflict can create a set of conditions which may simultaneously accentuate the need for remittances and encumber its reach. Existing studies on remittances in conflict-affected countries have focused on national data and have found that the onset of conflict is accompanied by higher receipts of remittances in countries such as Somalia, Sri Lanka (Fagen and Bump, 2007), Pakistan (Anwar & Mughal, 2015) and Nepal (Seddon, 2005). Some studies have also found that remittances do indeed help households weather economic hardship in conflict-affected areas, by extending a "lifeline" to those in dire need and preventing them from adopting costly coping strategies.

Yet, the context of a long-term term conflict can lead to heightened risk for investments in the area, as well as raise concerns over the security of life and property. These factors may dampen investment-focused remittances and also lead many remitters to reconsider their longerterm economic interest in conflict-affected communities. Owing to these considerations, and logistical impediments to financial transactions, conflict may in fact reduce household access to remittances, even as it accentuates economic hardship and the need for remittances in the first instance. Finally, when diaspora communities fund armed groups back home, remittances can initiate or prolong violence, making the relationship between

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conflict and remittances complex in terms of identifying causal links (Ballentine & Nitzschke, 2003; Collier, 2000; Horst, 2006; Orjuela, 2008). The relationship between conflict and remittances is therefore not direct or simple and can potentially vary across a range of household and community-level characteristics.

While existing studies have shown that exposure to conflict (and other shocks, more broadly) can be positively or negatively correlated with remittances, there is no microeconomic evidence on the causal effects of conflict on remittances. This paper specifically examines:

i. How does exposure to violent conflict affect household-level remittance receipts?
ii. Do such effects vary across groups of households, and what factors explain such differences?

I situate the above questions in the context of the massive 2010 floods in Pakistan that covered conflict-affected and non-conflict areas. While not representative of Pakistan as a whole, the flood-affected areas are a valuable setting to examine this causal relationship because (a) the post-flood context implies high covariate household distress and the need for external help through remittances, and (b) several areas of Pakistan that were flooded in 2010 had also been exposed to growing and varying degrees of violent conflict over the preceding decade, allowing sufficient variation to examine causal effects. I use a large household dataset representative of all the flood-affected areas of Pakistan in 2010 and develop sub-district-level indices of violent conflict exposure over the 2001–10 period. To address the endogeneity issue between conflict exposure and remittance receipts, I exploit variations in community-level distances to the Afghan border, a correlate of proximity to the Taliban's infiltration into Pakistan following the War on Terror, and thereafter of areas of militant operation and eventually confrontation with the Pakistani state to instrument conflict exposure. I also control for a range of potentially confounding factors. This empirical strategy allows me to estimate the causal relationship between violent conflict and remittance receipts, and to examine underlying heterogeneities.

I find that overall, conflict reduces the likelihood of households receiving any remittances, as well as the value of remittances. Unlike the macro-level analysis that finds a positive association between conflict and remittance receipts (Anwar & Mughal, 2015), this paper uses a microeconomic lens to determine causal effects and finds the opposite effect, indicating a significant macro–micro gap. Significant heterogeneities underlie these results: conflict in fact increases the likelihood of households in the lowest quintile of monthly per capita food consumption expenditure receiving any remittance. Attempting to explore these divergent effects across households further, I posit that the divergent effects across food expenditure groups provides suggestive evidence for the opposite effects of conflict on remittances motivated by altruism and the need to supplement recipient household income on the one hand, and by investment on the other—assuming that households in lower food expenditure quintiles are more likely to use transfers for consumption, while those in higher quintiles are more likely to use them to make investments. The assumption of variation in relative spending preferences *viz.* consumption and investment items by income groups is further strengthened by an analysis of actual expenditures made by households out of flood relief cash transfers provided by the Government of Pakistan. Cash transfer recipients in lower food expenditure quintiles are less likely to invest than to consume the amounts received, compared to those in higher quintiles. If this characterization holds for spending preferences for of other transfers, remittances in particular, the opposite effects of conflict on the likelihood of the poorest and the richer households receiving remittances may be because altruistic remittances respond positively to conflict, while those motivated by investment respond negatively.

The rest of this paper is organized as follows: Section 2 provides an overview of the literature on conflict and remittances, highlighting crucial gaps for the present and any future research to address. Section 3 discusses the history of violent conflict in Pakistan in the decade before the 2010 floods, as well as the context of remittances in Pakistan, and the sources of data used. Section 4 outlines the Instrumental Variables estimation strategy, and discusses potential threats and the means of mitigating against them. Results are presented in Section 5. Section 6 discusses the findings in relation to the existing literature and concludes with notes for policy.

2. LITERATURE REVIEW

The New Economics of Labour Migration (NELM) situates the decision to migrate (and eventually to remit money back) within the household, rather than with the individual. It posits that migration is undertaken by particular members of a household as a strategy with three underlying alternate hypotheses (i) relative deprivation: migration is undertaken by the relatively poor to diversify and increase household income sources by tapping into distant income sources, (ii) investment: migration is motivated by the need to increase household investments by channeling remittances in agriculture or enterprise, (iii) insurance: migration is motivated by the need insure against a range of financial and other risks (Stark, 1980; Stark & Bloom, 1985; Lucas and Stark, 1985).

Empirical studies have found evidence for remittance receipts being spent on multiple uses; for consumption items such as food, clothing, and health expenses (Connell & Brown, 2005; IOM, 2003; Meyers, 1998; Savage & Harvey, 2007) and social obligations (Carling, Erdal, & Horst, 2012); as well as on investments in real estate (Adams & Cuecuecha, 2010; Ballard, 2005), enterprises (Amuedo-Dorantes & Pozo, 2006b; Betts, Bloom, Kaplan, & Omata, 2014; Campbell & Kakusu, 2006; Carling *et al.*, 2012; Horst, 2006; McCormick & Wahba, 2002), education (Adams & Cuecuecha, 2010), agriculture (Ballard, 2005), and a combination (Ahmed & Zarzoso, 2013). In reality it is however hard to isolate motives as they may often be overlapping, and because standard socioeconomic surveys typically do not include details on remittance use.

Remittances are sensitive and respond to changes in the external environment, to factors including but not limited to conflict, both positively and negatively. Spatafora (2005) shows that remittance receipts increased considerably in response to financial crises in Indonesia in 1997, Ecuador in 1999 and Argentina in 2001. Similarly, studies have found that remittance receipts at the country level increased in the aftermath of natural disasters. Using a cross-country dataset Yang (2005) finds that remittances increase following hurricane events. Yang and Choi (2005) find that remittances were able to partially offset weather shock-induced losses in the Philippines. Other studies have also found that remittances increase in response to particular natural disaster events in several countries including the Dominican Republic and Haiti (World Bank, 2006), Bangladesh (Clay & Benson, 2006; World Bank, 2006), Jamaica (Clarke & Wallsten, 2004), Guatemala (Gellert, 2006) and Grenada (World Bank, 2005). In all

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