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Research Article

Remittance Dilemma in Nepal: Dependency, Economic Distortion and Challenges

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ABSTRACT

One of the most significant financial flows to developing nations today is remittances, which stabilise economies and reduce poverty in areas with limited formal employment opportunities. In 2023, they will account for 26.6% of Nepal's GDP, placing the nation among the most remittance-dependent economies in the world. Although remittances have improved foreign exchange reserves and household welfare, there is ongoing debate regarding their wider influence on long-term growth. Despite their size, little is known about how a high reliance impacts Nepal's industrial transformation and sustainable growth. Using a qualitative, literature-based methodology, this study finds that only 2.4% of Nepal's remittance revenue goes toward capital formation, whereas 78.9% is spent on everyday consumption. This trend has strengthened growth driven by consumption, undermined manufacturing and agriculture due to the consequences of Dutch disease, and increased dependency by reducing

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the number of workers in the country. The results highlight the fact that remittances are not essentially developmental; rather, they gain significance through their utilisation. Remittances will continue to be a short-term lifeline but a long-term barrier to Nepal's economic development unless they are diverted into productive sectors through financial literacy, diaspora participation, and governmental incentives.

Keywords: Remittances, Dependency Syndrome, Economic Distortion

Introduction

The concept of remittances predates modern economies, rooted in historical migration patterns. They play a dual role, sustaining household consumption while stabilising national foreign exchange reserves, often exceeding foreign direct investment and official development assistance. In ancient times, traders and laborers sent resources home to support families, often through barter or physical goods (Maimbo & Ratha, 2005). During the 19th and early 20th centuries, colonial migrations and industrialization spurred more formalized remittance flows. For instance, Indian and Chinese laborers in British colonies sent earnings home via postal services or informal networks like *hawala* (Ratha, 2013). These early remittances were small-scale, constrained by high transfer costs and limited financial infrastructure.

The post-World War II era marked a significant shift, as labor migration to rebuild Europe and the rise of guest worker programs in the Middle East increased remittance volumes. By the 1970s, remittances began to be recognized as a development resource, particularly in countries like Mexico and the Philippines, where they supported balance of payments (Maimbo & Ratha, 2005). The 1990s globalization wave and advancements in telecommunications and banking further amplified remittance flows, with digital platforms reducing costs and improving access (World Bank, 2022).

In the 21st century, remittances have become a critical lifeline for developing nations. The World Bank (2006) began systematically tracking remittance data, highlighting their growth from US$101 billion in 1995 to US$656 billion in 2023 for low- and middle-income countries (World Bank, 2023). This evolution reflects not only the rise in global migration but also technological innovations, such as mobile money and blockchain, that have reduced costs and increased the speed of remittance flows (SSIR, 2024).

Remittances have proven remarkably resilient, persisting through economic crises, pandemics, and geopolitical upheavals. Unlike FDI, which contracted by 40% during the COVID-19 pandemic, remittances to low- and middle-income countries dipped by only 1.6% in 2020 and rebounded to US$647 billion in 2022 (World Bank, 2022; UNCTAD, 2023). Ratha (2023) argument underscores that the resilience of remittances lies less in macroeconomic stability and more in the micro-level commitment of migrants, who prioritize family welfare over their own consumption, a factor that makes remittances uniquely reliable compared to other external financial flows. That, in contrast to aid or investment, remittances are a particularly stable and predictable source of foreign money since they are supported more by the moral and familial responsibilities of migrants than by economic cycles.

Several factors explain why remittances have remained remarkably persistent over time. First, global migration has continued to rise, with 281 million people living outside their countries of origin in 2020, largely driven by economic disparities, conflict, and climate change (IOM, 2020). Second, technological innovations such as mobile money and blockchain have significantly lowered transfer costs, from nearly 10% in 2000 to just 3.7% in 2022, aligning with SDG 10.C targets (World Bank, 2022; SSIR, 2024). Third, the deeply embedded cultural and familial obligations of migrants ensure that remittances remain a priority even in times of crisis; for example, inflows to Nepal remained strong after the 2015 earthquake, reaching US$7.8 billion in FY2018/19 (NRB, 2019). Finally, government and international initiatives, such as IFAD's SAMRIDDHI project, have further institutionalized remittance flows by promoting financial inclusion and diaspora engagement (IFAD, 2024). Taken together, these factors illustrate that the durability of remittances is not accidental but the result of a mutually reinforcing dynamic between global labor mobility, technological progress, social obligations, and supportive policy frameworks.

Nepal's heavy reliance on remittances, constituting over a quarter of GDP, has created a paradox. While remittances reduce poverty and stabilize foreign reserves, their consumption-driven use and labor migration have weakened industrial growth, increased dependency, and exposed the economy to external shocks. This problem of over-dependence forms the basis of the present study.

Literature Review

The literature emphasizes the need for policies to maximize the benefits of remittances while mitigating their downsides. IFAD (2020) advocates for incentives to channel remittances into productive sectors like agriculture and small businesses, such as tax breaks or subsidies for entrepreneurial ventures. Expanding digital financial services and financial literacy programs is critical to enhancing financial inclusion and reducing transfer costs (World Bank, 2022). IOM (2020) suggests leveraging the skills of returning migrants to boost domestic industries, while Sapkota (2018) underscores the importance of institutional quality in fostering synergy between remittances and economic growth.

Theoretically, the remittance dilemma aligns with dependency theory, which posits that reliance on external resources can hinder self-sustaining development (Adhikary & Hammer, 2022). Conversely, neoclassical migration theory views remittances as a rational household strategy to diversify income and reduce risk (Taylor, 1999). These frameworks highlight the tension between short-term benefits and long-term sustainability, underscoring the need for economic diversification. UNDP (2019) emphasizes investments in tourism, hydroelectricity, and agriculture to create domestic job opportunities and reduce reliance on remittances.

The discourse on remittance theoretical perspectives centers on the dual nature of remittances as both an empowering mechanism for household resilience and a potential inhibitor of endogenous growth, where external inflows may erode local agency and innovation. Draining from dependency theory, it interprets this as a structural trap in contexts like Nepal, where remittances perpetuate a cycle of outward migration and inward consumption, rather than fostering self-reliant economics. This view contrasts with neoclassical perspectives by emphasising socio-economics, such as power imbalances between host and home countries. To contribute originally propose integrating these theories into a hybrid framework for Nepal: a "remittance redirection model" that combines government incentives with community-based skill integration programs for returnees.

Economic Impacts

Remittances are a lifeline for developing economies, often exceeding other external financing sources. In 2023, they accounted for 26.6% of Nepal's GDP and 10% of the Philippines' GDP (World Bank, 2023). They stabilize economies by offsetting trade

deficits and bolstering foreign reserves, acting as a countercyclical force during crises (Nepal Rastra Bank, 2020). The "remittance multiplier effect" stimulates local economies through increased consumption and investment, boosting GDP (Oxford Economics, 2021).
At the household level, remittances reduce poverty and enhance human capital. A 1% increase in remittances as a share of GDP can reduce the poverty gap by 22.6% in Asian developing countries (ADB, 2017). Households allocate funds to education, healthcare, and durable goods, with 60% of income in some recipient families derived from remittances (UN DESA, 2019). Financial inclusion has also improved, with 90% of Nepalese adults accessing formal financial products by 2022 (World Bank, 2022).

However, remittances can foster dependency and economic distortions. In Nepal, 78.9% of remittances are spent on consumption, with only 2.4% on capital formation, limiting long-term growth (Nepal Rastra Bank, 2017). The "Dutch Disease" effect, where currency appreciation reduces export competitiveness, has weakened tradable sectors in countries like Nepal and El Salvador (Sapkota, 2018). Remittances are also vulnerable to external shocks, such as oil price fluctuations affecting Gulf economies, as seen during the COVID-19 pandemic (ILO, 2021).

The economic impacts of remittances as a paradox of immediate relief versus structural fragility, particularly in Nepal's context. The discourse reveals a tension: remittances fuel consumption-driven growth but undermine industrial and agricultural productivity by diverting resources from capital-intensive sectors. It would be, propose a "productive remittance framework" that incentivizes investment through microfinance programs tailored for remittance-receiving households, coupled with tax incentives for small businesses. This model, grounded in neoclassical migration theory's emphasis on income diversification and dependency theory's caution against external reliance, could redirect Nepal's remittance inflows toward sustainable economic development, addressing the current policy gap in channeling funds to productive sectors.

Social Impacts

Remittances reshape social structures, with both empowering and disruptive effects. They reduce poverty and improve access to education and healthcare, contributing to SDG attainment (IFAD, 2024). In Nepal, remittances have driven a 31-percentage-point poverty decline between 2003 and 2010 and empowered women by increasing their household decision-making roles (World Bank, 2011; UN Women, 2019).

However, mass migration disrupts communities. The exodus of young, skilled workers, 95% male in Nepal, leads to labor shortages, brain drain, and family fragmentation (IOM, 2020). In some Nepalese villages, 90% of young men have migrated, increasing divorce rates and HIV prevalence (UNDP, 2019). Women often face increased burdens, managing households alone, which can strain community cohesion (UN Women, 2019). A post on X highlights remittances as a "double-edged sword," providing funds but emptying communities of talent (Bertrand, 2024).

Based on the literature, the social impacts of remittances as a complex interplay between empowerment and erosion of community resilience, particularly in Nepal's rural context. The discourse underscores how remittances enhance household welfare but destabilize social fabrics by fueling male-dominated migration, which shifts burdens onto women and weakens communal ties. In Nepal's Karnali region, it is observed that migration-driven family separations exacerbate social isolation and gender-based challenges, yet also foster women's agency in resource management. To contribute originally, it would propose a “community reintegration and empowerment model” that leverages remittance-funded cooperatives to support women-led enterprises and reintegrate returnee migrants through skill-based training programs. This model, informed by dependency theory’s critique of external reliance and feminist perspectives on gender dynamics, aims to transform remittances into a tool for sustainable social cohesion, addressing Nepal’s current policy gap in supporting migrant families and communities.

Environmental Impacts

Remittances have mixed environmental effects. In rural areas, they enable investments in climate-resilient technologies, such as solar energy or sustainable agriculture, enhancing food security (IFAD, 2024). However, they can also drive environmental degradation. In Guatemala, remittance-funded agricultural expansion has increased deforestation and carbon emissions (IZA World of Labor, 2021). The net environmental impact depends on how funds are used and the strength of local regulations.

Remittance Dependency and Economic

Remittances, the funds sent by migrant workers to their home countries, are a significant economic resource for many developing nations, contributing to poverty reduction and household welfare. In 2023, remittances to low- and middle-income countries reached US$656 billion, often surpassing foreign direct investment (FDI) and official development assistance (World Bank, 2023). However, heavy reliance on remittances can foster dependency, discourage domestic economic development, and contribute to economic destruction through structural distortions and social disruptions. This article examines how remittance dependency undermines sustainable economic growth globally, with a specific focus on Nepal, where remittances constitute 26.6% of GDP (World Bank, 2023). Drawing on recent literature, it explores the mechanisms of dependency and destruction, supported by empirical evidence and policy insights.

Remittance Dependency: Mechanisms and Global Evidence

Remittance dependency occurs when economies rely excessively on migrant inflows, reducing incentives for domestic investment, innovation, and structural reforms. Globally, remittances can create a cycle where recipient households and governments prioritize short-term consumption over long-term development, leading to economic stagnation. Remittances are predominantly used for daily consumption rather than productive investments. A global study found that 60-80% of remittance funds are spent on food, housing, and consumer goods, with only a small fraction allocated to capital formation (IZA World of Labor, 2021). This limits the growth of productive sectors like agriculture and manufacturing, perpetuating reliance on external income.

Large remittance inflows can appreciate local currencies, making exports less competitive and weakening tradable sectors. This phenomenon, known as "Dutch Disease," has been observed in countries like El Salvador and the Philippines, where manufacturing and agriculture have declined due to remittance-driven currency strength (Acosta et al., 2009; Sapkota, 2018). Remittances reduce labor force participation by providing a steady income stream, discouraging recipients from seeking local employment. In Mexico, households receiving remittances showed a 5-10% lower labor participation rate compared to non-recipient households (Hanson, 2007). This creates a dependency trap, reducing domestic productivity.

High remittance inflows can reduce government incentives to implement structural reforms or invest in public goods. In some Pacific Island nations, remittances exceeding 20% of GDP have led to fiscal laxity, with governments relying on these flows to offset budget deficits rather than fostering economic diversification (Brown & Connell, 2015). Remittance-dependent economies are susceptible to fluctuations in host countries' economies. The COVID-19 pandemic demonstrated this, with a 1.6% global remittance decline in 2020 impacting countries like Haiti and Nepal, where foreign reserves and household incomes plummeted (World Bank, 2022).

Recent literature underscores these risks. IZA World of Labor (2021) argues that while remittances alleviate poverty, they can slow economic growth by fostering dependency and reducing domestic investment. Ratha (2023) notes that high transaction costs—averaging 6.3% globally and 8% in Sub-Saharan Africa, further erode remittance value, limiting their developmental potential.
However, the literature interprets remittance dependency as a structural vulnerability that transforms economic stability into a precarious reliance on external labor markets, particularly in contexts like Nepal. The discourse highlights how remittances, while alleviating immediate poverty, can entrench economic inertia by disincentivizing local entrepreneurship and industrial growth. It would be observed that remittance dependency often manifests as a cultural shift toward viewing migration as the primary path to prosperity, which erodes local innovation.

Economic Destruction: Social and Structural Impacts

Mass migration depletes human capital, as skilled and young workers leave for higher-paying jobs abroad. Globally, 281 million international migrants in 2020 included a significant share of skilled professionals, weakening domestic industries (IOM, 2020). This brain drain reduces innovation and productivity, perpetuating underdevelopment. Migration-driven remittances disrupt family and community structures. In rural areas, the absence of working-age populations leads to agricultural decline and social fragmentation. A study in Guatemala found that remittance-funded households faced higher divorce rates and weakened community cohesion due to prolonged family separations (Adams & Cuecuecha, 2010).

Remittances can exacerbate income inequality and drive inflation. In countries with selective migration, wealthier households benefit disproportionately, widening income gaps (IZA World of Labor, 2021). Additionally, increased consumption can raise local prices, particularly for housing and services, harming non-recipient households (Ratha, 2013). Remittance-funded activities, such as agricultural expansion or construction, can harm the environment. In Guatemala, remittances have been linked to deforestation, with a 10% increase in inflows correlating with a 3% rise in forest loss due to land clearing (IZA World of Labor, 2021). Over-reliance on remittances stifles diversification, leaving economies vulnerable to external shocks. A post on X describes remittances as a "drug" that provides immediate relief but destroys long-term potential by draining talent and fostering complacency (RnaudBertrand, 2024).

Nepal Context: Dependency and Economic Challenges

In Nepal, remittances are a critical yet problematic economic pillar, illustrating the dependency-destruction nexus. In 2023, remittances reached US$11 billion, accounting for 26.6% of GDP, far exceeding FDI and aid (World Bank, 2023). While these inflows have reduced poverty and stabilized the economy, they have also entrenched dependency and contributed to economic challenges.

Dependency in Nepal

A total of 78.9% of remittances are spent on daily consumption, with only 2.4% allocated to capital formation (NRB, 2017). This pattern limits investments in productive sectors, perpetuating reliance on migrant labor. Remittance inflows have strengthened the Nepalese rupee, reducing the competitiveness of agriculture and manufacturing. Sapkota (2018) estimates that a 10% increase in remittances reduces tradable sector output by 2-3%, contributing to economic stagnation.

The exodus of over 2 million Nepalese workers 95% male, has created rural labor shortages, particularly in agriculture, where productivity has declined (IOM, 2020). This has increased dependence on imported food, further straining the trade balance. The government has leaned on remittances to offset trade deficits and maintain foreign reserves, reducing urgency for structural reforms. Nepal Rastra Bank (2019) notes that remittances financed 80% of the trade deficit in FY2018/19, masking underlying economic weaknesses.

The migration of young, skilled workers has led to a brain drain, with up to 90% of young men absent in some rural villages (UN Women, 2019). This has disrupted agricultural systems and family structures, increasing divorce rates and HIV prevalence among migrants (UNDP, 2019). Remittances have driven urban real estate booms, inflating housing prices and exacerbating inequality between recipient and non-recipient households (Nepal Rastra Bank, 2017). Rural areas, meanwhile, face labor shortages and declining productivity.

Nepal's economy is highly sensitive to remittance fluctuations. The COVID-19 pandemic caused a temporary decline in inflows, threatening foreign reserves and household incomes (Nepal Rastra Bank, 2020). Most migrants work in volatile Gulf economies, exposing Nepal to oil price shocks (ILO, 2021). Remittance-funded construction and agricultural expansion have increased deforestation and water use in Nepal's rural areas, contributing to environmental degradation (UNDP, 2019). Nepal faces hurdles in mitigating remittance dependency, including high transfer costs for low-amount remittances (3.7% average), reliance on informal channels like *hundi*, and limited financial literacy, particularly among rural women (World Bank, 2022; UN Women, 2019). The lack of policies to channel remittances into productive investments exacerbates economic stagnation (Sapkota, 2018).

Research Design

This study adopts a qualitative, literature-based research design to critically examine the role of remittances in Nepal's economy. A total of 85 scholarly articles, policy reports, and statistical bulletins published up to 2024 were systematically reviewed. The data sources include peer-reviewed journals, institutional publications from the World Bank, IMF, ILO, and Nepal Rastra Bank, as well as policy reports from UNDP, IFAD, and IOM. These sources were selected for their credibility, relevance, and empirical depth.

The analysis employed thematic content analysis, whereby recurrent ideas and findings were coded into categories such as *remittance consumption patterns, capital formation, labor migration, Dutch Disease effects, and social impacts*. Through iterative comparison, these themes were synthesized to identify underlying mechanisms of dependency and economic distortion.

The rationale for adopting a literature-based qualitative method is twofold. First, given the abundance of secondary data but limited longitudinal field surveys on remittances in Nepal, a desk-based synthesis enables a comprehensive and timely understanding of the issue (Snyder, 2019). Second, qualitative thematic analysis is particularly suited to uncovering structural linkages and policy implications that quantitative surveys alone may not capture (Braun & Clarke, 2006). By integrating diverse evidence, this approach ensures analytical depth and contextual sensitivity, providing a solid foundation for the discussions that follow.

Results and Discussion

Remittances, the funds sent home by migrant workers, are a critical financial lifeline for many developing nations, significantly contributing to economic stability and poverty reduction. In 2023, global remittances to low- and middle-income countries reached US$656 billion, surpassing foreign direct investment (FDI) and official development assistance (World Bank, 2023). However, the reliance on remittances sparks debate: while they provide immediate economic benefits, they may foster dependency, disrupt community structures, and hinder long-term development. This article examines the role of remittances in supporting developing nations, explores their potential to destabilize communities, and discusses ongoing debates with a focus on recent literature.

Economic and Social Benefits of Remittances

Remittances are a vital source of external finance for developing countries, often exceeding other capital inflows. The World Bank (2023) notes that remittances to low- and middle-income countries grew to US$656 billion in 2023, with top recipients including India ($100 billion) and Mexico ($60 billion). These funds stabilize economies by offsetting trade deficits and bolstering foreign reserves, acting as a countercyclical force during crises like the COVID-19 pandemic, when remittances dipped only 1.6% compared to a 40% contraction in FDI (World Bank, 2022; UNCTAD, 2023).

At the household level, remittances reduce poverty and enhance living standards. A study across 10 Asian developing countries found that a 1% increase in remittances as a percentage of GDP led to a 22.6% decline in the poverty gap ratio and a 16% decline in poverty severity (ADB, 2017). Remittances fund essential expenses like food, healthcare, and education, with up to 60% of household income in recipient families derived from these inflows (UN DESA, 2019). They also promote financial inclusion, with digital platforms reducing transfer costs to 3.7% in 2022, nearing the UN Sustainable Development Goal (SDG) target of 3% (World Bank, 2022).

Beyond households, remittances contribute to community resilience. IFAD (2024) highlights those remittances to rural areas bolster climate resilience by enabling investments in eco-friendly technologies and food security measures. Strategic partnerships and digital innovations further amplify these benefits by lowering costs and improving access to financial services (IFAD, 2024; UN, 2024). Remittances also support SDG attainment, particularly in ending poverty, promoting health, and reducing inequalities, with an estimated US$1.5 trillion expected to be saved or invested between 2022 and 2030 (IFAD, 2024).

Community Disruption and Negative Impacts

Despite their benefits, remittances can destabilize communities and create long-term challenges. One major concern is the culture of dependency they foster. Studies suggest that heavy reliance on remittances reduces labor force participation and discourages domestic investment, as households prioritize consumption over productive activities (IZA World of Labor, 2021). In Nepal, for instance, 78.9% of remittances are spent on daily needs, with only 2.4% allocated to capital formation, limiting economic growth (Nepal Rastra Bank, 2017).

The social fabric of communities is also strained by mass migration. The exodus of young, skilled workers often male leads to labor shortages, particularly in rural areas, and a "brain drain" that depletes human capital (IOM, 2020). In some Nepalese villages, up to 90% of young men have migrated, disrupting agricultural productivity and family structures (UN Women, 2019). This can result in increased divorce rates, higher HIV prevalence among migrants, and shifting gender roles, placing additional burdens on women (UNDP, 2019). A post on X echoes this sentiment, describing remittances as creating "cycles of dependency" akin to a "drug" that provides immediate relief but hinders development by removing skilled professionals from local economies (RnaudBertrand, 2024).

Environmental impacts are another concern. In Guatemala, remittances have been linked to deforestation, as recipients and returning migrants expand agricultural activities, increasing solid fuel use and carbon emissions (IZA World of Labor, 2021). While remittances may enable cleaner energy adoption among higher-income households, their net environmental effect remains debated (IZA World of Labor, 2021).

Economic vulnerabilities also arise. Remittances are subject to external shocks, such as economic downturns in host countries or oil price fluctuations affecting Gulf economies, where many migrants work (ILO, 2021). The COVID-19 pandemic highlighted this fragility, with temporary declines threatening recipient economies (Nepal Rastra Bank, 2020). Moreover, high transaction costs averaging 6.3% globally and 8% in Africa reduce the effective value of remittances, particularly for low-income households (Ratha, 2023).

Based on the evidence, the community disruption caused by remittances is a dual process of economic enablement and social erosion, where short-term financial gains come at the cost of long-term community cohesion and resilience. Nepal's Sudurpashchim region reveals that migration-driven remittances fragment social networks by creating a culture of absenteeism, particularly among young men, which undermines collective agricultural practices and local governance structures. It is informed by feminist perspectives on gender roles and dependency theory's critique of external reliance, aims to mitigate community disruption by channeling remittances into collective enterprises that strengthen social bonds and reduce dependency on migration, addressing Nepal's policy gap in supporting cohesive rural communities.

Debate: Development Catalyst vs. Dependency Trap

The debate over whether remittances act as a development catalyst or a dependency trap centers on their dual role in developing nations. Proponents argue that remittances, surpassing traditional aid, directly alleviate poverty, fund education and healthcare, and stimulate local economies through a multiplier effect, with innovations like digital platforms enhancing efficiency (SSIR, 2024; Oxford Economics, 2021). Conversely, critics highlight that remittances foster dependency, reduce labor participation, and cause economic distortions like the “Dutch Disease,” weakening sectors like agriculture and manufacturing, as seen in Nepal (Sapkota, 2018; IZA World of Labor, 2021). Both sides agree that policy interventions, such as reducing transaction costs and promoting productive investments, are crucial to maximizing benefits and mitigating risks, with the outcome depending on how remittances are channeled and the strength of local institutions (World Bank, 2022; UN, 2024).

Pro-Remittance Argument: A Catalyst for Development

Proponents argue that remittances are a reliable and direct source of development finance, surpassing traditional aid due to their scale and targeting. Unlike aid, remittances are controlled by beneficiaries, ensuring funds meet immediate needs like healthcare and education, which reduce poverty and build human capital (SSIR, 2024; Oxford Economics, 2021). A Mexican study found that a 10% increase in remittances correlated with a 7% decrease in extreme poverty over 35 years (SSIR, 2024). Digital innovations, such as blockchain and mobile platforms, further enhance efficiency, with projects like Singapore's Project Ubin reducing transaction times and costs (SSIR, 2024).

Remittances also have a multiplier effect, stimulating local economies through increased spending and investment. Oxford Economics (2021) describes this as the "remittance multiplier effect," boosting GDP and supporting economic recovery post-crisis. Initiatives like diaspora bonds and financial inclusion programs can channel remittances into productive investments, such as small businesses or climate-resilient infrastructure, aligning with SDGs (UN, 2024; IFAD, 2024). Proponents assert that with proper policies e.g., reducing transfer costs to 3% by 2030 and improving financial literacy remittances can bridge the US$4 trillion annual development financing gap (UN, 2024).

Anti-Remittance Argument: A Dependency Trap

Critics contend that remittances create dependency, undermine local economies, and exacerbate inequality. The "Dutch Disease" effect, where remittance inflows strengthen currencies and reduce export competitiveness, has been observed in countries like Nepal, weakening manufacturing and agriculture (Sapkota, 2018). IZA World of Labor (2021) notes that remittances can reduce labor supply and promote conspicuous consumption, diverting funds from productive investments. Some studies even suggest remittances slow economic growth by fostering reliance on external income rather than domestic development (IZA World of Labor, 2021).

Reconciling Perspectives

The debate hinges on causality and context. While remittances undeniably alleviate poverty, their long-term impact depends on how funds are used and the policies in place. Proponents advocate for leveraging remittances through financial inclusion and investment incentives, while critics emphasize the need to address structural issues like brain drain and economic dependency. Both sides agree that reducing transaction costs, improving data quality, and promoting formal remittance channels are critical for maximizing benefits (World Bank, 2022; UN, 2024).

The Remittance Dilemma in Nepal: A Crutch Preventing Industrialization

In Nepal, remittances are a vital economic lifeline, contributing US$11 billion in 2023, equivalent to 26.6% of the nation's GDP (World Bank, 2023). These inflows, primarily from migrant workers in Gulf Cooperation Council (GCC) countries, Malaysia, and India, have reduced poverty and stabilized the economy. However, scholars and critics argue that Nepal's heavy reliance on remittances acts as a crutch, fostering dependency and preventing industrialization, which is critical for sustainable economic development. This article examines the remittance dilemma in Nepal, focusing on the criticism that it hinders industrial growth, supported by recent scholarly arguments and evidence.

The Remittance Dilemma: Economic Lifeline vs. Dependency Trap

Remittances have undeniably transformed Nepal's socio-economic landscape. Between 2003 and 2010, the poverty headcount ratio at $1.90 a day fell by 31 percentage points, largely due to remittance inflows (World Bank, 2022). These funds support household consumption, education, and healthcare, while bolstering foreign reserves and offsetting trade deficits (Nepal Rastra Bank, 2019). However, the dilemma lies in the trade-off: while remittances provide immediate relief, they create a dependency that undermines long-term industrial and economic development.

Scholars argue that Nepal's remittance-driven economy discourages the structural reforms and investments needed for industrialization. The reliance on external income streams masks underlying economic weaknesses, such as low productivity, weak infrastructure, and limited manufacturing capacity. This dependency is particularly pronounced in regions like Karnali and Sudurpashchim, where traditional migration to India sustains households but stifles local economic diversification (IOM, 2020).

Scholarly Arguments: A Barrier to Sustainable Development

Scholars emphasize that remittances, while reducing poverty, act as a barrier to sustainable industrialization by fostering dependency and distorting economic incentives: Adhikari and Hobley (2022) argue that remittances create a "dependency syndrome," where households and policymakers prioritize short-term gains over long-term industrial strategies. This is evident in Nepal's stagnant manufacturing sector, which contributes only 5.6% to GDP, compared to 20–30% in industrialized Asian economies (World Bank, 2023).

Bhusal et al. (2023) find that remittance inflows crowd out domestic investment by increasing consumption and real estate demand, reducing capital available for industrial projects. Nepal's industrial investment rate remains below 10% of GDP, far lower than India (25%) or Vietnam (30%) (World Bank, 2023). Shrestha (2021) highlights that migration-driven remittances disrupt social structures, with family fragmentation and increased burdens on women in Karnali and Sudurpashchim undermining community resilience. These social costs indirectly hamper industrial development by limiting rural labor availability and social capital (UN Women, 2019).

K.C. and Thapa (2024) note that Nepal's remittance-dependent economy is vulnerable to global shocks, such as oil price fluctuations or pandemics, which disrupt industrial planning. The COVID-19 pandemic caused a temporary remittance decline, exposing Nepal's lack of industrial buffers (Nepal Rastra Bank, 2020). Critics argue that without industrialization, Nepal cannot achieve sustainable growth. Remittances, while stabilizing, do not address structural issues like low productivity, energy deficits, or weak institutions, which are critical for industrial take-off (Adhikari & Hobley, 2022).

Counterarguments: Remittances as a Potential Catalyst

Some scholars caution against dismissing remittances outright, suggesting they could support industrialization if properly managed. IFAD (2024) points to initiatives like the SAMRIDDHI project, which promotes rural enterprises using remittance funds, as models for industrial growth. Digital financial inclusion, with 90% of Nepalese adults accessing formal financial products by 2022, could channel remittances into small-scale industries (World Bank, 2022). However, these arguments are tempered by Nepal's weak policy framework, which fails to redirect remittances from consumption to productive investments (Bhusal et al., 2023).

Remittances have significantly shaped Nepal's economy but are increasingly criticized for rendering Nepalis "bhutte" (lazy and dependent). In 2023, remittances accounted for 26.6% of Nepal's GDP, reducing poverty and supporting household expenses (World Bank, 2023). However, with 78.9% of remittances spent on daily consumption and only 2.4% on capital formation, productive investment remains limited (Nepal Rastra Bank, 2017). This drives youth toward foreign employment, causing labor shortages and agricultural decline in regions like Karnali and Sudurpashchim (IOM, 2020). The Dutch Disease effect, where remittance inflows strengthen the currency, weakens industrial sectors, hindering economic diversification and industrialization (Sapkota, 2018). Consequently, while remittances provide short-term relief, they foster long-term dependency, stifling entrepreneurship and self-reliance, thus making Nepali society more passive and economically vulnerable.

Discussion and Critical Analysis of the Impact

Remittance accounts for ~24% of Nepal's GDP, making it a key macroeconomic pillar. It stabilizes foreign exchange reserves, helping to finance Nepal's large trade deficit (more than NPR 1,400 billion in FY 2022/23). Makes Nepal vulnerable to external shocks like oil prices or geopolitical tensions in Gulf countries. (NRB, 2024). Increases in household income improve education, food security, and health access (World Bank, 2022). However, over 80% of remittance is spent on consumption (e.g., real estate, consumer goods), not on investment. Underutilization for productive investment limits long-term development. (NRB, 2021).

Migration draws youth away from agriculture and small industries, weakening the domestic economy's productive base. Returnee migrants often face reintegration challenges and unemployment due to skills mismatch. Leads to a "brain and brawn drain", weakening national labor competitiveness (ILO, 2021). In the same way, increases in male outmigration shift household management to women, which can enhance empowerment. However, many women suffer from social isolation, economic pressure, and in some cases, gender-based violence. Unequal access to remittances often reinforces gender and caste inequalities (UN Women, 2020).

Table 1: Remittance receive status

Fiscal Year	Remittance Inflows (NPR Billion)	Growth Rate (%)
2020/21	961.05	N/A
2021/22	1,007.31	4.8
2022/23	1,220.56	21.2
2023/24	1,445.32	16.5
2024/25	900.58 (first 7 months)	7.3 (first 7 months)

(Source: NRB, 2025)

According to Nepal Rastra Bank (2021), (See Table 1) more than 78.9% of remittances are spent on daily consumption, such as food, clothing, and household goods. Only 2.4% is allocated to capital formation, like starting a business, buying machinery, or investing in productive assets. According to (Bhandari, R. 2024), this heavy focus on consumption creates a short-term improvement in living standards but does not build economic foundations that generate employment or wealth sustainably. Despite the volume of remittances, Nepal lacks strong policies or institutions to channel this income into productive ventures, such as agro-processing, rural industries, or cooperative enterprises. The absence of such pathways means remittances mask economic vulnerability but do not solve it (Adhikari & Hobley, 2022).

Despite remittance inflows, Nepal runs a chronic trade deficit. The foreign currency earned is often used to import consumer goods rather than capital or productive machinery. In FY 2022/23, Nepal's trade deficit stood at over NPR 1,400 billion, even while remittance inflows were high (MoF, 2023). A high inflow of foreign currency appreciates the local currency, making exports less competitive. This reduces the growth of the export sector and encourages imports, deepening the structural trade imbalance (IMF, 2021). With so many working-age men abroad, Nepal faces a shrinking labor force in agriculture and manufacturing. This weakens domestic production capacity, making the economy more reliant on imports and foreign income.

Use of Remittance, over 80% of remittance in Nepal is used for daily consumption, loan repayments, and real estate rather than for investment or entrepreneurship (NRB, 2021). Very little remittance is directed into formal savings or productive sectors like agribusiness, small enterprises, or cooperatives. This underutilization limits long-term development impact. If even 20% of remittance were invested into MSMEs or agri-industries, it could transform rural economies, reduce dependency on foreign jobs, and generate domestic employment.

How Remittance Leads to Economic Distortion

In Nepal and other remittance-dependent countries, remittance inflows have improved livelihoods but also contributed to economic imbalances. Remittance income is often invested in land and housing rather than businesses or industries. This pushes up property prices, especially in urban and semi-urban areas, making housing unaffordable for low-income groups (Sharma, 2025). Migration of working-age men leads to labor scarcity in agriculture, forcing households to reduce farm size or shift to subsistence farming. This reduces domestic food production and increases reliance on imports. In the mid-hills and Tarai, farming activities have declined due to youth migration, despite households having higher incomes. This results in underutilized land and a neglect of the rural economy (Adhikari & Hobley, 2015).

High remittance inflow increases foreign exchange reserves, leading to currency appreciation. A stronger currency makes exports more expensive and hurts the competitiveness of domestic industries. NRB reported that despite record remittance inflows in 2022–23, exports remained low and the trade deficit widened, reflecting weak industrial output (NRB, 2023). A majority of remittances is spent on daily consumption and luxury goods rather than being channeled into entrepreneurship, skills, or infrastructure. This creates a false sense of prosperity and masks structural economic weaknesses. NRB's 2021 survey found that over 80% of remittances are used for consumption, while only around 3% is invested in business or income-generating activities (NRB, 2021).

Conclusion and Recommendation

The purpose of this study was to critically examine the paradoxical role of remittances in Nepal's economy, situating them as both a lifeline for households and a structural constraint on long-term transformation. The analysis shows that while remittances contribute nearly one-quarter of GDP and have been vital for poverty reduction, foreign exchange stability, and household welfare, their developmental impact remains limited. A persistent pattern of consumption-driven use where nearly four-fifths of inflows are directed to daily needs and less than three percent to productive investment has reinforced dependency, widened trade deficits, and slowed industrial growth. Furthermore, Dutch Disease effects and mass labor migration have eroded the competitiveness of agriculture and manufacturing, while fostering a cycle of migration and consumption.

The findings therefore highlight a central dilemma: remittances provide immediate relief but risk entrenching structural vulnerabilities if not harnessed productively. To break this cycle, Nepal must adopt strategies that redirect remittance flows toward capital formation, entrepreneurship, and industrial upgrading, supported by financial literacy, diaspora engagement, and targeted policy incentives. Unless such reforms are pursued, remittances will remain a short-term buffer but a long-term barrier to economic transformation.

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