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Jakhongir Kakhkharov

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Abstract

Transforming remittances and savings of labor migrants into a source of financing for entrepreneurship as well as other development projects is the focus of the migration policies of many governments in migrant sending countries. Unilateral transfers from overseas play an increasingly important role globally in the economies of the majority of developing countries. Remittances and savings of labor migrants have facilitated the development of Uzbekistan’s financial sector, by prompting the development of sophisticated money transfer operators. However, the extent of the impact of these flows on financing needs of business enterprises is still unclear.

The aim of this research is to analyze the impact of remittances from labor migrants on easing the financial constraints of small businesses in Uzbekistan. In other words, the research sheds light on the significance of remittances and savings of labor migrants for entrepreneurship. As such, this research has important policy implications. Small businesses are believed to be crucial for job creation and economic growth. The results of this paper indicate that the link between labor migration and business investment in Uzbekistan is rather equivocal. Data on the use of remittances from relatively larger scale surveys show that a small number of recipient households invest in entrepreneurship. This may be due to the fact that remittances Uzbek households receive are small and mainly used to address immediate consumption needs.

Key words: remittances, labour migration, investments, Uzbekistan

JEL Codes: F24, O15, E22
1. Introduction

Transforming remittances and savings of labor migrants into a source of financing for entrepreneurship as well as other development projects is the focus of the migration policies of many governments in migrant sending countries. Unilateral transfers from overseas play an increasingly important role globally in the economies of the majority of developing countries. Remittances and savings of labor migrants have facilitated the development of Uzbekistan’s financial sector, by prompting the development of sophisticated money transfer operators. However, the extent of the impact of these flows on financing needs of business enterprises is still unclear.

The aim of this research is to analyze the impact of remittances from labor migrants on easing the financial constraints of small businesses in Uzbekistan. In other words, the research sheds light on the significance of remittances and savings of labor migrants for entrepreneurship. As such, this research has important policy implications. Small businesses are believed to be crucial for job creation and economic growth. The results of this paper indicate that the link between labor migration and business investment in Uzbekistan is rather equivocal. Data on the use of remittances from relatively larger scale surveys show that a small number of recipient households invest in entrepreneurship. This may be due to the fact that remittances Uzbek households receive are small and mainly used to address immediate consumption needs. However, as the size of remittance income increases households exhibit greater desire to invest. Remittances, therefore, have the potential to become a vital investment source for MSMEs (Micro Small and Medium Enterprises) if augmented with a bank credit and/or an increase in the amount of remittances. Moreover, even if households do not invest remittances in entrepreneurship, Uzbekistan’s financial sector appears to be benefiting from this inflow of funds. A small part of remittances may even be turning into bank loans that the private enterprises need to grow. In addition, some small scale surveys hint at the possibility that the effect of remittances on MSME investment could be much more noteworthy than depicted by larger scale surveys. Further research into investment behavior of non-remitting migrants and their household could shed more light on this issue. Ultimately, analysis of household survey data indicate that to increase positive effect of remittances, policy makers should consider strategies to reform the banking
sector to boost its role in financing micro and small business, encourage investment of remittances into MSMEs by developing the education sector focused on nurturing business skills among migrants, and improve business environment. The rest of the paper is organized as follows. Section 2 reviews the literature on the topic. Section 3 briefly describes the setting for remittances in Uzbekistan. Section 4 introduces the data and methodology of the paper. Section 5 presents the analysis and interpretation of the empirical observations, and section 6 draws conclusions and discusses policy implications.

2. Literature Review

Small businesses face significant financial constraints even in the best of circumstances. Evidence suggests that, even in the case of mature economies, the formation and survival of small firms often depends on relaxation of capital constraints by injection of personal funds of owners (Holtz-Eakin, Joulfaian, and Rosen 1994a, Holtz-Eakin, Joulfaian, and Rosen 1994b, Blanchflower and Oswald 1998). Entrepreneurs in developing countries confront much less efficient credit markets, and available evidence from World Bank Enterprise Surveys (www.enterprisesurveys.org) indicates that access to credit is a major concern for about a third of surveyed enterprises in the developing world.

The New Economics of Labour Migration (NELM), developed by Stark (1991) and others, links remittance behaviour to migration decision. According to NELM, migration decisions are a collective choice or a family strategy which aims not only to maximize income, but also to minimize risks, diversify income earnings, and relax financial constraints through remittances. Thus, the NELM gives an important insight into the migration decision by linking labour migration decisions with public policy and capital market failures in the labour source countries. In making the decision on migration, households design their own strategy to cope with the absence of appropriate credit, insurance instruments and public protection. Remittances from a family member abroad provide an additional source of funding; insurance in case the main source of family income falters, and financial protection in case of rainy days.

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As such, migration can be viewed as a result of risk aversion on the part of a household that has insufficient income. In general, the NELM proved to be an innovative, realistic, useful and widely applied in recent migration studies.

Critics of the NELM point out at its shortcomings associated with its strong assumptions of rationality and negligence of the role of informal institutions (community, extended family, informal associations and etc.) as noneconomic determinants of human motivation and behaviour (Aslan 2011, Hagen-Zanker 2010). In the context of Uzbekistan and Central Asia, these informal institutions and social networks seem to play a significant role in migration and remittance decisions. Amuedo-Dorantes and Pozo (2006) go further in measuring the insurance motive by distinguishing between self and family insurance and altruism. They do so by looking at what remittances are used for. If remittances respond to income risks in the host economy and are used for consumption they are sent to the family as part of a co-insurance agreement. If they are used for asset accumulation instead, the family acts as an investor for the migrant, so remittances are sent for self-insurance. In essence they are like savings. The authors’ findings show that those migrants with greater income risk remit more and that different types of migrants use different insurance methods.

Rapoport and Docquier (2006) in their thorough review of literature on the economics of migration and remittances note that most of the empirical literature on migration and entrepreneurship concentrates on migrants who return to their home countries. One reason for this may simply be that the return migration channel is quantitatively more important than the remittances channel. Another reason has to do with data constraints: while the data sets on returned migrants are relatively rich, household surveys generally provide no information on the wealth distribution prior to self-employment, and do not always properly track the exact uses of remittances. Moreover, Rapoport and Docquier (2006) also argue that while the relative importance of self-employment is a distinctive feature of the labour force of most developing countries, evidence suggests that the credit market only plays a minor role in financing investments in small businesses. For example, Mesnard (2004) indicates that during the 1980s, 87% of the entrepreneurial projects started by Tunisian returned migrants were financed in full through accumulated savings while abroad, with only 13% receiving complementary financing from governmental programs, and none
relying on private bank credits. Similarly, Dustmann and Kirchkamp (2002) show that only 1.2% of Turkish return migrants who were self-employed in 1988 resorted to bank credits as a major source of financing their start-up costs. In such a context, it is clear that for many prospective entrepreneurs in developing countries, temporary migration is often the only means of developing their own enterprises.

Woodruff and Zenteno (2007), using econometric methods, estimated the impact of access to remittances on capital investment in micro-enterprises in Mexico. The analysis indicates that remittances are responsible for more than one-quarter of the capital invested in micro-enterprises throughout urban Mexico. The authors estimate that in ten states with the highest rates of migration to the United States, more than 40 per cent of the capital invested in microenterprises is associated with remittances. Brown (1997) researches another facet of remittances and investment in entrepreneurship, and finds that those migrants that intend to return home send more remittances, for example as investment in their assets at home. McCormick and Wahba (2001), using probit model, document that the amount and duration of overseas stay positively influence the probability of becoming an entrepreneur amongst literate Egyptian migrants. Amongst illiterate migrants savings alone increase the probability of engagement in entrepreneurship. This result suggests that skill acquisition is more relevant for subsequent entrepreneurship activity upon return than accumulating funds. Considering the link between remittances and entrepreneurship in the Philippines, Reyes et al. (2013) find that the factors inhibiting the likelihood that recipients of remittances engage in entrepreneurial activity include number of dependents, food expenditure, level of wages and salaries received by the household, and construction of shelter. There are also facilitating factors such as age, number of households with job, and specific occupation of household members. Highly educated migrants also tend to have higher entrepreneurial income compared to less educated ones. Furthermore, households with household members who are professionals or technicians are likely to have higher income from entrepreneurial activity.

It should be noted in this context that in Uzbekistan, labor migration is seasonal with a clear intention of returning home after a seasonal period of labor migration, which may be a facilitating factor for investment of remittances into MSMEs. However, in many cases these migrants will have to rely on their own funds because, as noted by
Ruziev and Midmore (2012), a large group of individuals in Uzbekistan is considered as ‘unbankable’ by the formal financial system because of high transaction costs usually associated with the typically small size of loans, higher perceived risks, low profit margins, and most importantly lack of traditional collateral. This could be one of the important reasons why remittances do not contribute to development of the Uzbekistan’s economy significantly. Opening of small retail outlets, buying an apartment and renting it out, opening small internet cafes, restaurants, and buying cars and using them as taxi cabs are the usual limits of investment for Uzbek migrants starting up their own MSMEs (Marat 2009). As a matter of fact, in another Central Asian country – Tajikistan, Clément (2011), using propensity score matching methods, fails to find any evidence of positive impact of remittances on investment expenditures of households.

Another reason why many Uzbek migrants fail to become successful entrepreneurs could be due to the fact that the majority of them end up wasting their hard earned income in lavish cultural ceremonies, such as weddings (Irnazarov 2015). Many respondents to a small-scale survey conducted in Moscow by Juraev (2012) and UNDP sponsored surveys implemented in Uzbekistan (UNDP 2008) also point out that many of Uzbek workers overseas joined the ranks of labor migrants in order accumulate enough funds to arrange for weddings.

Finally, there is a strand of literature on effects of migration and remittances which documents the decrease in labor supply and increase in leisure among migrant sending or remittance receiving households (Chami, Jahjah, and Fullenkamp 2003, Ruiz and Vargas-Silva 2009), which impacts negatively investment in entrepreneurship. Nevertheless, Yang (2008) reports that income effects matter most - favorable exchange rate shocks in the Philippines, for instance, raised hours worked in self-employment, and led to greater entry into relatively capital-intensive enterprises by migrants' origin households in the end of 1990s.

3. Setting for Remittances in Uzbekistan

With a population of about 30 million people, Uzbekistan is the most populous country in Central Asia and one of the leading sources of migrants in the post-Soviet area. Russia is the main destination for the majority of Uzbek labour migrants.
According to Russia’s Federal Migration Service (FMS), the number of Uzbek labourers in Russia peaked in 2014 at about 2.7 million, but because of the fall in oil prices and the devaluation of the Russian rouble, the number had decreased to about 1.8 million by 2016. Despite the slump, in the Commonwealth of Independent States (CIS), Uzbekistan is the top recipient of remittances sent from Russia (Central Bank of Russia 2014a, b, 2015). Most Uzbek labourers migrate because of limited job opportunities in Uzbekistan and a large wage differential between that available at home and in destination countries, so the number of families that depend on remittances is large. From 2006 until the 2014 economic downturn in Russia, the recorded remittances from Russia to Uzbekistan increased at double-digit rates and exceeded 6.6 billion US dollars (approximately 12% of Uzbekistan’s GDP) in 2013 (Central Bank of Russia 2014a). Part of this increase in recorded remittances was due to decreased transfer fees, and another part was due to an increase in the number of labour migrants (Kakhkharov, Akimov, and Rohde 2017).

Notwithstanding this spectacular growth in migration and remittances, Central Asia—particularly Uzbekistan—remain little explored in terms of remittances’ causal impact on household investment in small business. Brück et al. (2014) argue that, despite its interesting experience of transition and development, Central Asia is understudied because of the lack of household-level datasets. This paper bridges this gap by using unique household-level survey data collected by the German Agency for International Development (GIZ) and the World Bank.

4. Data and Methodology

Data. This research uses data from a survey of the jobs, skills, and migration of citizens in Uzbekistan: “Uzbekistan Jobs, Skills, and Migration Survey” to explore the link between remittances and investment. The survey was developed and conducted jointly by the German Society for International Cooperation (GIZ) and the World Bank in 2013-2014. The survey collected comprehensive information not typically captured by traditional household surveys and is representative at the national, regional (Oblast), and urban/rural levels. Two distinct instruments are employed in the survey: a core questionnaire and a skills questionnaire. The sample size of the core questionnaire is 1,500 households with a total of 8,622 individuals. One individual per
household was randomly selected to partake in the skills questionnaire. The second skills questionnaire sample thus consisted of 1,500 individuals.

1. Core questionnaire. The core questionnaire contains modules focusing on the following topics: education, employment, migration, health expenditure, remittances, government transfers, financial services, subjective poverty, housing conditions, and household expenditures.

2. Skills questionnaire. The skills questionnaire contains detailed modules on labor and work expectations, migration and preparation for migration, language skills, and technical skill training.

In addition, the paper also uses the secondary data from small scale surveys conducted by Juraev (2012) and UNDP (2008).

**Methodology.** In this paper, both quantitative and qualitative research methods along with deductive reasoning are used to address the research objective – the inquiry into the impact of labor migration and remittances on entrepreneurship. The paper investigates the effect of remittances on entrepreneurship in Uzbekistan by examining investment decisions of recipients and comparing households in receipt of remittances from abroad with non-recipient ones. Analysis of statistic data from the survey was used in order to shed light on this issue.

**5. Analysis and interpretation**

Access to finance remains one of the most daunting obstacles to the growth of MSMEs in the developing world. According to the World Bank’s Enterprise Surveys, most businesses in surveyed countries list the problem as one of the three main obstacles to growth. EBRD maintains that “limited access to finance is a particularly acute problem for firms younger than five years” (EBRD 2015). Uzbekistan’s situation with access to finance is an interesting case: the country ranked the lowest among transition countries in terms of percentage of firms using banks to finance investments according to Business Environment and Enterprise Performance Survey (BEEPS) IV conducted in 2008-2009. As Figure 1 illustrates, just fewer than 10 per cent of firms reported having a loan or a line of credit in that period’s BEEPS. However, in the next wave of BEEPS (BEEPS V) conducted in 2013-14, this share
increased to more than 25 per cent (EBRD 2015). Incidentally, remittances to Uzbekistan during the period between BEEPS IV and V also increased substantially. According to the data of the Central Bank of Russia (2015), remittances from Russia to Uzbekistan via money transfer operators (MTOs), reached $5.581 billion in 2014, whereas in 2009 this flow stood at just over $2 billion. Estimates show that if remittances from other countries are taken into account, the total income of the Uzbek economy from labor migration may have reached $7-8 billion in 2014, which is equal to almost half of the exports, and several times as much as the volume of direct foreign investments in the country in 2014. The share of remittances in GDP also increased substantially during this period. This increase in the proportion of firms using loans is in line with the empirical research results showing the positive impact of remittances on financial development and credit creation (Kakhkharov 2014, Aggarwal, Demirgüç-Kunt, and Pería 2011).

**Figure 1. Remittances from Russia and firms borrowing from banks to finance working capital and investment**
Source: World Bank, Enterprise Surveys (enterprisesurveys.org), Central Bank of Russia data on bilateral remittances, estimations of remittances from Russia for 2002 and 2003 from Shelburne and Palacin (2008), and calculations of the author.

However, in the micro level, according to subjective self-assessment of respondents in GIZ/World Bank survey, only a small percentage of households receiving remittances invest in a small business. As depicted in Figure 2, 449 households out of 1500 admitted that they receive remittances. Responding to the question “what do you use remittances for?”, only 7.4 per cent of households in receipt of remittances mentioned investments in an enterprise or farm.

![Figure 2. The number of remittance receiving households investing and not investing in an enterprise or farm](image)

These results are broadly in line with the outcomes of the survey conducted by the research center “Tahlil” and funded by UNDP. As a matter of fact, only 6.4 per cent of respondents indicated that the main aim of their temporary migration was to earn money for start-up capital for their own business (UNDP 2008). It is notable that 11 per cent of respondents to the small scale survey of 150 labor migrants in Moscow conducted by Juraev (2012) declared that they were considering to save money to start their entrepreneurship activities back home. This discrepancy in the results of
GIZ/World Bank and UNDP surveys on the one hand and Juraev’s survey on the other hand may be due to the fact that the survey conducted in Moscow captured those migrants who do not remit (37.8 per cent in Juraev’s survey). As a matter of fact, these migrants may save up more funds and invest in a business upon return.

The results of the three surveys discussed above contrast with the results of interviews conducted by Juraev in Olot district of Bukhara region of Uzbekistan (Juraev 2012), albeit with a limited number of households - 30. The interviews with household members indicate that 20 per cent of households receiving remittances from Russia invested in small business or entrepreneurship. Furthermore, 21 respondents (71 per cent) reported that remittances were used to buy cattle – a type of agricultural investment. One of the reasons for this disparity in results, in addition to the small sample size, could be the fact that households systematically underreport remittances in household surveys (Shonkwiler, Grigorian, and Melkonyan 2011). In Uzbekistan, this underreporting may also be quite common given the fact that respondents, being afraid of unexpected repercussions, could be reluctant to divulge precise data about their income. One way to test this hypothesis, which is outside the scope of this paper, could be to compare expenditures of households receiving and not receiving remittances with their reported income, similar to the one done by Abdulloev, Gang, and Landon-Lane (2012) for the case of Tajikistan. Therefore, it is possible that respondents in Olot were much more honest in their responses compared to households interviewed in the GIZ/World Bank survey and Juraev’s Moscow survey. As a matter of fact, the interviewer in Olot approached the interviewees with the help of a local assistant, and this may have helped to establish a frank and sincere setting.

As Figure 3 shows, the GIZ/World Bank survey respondents note that the main reasons not to invest is inadequate entrepreneurial skills. In fact, 28.41 per cent of respondents indicated this as the main reason. The other two main reasons are insufficiency of funds available for investment (22.84 per cent), and other commitments to make (21.45 per cent). Other commitments probably include urgent family expenditures on consumer durables, health, education, and traditional rites.
Figure 3. Reasons for not investing in entrepreneurship

Source: World Bank-GIZ “Jobs, skills, migration, consumption” survey 2013

Juraev (2012) also reports that unwillingness to invest in a business could be due to the fact that many migrants doubt the possibility of earning appropriate income running a small business. The majority of respondents (55 per cent) to Juraev’s Moscow survey indicate among obstacles to running their own business that their savings are not enough to start business activity - it is notable that migrants do not even take into account the possibility of borrowing from a bank. About a third of respondents cited lack of knowledge and managerial skills as a hindrance for engaging in entrepreneurial activity and 26 per cent were concerned about the lack of experience in business.

Issues associated with banks top the list of problems hindering entrepreneurship in the interviews conducted in Olot as well. For instance, Juraev (2012) reports that 29 of 35 interviewed migrants complained about different aspects of dealing with banks in Uzbekistan, which make running a successful small business difficult. A quite sizeable proportion of respondents in this small-scale survey also referred to lack of essential knowledge (42.9 per cent), inspections of state agencies (40 per cent), and corrupted official at local levels of executive power (34.3 per cent). These are problems that all entrepreneurs are facing in Uzbekistan and it appears these
discourage investment in small business that potential entrepreneurs among labor migrants may consider to undertake.

Remittances can potentially influence the desire of beneficiaries to invest in a business in future. Therefore, the World Bank/GIZ survey asked all households if they intend to start a business (in their home country or overseas). Figure 4 compares households who receive remittances with those who do not in terms of their willingness to start their own business.

**Figure 4. Percentage of intending to start own business among households receiving and not receiving remittances**

Source: World Bank-GIZ “Jobs, skills, migration, consumption” survey 2013

It appears from Figure 4 that the percentage of households receiving remittances and intending to start a business in their home country is slightly higher compared to that of not receiving remittances. On the other hand, higher proportion of beneficiaries of remittances declared that they do not intend to start a business.

In order to explain investment motivation of households from the data collected in the survey, the next three figures further examine how the share of remittance income in total income effects investment decisions of households. This should reveal how remittance income impacts investment decisions of households.
Figure 5. Relationship between the share of income derived from remittances and intention to start own business

Source: World Bank-GIZ “Jobs, skills, migration, consumption” survey 2013

Figure 5 shows how the intention to start business among recipients of households varies depending on the proportion of remittances in the total income of households. It is notable that the intention to open own business is the highest among those who do not receive a significant part of their income from remittances – 0.3-9 per cent. This could be indicative of the fact that households receiving a small portion of their income in the form remittances lack capital to invest in entrepreneurship or there could be other factors preventing them from investing.
Figure 6. Relationship between the amount of remittances received and household investments in business

Source: World Bank-GIZ “Jobs, skills, migration, consumption” survey 2013

Figure 6 illustrates the relationship between the amount of remittances households receive and investment in an enterprise or a farm. Households are divided into four yearly remittance income brackets – $0-500, $500-950, $1,000-1,950, and $2,000-9,600 and the percentage of households investing in business is calculated for each bracket. As expected, it appears that the percentage of those investing in business in the highest income bracket is greater than in any other brackets. In combination with the observations made analyzing Figure 5, this indicates that households do not invest at least partly due to insufficiency of funds.

Now let us look at which households are likelier to invest in Uzbekistan depending on the timing of return of a migrant household member. It is expected that the households with a migrant who returned recently would have greater propensity to invest compared to those in which migrants returned a while ago because the latter one would have spent the savings accumulated during migration on other expenditures.
As Figure 7 shows, the households with family members having more recent migration experience invest more than those who came back earlier – resulting in investment decay over time. It appears that the longer migration experience goes back in time, less likely the household is to invest. In other words, since the earnings of migrants are not large and a significant portion of the migration savings are going to other types of expenditures, the farther the migration period less money left for investment. Only 1.6 per cent of households with a migrant returned in 2010-2011 invested compared to 6.62 per cent among those with member returned in 2012. In addition, 4.85 per cent of households with a migrant still abroad invest.\(^1\) The percentage for the latter is low probably due to the fact that migrants in neighboring countries, e.g. Kazakhstan, still bring most of their earnings home with them when they return (Kakhkharov and Akimov 2015)

\(^1\) The survey was conducted in 2013
6. Conclusion

The results of the present research indicate that the impact of remittances on entrepreneurship must be studied carefully. Relatively larger scale surveys of remittances reveal that remittances do not contribute to investment substantially. However, some small scale surveys show that actual contribution of remittances on MSME investment may be underestimated in bigger surveys. Moreover, a closer look at the investment generated by the savings of migrant returnees is necessary to have a comprehensive picture of the situation. Further analyses point out that households in receipt of remittance do not invest primarily due to the small size of remittances, lack of entrepreneurial skills, inadequate banking system, and presence of other pressing expenditure needs.

However, even if remittances are not used directly by beneficiary households in entrepreneurship, they still facilitate credit creation by helping households to buy physical assets, such as cars, jewelry, which subsequently could be used as collateral. This is crucial for banking systems similar to Uzbekistan’s, where lending is mainly facilitated by collateral.

It appears that the best way to stimulate efficient use of remittances and savings of migrants is to create an economic environment facilitating development in general, such favorable conditions for conducting business and a well-functioning financial system. The education and vocational system focused on developing entrepreneurial skills would also induce migrants to invest in their home economies and reap benefits offered by remittances more efficiently.
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