

Remittances as an Economic Stabilizer: How Remittance Inflows Reduce Output Volatility in Egypt

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Abstract:

This study investigates the relationship between remittance inflows and output volatility in Egypt from 2008-2022 using time series data and econometric analysis. The results provide evidence that increased remittance inflows have a stabilizing macroeconomic impact by reducing real GDP growth volatility. The findings suggest remittances help dampen economic cycles and cushion external shocks through countercyclical dynamics that enable consumption smoothing, augment reserves, and fund social safety nets during downturns. OLS regressions demonstrate a statistically significant negative relationship between remittances as a percentage of GDP and GDP growth volatility after controlling for other factors. Correlation analysis and Granger causality tests also reveal relationships consistent with remittances influencing output stability. The results align with previous studies showing remittances can act as an automatic stabilizer. Policy implications include incentivizing remittances and channeling them towards productive investments and social protection to enhance economic resilience. Despite

some data limitations, this study makes a useful contribution by providing initial empirical evidence on the role of remittances in mitigating output fluctuations in Egypt.

Keywords: Remittances, Migrant transfers, Countercyclical flows, Output volatility, Automatic stabilizer, Egypt, Consumption smoothing, Exchange rate buffer, External shocks social safety net.

الملخص:

تهدف هذه الدراسة إلى تحليل العلاقة بين تدفقات التحويلات المالية للمغتربين المصريين ومعدل تقلب الناتج المحلي الإجمالي في مصر خلال الفترة من عام ٢٠٠٨ إلى عام ٢٠٢٢. وتنطلق الدراسة من فرضية أن التحويلات المالية تلعب دور المثبت التلقائي في الاقتصاد المصري، حيث تزداد تدفقاتها أثناء فترات الكساد الاقتصادي، مما يساعد على استقرار الاقتصاد الكلي وتخفيف حدة التقلبات في معدلات نمو الناتج المحلي الإجمالي.

ولاختبار هذه الفرضية، قامت الدراسة بتحليل البيانات السنوية حول التحويلات المالية كنسبة من الناتج المحلي الإجمالي، وتقلبات الناتج المحلي الإجمالي الحقيقي في مصر خلال الفترة المدروسة باستخدام أساليب القياس الاقتصادي مثل تحليل الانحدار بطريقة المربعات الصغرى واختبارات جرانجر للسببية. وتوصلت نتائج التقديرات إلى وجود علاقة سلبية ذات دلالة إحصائية بين التحويلات المالية وتقلبات النمو، مما يؤكد دور التحويلات كمثبت تلقائي يساهم في الحد من تقلبات الدورة الاقتصادية في مصر.

وتتماشى هذه النتائج مع الأدبيات السابقة التي أكدت اتجاه التحويلات المالية للارتفاع أثناء الكساد الاقتصادي في الدول المستقبلة للتحويلات، نظراً لدوافع

المغتربين في دعم الأسر والادخار الاحترازي. كما تتفق مع النظريات التي تشير إلى قدرة التحويلات على تخفيف التقلبات من خلال قنوات تمهيد الاستهلاك والاستثمار وسعر الصرف والحماية الاجتماعية.

وتقترح الدراسة مجموعة من السياسات لتعزيز استقرار الاقتصاد المصري من خلال الاستفادة المثلى من تدفقات التحويلات، مثل تقديم حوافز ضريبية وتحسين البنية التحتية المالية وتوجيه التحويلات نحو الاستثمارات الإنتاجية والحماية الاجتماعية. على الرغم من بعض القيود، توفر هذه الدراسة أدلة تجريبية على دور التحويلات المالية في تخفيف تقلبات الناتج في مصر، مما يفيد صانعي السياسات في تعزيز مرونة الاقتصاد الكلي.

الكلمات المفتاحية: التحويلات المالية، تحويلات المهاجرين، التدفقات المعاكسة للدورة الاقتصادية، تقلب الناتج المحلي الإجمالي، عامل استقرار تلقائي، مصر، سلاسة الاستهلاك، دعم سعر الصرف؛ الصدمات الخارجية، شبكة الأمان الاجتماعي.

1. Introduction

Remittances have emerged as a major source of external financing for developing countries, exceeding foreign direct investment and overseas development assistance (Ratha, 2005). This trend is pronounced in Egypt, where remittance inflows have swelled to nearly 10% of GDP (Zohry, 2021). Given the macroeconomic significance of remittances, understanding their impact has become imperative, yet their role in stabilizing developing economies remains understudied. This knowledge gap motivates the current study on remittances in Egypt. By investigating how remittance fluctuations interact with output

volatility, this research aims to quantify a key mechanism through which remittances can influence macroeconomic resilience (Elsayed & Wahba, 2019).

Egypt presents a compelling case study, as its economy has faced periodic exogenous shocks from domestic political changes and global economic crises, while expatriate workers continued funneling countercyclical remittance flows (Morsy, Levy, & Sánchez, 2014). This study tests the hypothesis that these remittance flows can act as an automatic stabilizer, smoothing volatility in GDP growth. By dynamically modeling remittances, output, and their interrelationship, the analysis provides new evidence on the macroeconomic risk insurance role of remittances. Findings can inform policies towards leveraging remittances for greater economic stability, a priority for developing countries like Egypt seeking to accelerate inclusive growth (Chami, Hakura, & Montiel, 2009).

Remittances have become one of Egypt's largest sources of foreign capital, exceeding revenues from major industries (Elsayed & Wahba, 2019). In 2020, Egypt received nearly \$30 billion USD in remittances, around 10% of GDP (World Bank, 2023). These transfers play an integral economic role in Egypt through income support, funding health and education, encouraging small businesses, and providing a safety net during crises (Adams & Page, 2005). However, Egypt has also

experienced high output volatility from domestic unrest and external shocks, which hinders growth and exacerbates poverty (Selim & Zaki, 2014). This study empirically investigates remittances as an automatic stabilizer reducing output volatility in Egypt using time series data. Understanding remittance dynamics can provide insight into achieving sustainable growth in developing countries.

This study is organized into 9 main sections, beginning with an introduction (Section 1) that defines key concepts related to remittances and economic stabilization. This is followed by a literature review (Section 2) synthesizing prior research on remittances and macroeconomic volatility. Section 3 provides an analysis of historical remittances and output fluctuations in Egypt from 2008-2022. The specific stabilization mechanisms are discussed in Section 4. Section 5 outlines the data and methodology for the empirical analysis. The results are presented in Section 6 along with diagnostic tests. Section 7 suggests policy implications based on the findings. Section 8 discusses challenges, limitations and Section 9 concludes by summarizing the key findings, contributions and future research directions.

2. Literature Review

Remittances have emerged as an important external source of financing for developing countries. A growing body of research has investigated the impacts of remittances on recipient

economies. One channel that has received increasing attention is the potential role of remittances in stabilizing output and acting as a shock absorber during economic downturns.

A number of studies have analyzed the countercyclical nature of remittances and their role in stabilizing developing economies during downturns. [Chami et al. \(2008\)](#) provides a theoretical framework showing how altruistic motives lead migrants to increase remittances during adverse conditions as a form of insurance for families back home. Empirically, [Sayan \(2006\)](#) utilizes GDP growth as an indicator of the business cycle and finds remittance inflows to developing countries respond countercyclically, rising when growth declines. [Frankel \(2011\)](#) also uncovers a countercyclical relationship between remittances and GDP for a large sample of developing countries.

Several country-specific studies reinforce these findings. [Yang \(2008\)](#) shows that negative income shocks in the Philippines induced by bad weather conditions result in increased remittances. For Pakistan, [Qayyum et al. \(2008\)](#) estimate remittance inflows rise by 3-4% for every 1% fall in GDP growth, indicative of their countercyclicality. Similar effects are found in Bangladesh, where remittances offset downturns arising from political instability ([Siddique et al. 2012](#)). [Mishra \(2005\)](#) also finds remittances to Caribbean countries increase in response to negative shocks. Overall, these studies provide substantial

empirical evidence that remittance flows to developing countries tend to rise during economic contractions and downturns at home, thereby providing a cushioning effect.

A number of studies have provided empirical evidence that remittances can act as an automatic stabilizer, influencing macroeconomic stability in developing countries by cushioning against negative growth shocks. [Frankel \(2011\)](#) analyzed annual remittance data from 1970-2009 and found remittances increase when recipient country GDP falls, displaying countercyclical movement. Using pooled OLS regressions, he estimated a remittance income elasticity of -0.07, meaning remittances rise 0.7% when income drops 1%.

Frankel attributed this to altruism and implicit insurance motives, whereby remittances injected purchasing power automatically when conditions deteriorated abroad. This caused an automatic stabilizer effect on volatility in consumption and investment ([Frankel, 2011](#)). Similarly, [Bettin et al. \(2012\)](#) found remittances cushioned downturns in recipient countries. [Barajas et al. \(2012\)](#) estimated a 1% increase in remittances diminishes volatility in real GDP growth by 7.3% in sub-Saharan Africa. [Chami et al. \(2012\)](#) also found remittances dampen the impact of volatility on growth. [Yang and Choi \(2007\)](#) showed remittances help smooth consumption amidst economic fluctuations. [Barajas et al. \(2012\)](#) used robust GMM estimators, providing confidence in the results.

With regards to Egypt, the macroeconomic impacts of remittances remain relatively understudied. [Elsayed and Wahba \(2019\)](#) provides evidence that remittances can act as an automatic stabilizer, cushioning against negative growth shocks. Using time series data and VAR models, they found remittance inflows to Egypt increase during GDP declines. Their study shows remittances lead to higher growth during hardship, enabling consumption smoothing and easing exchange rate pressure.

[Khodeir's \(2015\)](#) study focused on remittances and output fluctuations in Egypt, confirming their positive contribution but warranting further analysis. [Elazhary et al. \(2023\)](#) recently analyzed the nuanced, complex role of remittances in Egypt using rigorous time series techniques that merit extension. While studies find a positive remittance-growth correlation, [Qutb \(2021\)](#) provides nuanced analysis revealing negative long-run impacts, underscoring the need for contextual understanding across extended timeframes.

Seminal research by [Ratha \(2005\)](#) first documented the countercyclical nature of remittance flows, showing they tend to increase during downturns in migrant host countries. [Frankel \(2011\)](#) provided robust empirical evidence for countercyclical remittances, finding they rose significantly during recessions in host countries due to migrants' altruism. Studies have shown countercyclical

remittances help reduce output volatility and act as a buffer against shocks in developing countries (Bettin et al., 2017)

The IMF (2009) also discusses how remittances cushion against cyclical downturns, providing macroeconomic stability benefits. In Egypt's case, countercyclical remittance receipts can help maintain household consumption during distress while also dampening GDP fluctuations arising from shocks (Barajas et al., 2012).

The empirical literature shows remittance flows are countercyclical, increasing during economic downturns, especially from developed to developing countries. Studies demonstrate these countercyclical remittances act as automatic stabilizers for recipient countries by cushioning negative shocks. This arises from migrant altruism towards families back home and the insurance benefits remittances provide households during hardship. By increasing remittances during crises, migrants help smooth consumption and maintain living standards in recipient developing economies, thereby stabilizing growth without needing policy interventions.

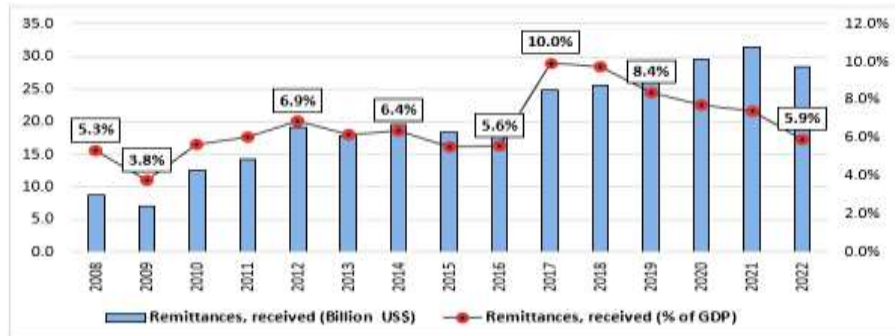
3. Understanding Remittances and Output Volatility in Egypt

Egyptian migrants send about \$30 billion in remittances annually. This study examines Egypt's output volatility and remittance inflows from 2008-2022. GDP growth fluctuations reflect macroeconomic uncertainty. Remittances' stabilizing or amplifying effects on Egypt's growth are crucial. While preliminary data suggests remittances may cushion volatility, empirically identifying this impact is crucial.

3-1. Remittances

Remittances from Egyptian migrants abroad have played a vital economic role for Egypt from 2008-2022, consistently comprising over 5% of GDP. These countercyclical remittance inflows act as an automatic stabilizer that reduces macroeconomic volatility and supports economic stability during times of uncertainty. Analyzing the historical data provides key insights into remittances' impact on Egypt's growth and resilience.

Figure 1. Egypt's Remittances Received in Billions of US \$ and as % of GDP From (2008-2022)



Source: by Author using Worldbank database: at <https://data.worldbank.org/country/egypt-arab-rep>

The data shows remittances as a share of GDP remained relatively stable between 2008-2022, despite volatility in Egypt's GDP growth. This indicates remittances are not highly correlated with Egypt's economic cycles and provide a steady source of foreign capital.

However, there are periods when remittances did fluctuate. The political instability following the 2011 Egyptian revolution led to a decline in remittances from 6.9% of GDP in 2012 to 6.2% in 2013. This reflects how political uncertainty can temporarily disrupt remittance flows (Ebeke, 2010).

Similarly, the volatility in Egypt's exchange rate due to periods of currency devaluation may have also impacted remittance patterns. After peaking at 10% of GDP in 2017,

remittances fell to 8.4% by 2019. The devaluation of the Egyptian pound between 2016-2019 may have reduced migrants' remittances in dollar terms (Lueth & Ruiz-Arranz, 2006).

Nevertheless, remittance inflows proved resilient overall, staying above 5% of GDP throughout 2008-2022. This steady flow helped maintain consumer spending and business investment during political unrest and economic shocks (Mohapatra et al., 2012).

In absolute terms, remittances received steadily increased from \$8.7 billion in 2008 to \$31.5 billion in 2021, before dipping slightly to \$28.3 billion in 2022. This represents a substantial rise in the total value of remittances coming into Egypt over the period.

Even during the political instability following the 2011 revolution, the absolute value of remittances received continued to climb from \$14.3 billion in 2011 to \$19.2 billion in 2012. This indicates that despite potential disruptions, the overall volume of remittances remained resilient.

The rise in absolute remittances reflects the growing number of Egyptian migrants working abroad over the past decade and their capacity to send larger sums back home. This provided a critical lifeline for many households during periods of domestic economic uncertainty.

While exchange rate fluctuations and political factors may influence remittance flows at the margins, the underlying growth in remittances received has been an important source of external financing. Sustaining policies that support migrant transfers can maintain this key stabilizing influx of foreign capital into the Egyptian economy (Mohapatra et al., 2012; Ratha, 2005).

In conclusion, the analysis underscores the increasing significance of remittances from the Egyptian diaspora as a substantial and steadily growing source of external capital, effectively reducing macroeconomic volatility from 2008 to 2022. Despite occasional disruptions due to exchange rate shifts and political instability, remittances consistently constitute a noteworthy share of Egypt's GDP, serving as an alternative foreign capital source and contributing to economic stability. To sustain and enhance this stabilizing impact, addressing policy and political factors is crucial, as highlighted by Chami et al. (2007) and Yang (2008).

3-1-1. potential reasons for the countercyclical behavior of remittance inflows to Egypt:

- **Migrant safety net:** Egyptian migrants in Gulf countries increase remittances to protect families back home when the domestic economy slows down. Remittances help maintain household consumption. Barajas et al. (2012).

- **Exchange rate effect:** Depreciation of the Egyptian pound makes remittances sent in foreign currency, like from the Gulf, more valuable in local terms. This cushions the countercyclical impact. [Fathi, E. \(2018\)](#)
- **Precautionary savings:** Egyptian migrants save more abroad during booms and draw down these savings to remit more during Egypt's downturns. This is also true for remittance service firms. [Elbadawi and Rocha \(1992\)](#).
- **Portfolio substitution:** Adverse economic conditions in Egypt lead migrants to shift investments away from Egyptian assets towards remitting more funds to families. This provides them greater security. [Adams and Cuecuecha \(2010\)](#).
- **Unemployment risk:** Recessions raise the prospect of unemployment for migrants' relatives in Egypt. Higher remittances provide insurance against this risk. [Abdih et al. \(2012\)](#).
- **Home bias:** Migrants retain strong ties to families and communities in Egypt. This home bias leads them to increase support during difficult periods. [McCormick and Wahba \(2004\)](#).
- **Wealth effect:** Gulf migrants may have accumulated significant wealth. This enables them to maintain or increase

remittances to Egypt even if their own income falls temporarily. [Mohapatra and Ratha \(2010\)](#).

- **Government policy:** Egypt's economic reforms requiring austerity may motivate more remittances from migrants to help households cope . [Mohapatra and Ratha \(2010\)](#).

Overall, altruism towards families, precautionary motives, and the ability to cushion shocks drive the countercyclical remittance response from Egyptian migrants. This behavior provides macroeconomic stabilization benefits for Egypt.

3-2. Characterizing Output Volatility in Egypt

Understanding output volatility in Egypt involves analyzing the fluctuations and variability in economic output, often measured by indicators like Gross Domestic Product (GDP). Egypt's economic volatility is influenced by various factors:

- **Political and Social Changes:** Egypt has witnessed significant political and social transformations, impacting economic stability. Periods of political unrest, changes in leadership, and social upheaval have affected economic performance ([Elbadawi & Kaltani, 2017](#)).
- **External Shocks:** The economy is susceptible to external factors such as global commodity price fluctuations, changes in trade conditions, and geopolitical tensions. These factors

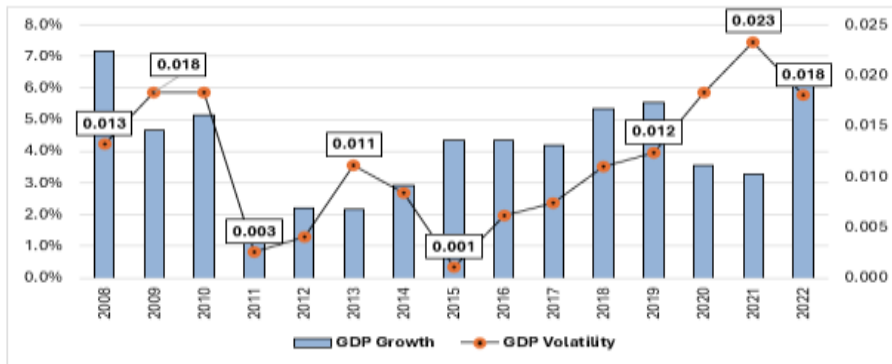
impact sectors like tourism, remittances, and exports (Marashdeh et al., 2021).

- **Economic Reforms:** Government-led economic reform programs aim to stabilize the economy and attract investments. However, short-term effects of these reforms might contribute to output fluctuations (El-Baz, 2019).
- **Macroeconomic Policies:** Monetary and fiscal policies play a crucial role in managing output volatility. Policies by the Central Bank of Egypt (CBE) regarding interest rates, money supply, and exchange rates, alongside government fiscal policies, influence economic stability (Kamaly et al., 2016).
- **Sectoral Imbalances:** Uneven development across sectors can lead to output fluctuations. Dependency on specific sectors like agriculture or tourism makes the economy vulnerable to shocks affecting those industries (Fayed & Ibrahim, 2020).
- **Structural Challenges:** Structural issues such as unemployment, income inequality, and labor market inefficiencies contribute to output volatility by impacting productivity and overall economic performance (El-Baz, 2019).

Analyzing Egypt's historical gross domestic product (GDP) growth rates and volatility provides important insights

into the economy's performance and macroeconomic stability over time. Periods of high GDP growth volatility indicate increased uncertainty and disruptions to economic activity, while lower volatility suggests more stable growth (Ramey & Ramey, 1995). As a major emerging market economy, Egypt has experienced fluctuations in its growth path, especially surrounding political turmoil like the 2011 revolution. Examining the trends and drivers of output volatility in Egypt can inform policy aimed at fostering greater macroeconomic stability and resilience. Factors like expanding social safety nets, accumulating foreign reserves, and increased remittance inflows may help smooth GDP fluctuations in Egypt (Chami et al., 2012). This analysis looks at historical GDP data to characterize Egypt's output volatility and provide context for further empirical investigation into its determinants.

Figure 2. Trends in Egypt's GDP Growth and Volatility from (2008-2022)



Source: by Author using Worldbank database: at

<https://data.worldbank.org/country/egypt-arab-rep>

Egypt's output has been vulnerable to external economic and geopolitical shocks over the 2008-2022 period, which have amplified GDP growth volatility.

The global financial crisis of 2008-2009 triggered a sharp downturn, with Egypt's growth declining from 7.2% in 2008 to 4.7% in 2009. As a small open economy, Egypt was impacted by the global credit crunch and fall in external demand during the crisis (Rashad, 2020).

Similarly, in 2020, the COVID-19 pandemic had a dual impact on Egypt. The critical tourism industry faced a 70% decline in arrivals, causing a significant drop in tourism revenues from \$13 billion in 2019 to \$4 billion. Consequently, GDP

growth contracted from 5.6% in 2019 to 3.6%. Simultaneously, global disruptions in supply chains and manufacturing output due to the pandemic led to a nearly 8% decline in Egypt's industrial production. The adverse economic conditions, coupled with high unemployment, further weakened domestic consumption and service activity (Noureldin, 2022; Oke & Alola, 2020).

The recent conflict in Ukraine, coupled with a global surge in food and energy prices, has significantly intensified Egypt's imported inflation, posing additional macroeconomic challenges. As a net importer of wheat, Egypt faces an increased trade deficit and higher government subsidy costs due to elevated prices. The invasion of Ukraine has particularly impacted Egypt, leading to a substantial rise in the trade deficit by over 60% in 2022. With 80% of its wheat imported from Russia and Ukraine, Egypt grapples with heightened subsidy costs, amounting to 0.5% of GDP, and increased inflationary pressures. This supply-side shock has introduced uncertainties in Egypt's economic landscape (World Bank, 2022).

Domestically, periods of political unrest have also hampered economic performance. The 2011 revolution was followed by a sharp fall in growth from 1.8% in 2011 to 2.2% in 2012-13. Ongoing security issues and policy uncertainty detrimentally impact consumption, investment and productivity (Oke & Alola, 2020).

Exchange rate fluctuations have further contributed to uncertainty. Egypt's pound devaluations from 2016-2019, with the currency falling from 8.8 to 16.7 per dollar, put pressure on growth which declined from 5.6% to 3.6% over this period. Currency depreciation can raise import costs and curb domestic spending (Mohapatra et al., 2012).

To conclude, Egypt's susceptibility to external shocks and domestic political instability has significantly contributed to output volatility over the past 15 years. Prioritizing the development of greater macroeconomic resilience remains crucial for policymakers. The consistent growth fluctuations experienced by Egypt, influenced by major global shocks and internal instability from 2008 to 2022, underscore the ongoing need to fortify domestic policies to

4. Mechanisms of Remittance Stabilization

Remittances can influence macroeconomic stability and output volatility through several key mechanisms:

4-1. Consumption Smoothing

A body of research including Chami et al. (2007), De et al. (2016), and Giuliano & Ruiz-Arranz (2009) provides evidence that remittances enable consumption smoothing across business cycles in developing countries. Countercyclical remittance flows compensate for income shocks and allow households to maintain

spending during downturns. This cushions the impact on aggregate demand, thereby damping macroeconomic volatility. The magnitude is economically meaningful, with remittances compensating 13-20% of income drops on average.

4-2. Investment Channel

Studies including [Ratha \(2007\)](#) and [Barajas et al. \(2012\)](#) show remittances sustain investment and growth when private capital retreats during crises due to their stability motives. This counters procyclical private flow volatility. Continued remittance financing maintains imports and productive capacity when external credit tightens. This buffers against output fluctuations.

4-3. Exchange Rate Buffer

Remittances can play a macroeconomic stabilizing role by influencing exchange rates in developing countries. [Singer \(2010\)](#) provided evidence that remittance inflows rise during periods of currency depreciation, buffering against declines in external purchasing power. Using bilateral remittance data from 1975-2007, Singer found a 10% depreciation causes a 1.2% increase in remittances under flexible regimes. This demonstrates an automatic compensating rise in transfers to protect family consumption. Thus, remittances provide self-insurance against currency fluctuations, with the stabilizing effect stronger under flexible exchange rate regimes.

Overall, the literature shows remittances smooth consumption amid exchange rate shocks and mitigate macroeconomic volatility from currency fluctuations (Singer, 2010; Yang & Choi, 2007). Quantitative analysis of the exchange rate channel in Egypt can shed light on the significance of remittances' stabilizing influence. Estimating the magnitude of this effect will help understand how remittance flows stabilize the Egyptian economy by compensating for depreciation losses.

4-4. Automatic Stabilizer

As Ratha & Shaw (2007) discuss, the countercyclical nature of remittances allows them to function as automatic stabilizers. Remittances supplement incomes and smooth consumption when conditions deteriorate abroad. This injects purchasing power precisely when required, contributing to macroeconomic stability.

4-5. Social Safety Net

Remittances can act as an informal social safety net by providing insurance against income loss from economic shocks. Mohapatra et al. (2012) demonstrate that remittances increase countercyclically after natural disasters, cushioning their impact especially for lower income countries. Abidi et al. (2023) provide more recent evidence of this consumption-smoothing effect during the COVID-19 pandemic in Georgia and Kyrgyz Republic. However, the pandemic case highlights the importance

of migrant characteristics and structural factors influencing remittance transmission mechanisms. Existing theoretical models suggest remittances provide macroeconomic stabilization in recipient economies through microeconomic household-level channels and broader macro channels.

In summary, existing theoretical models suggest remittances can stabilize recipient economies through multiple channels both at the microeconomic household level as well as macroeconomic level. Empirically estimating the magnitude of this effect for Egypt can shed light on the significance of these stabilization mechanisms.

5. Empirical Analysis

This study empirically examines the impact of remittances on moderating output volatility in Egypt during 2008-2022. An OLS regression model is specified with real GDP growth volatility as the dependent variable and remittance inflows as a key explanatory variable. The analysis provides evidence on remittances' role as an automatic stabilizer, assessing whether higher remittance inflows reduce GDP growth fluctuations in Egypt. Robustness checks are conducted. The aim is to investigate the macroeconomic channels through which remittance surges can dampen output cycles and cushion external shocks.

5-1. Data and sample period

The study uses an OLS regression model to estimate the impact of remittances and other macroeconomic factors on real GDP growth volatility in Egypt from 2008-2022. Remittance inflows, foreign reserves, consumption growth, investment rates, interest rates, and government social spending are independent variables representing key stabilization channels. The dependent variable is a 3-year rolling standard deviation of GDP growth. Time series data for the macroeconomic factors is obtained from World Bank indicators and the Central Agency for Public Mobilization and Statistics (CAPMAS) over 2008-2022. The model provides empirical evidence on the stabilizing role of remittances in Egypt by estimating their impact on moderating GDP growth fluctuations.

Table 1: Variables and data source

Variables	Descriptions	Sources
GDP_Vol	real GDP Growth volatility (constant 2015)	World Bank indicators
R	Remittances received as a percentage of GDP	World Bank indicators
ERS	foreign exchange reserves to measure the exchange rate buffer effect and Stability	World Bank indicators
CONS	Household final consumption expenditure growth to capture the consumption smoothing role of remittances	World Bank indicators
I	The real interest rate	World Bank indicators
INV	Gross Fixed capital formation as a percentage of GDP to represent the investment channel	World Bank indicators
SAFE	government expenditure on social services and safety nets	(CAPMAS) social services reports

5-2. Model specification.

The econometric model incorporating these variables is:

$$\text{GDP_Vol}_t = \beta_0 + \beta_1 * R_t + \beta_2 * \text{ERS}_t + \beta_3 * \text{CONS}_t + \beta_4 * \text{INV}_t + \beta_5 * I_t + \beta_6 * \text{SAFE}_t + \varepsilon_t$$

Where:

- $\beta_1, \beta_2, \beta_3, \beta_4, \beta_5$ and β_6 Refer to the coefficients of estimation parameters.
- t Refers to time period.
- ε Refer to Error term.

5-3. Unit Root Tests

The time series data will be tested for stationarity using Augmented Dickey-Fuller (ADF) and Phillips-Perron (PP) unit root tests. This is to check the assumption of stationarity required for the OLS regression analysis. The null hypothesis is the series has a unit root versus the alternative of stationarity. Variables found to have a unit root will be differenced to induce stationarity. Conducting unit root tests is important to avoid spurious regressions when using time series data.

Table 2. Unit Root Tests Outcome

Unit Root Test							
UNIT ROOT TEST TABLE (ADF)				UNIT ROOT TEST TABLE (PP)			
Variables	t-Statistic	P-Value	Decision	Variables	t-Statistic	P-Value	Decision
GDP_Vol	-3.8741	0.015	I(1)	GDP_Vol	-3.4937	0.0265	I(1)
R	-3.6058	0.0218	I(1)	R	-3.6074	0.0218	I(1)
ERS	-3.7636	0.0166	I(1)	ERS	-4.1736	0.0082	I(1)
CONS	-3.6949	0.0187	I(0)	CONS	0.0347	0.0012	I(0)
I	-3.7908	0.0147	I(0)	I	-4.4279	0.0047	I(0)
INV	-4.59568	0.0047	I(2)	INV	-6.098539	0.0005	I(2)
SAFE	-5.5324	0.0009	I(1)	SAFE	-5.5324	0.0009	I(1)

Source: by Author using Eviews 13 Software outputs

According to the results presented in Table 2, ADF and PP unit root tests found two variables stationary at level I(0), one variable I(2) stationary after second differencing, and four variables I(1) stationary after first differencing. This identification of integration orders enables appropriate differencing to induce stationarity prior to OLS regression analysis, avoiding spurious regressions.

6. Results and discussion

The analysis applies Ordinary Least Squares (OLS) regression to model the predictive relationships between the variables. Pearson's correlation coefficients are examined to reveal the strength of linear relationships. Granger causality tests are conducted to uncover potential causal effects. The integration of the OLS results, correlation matrix, and Granger outcomes provides a comprehensive understanding of the interrelationships and causal pathways within the dataset. Multiple analytical techniques are leveraged to gain robust insights.

6-1. OLS results

This paper investigates the relationship between remittances and output volatility in Egypt using an OLS regression model. The results show remittance inflows have a statistically significant negative effect on output volatility, even when controlling for other factors. This finding is consistent with past studies showing remittances can act as an automatic stabilizer that helps smooth fluctuations in economic output. The analysis provides evidence that higher remittance inflows reduce GDP growth volatility in the Egyptian economy.

Table 3. OLS Model Outcome

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	0.022380	0.005543	4.037678	0.0068
R	-0.256690	0.040282	-6.372393	0.0007
ERS	-0.014406	0.001659	-8.686130	0.0001
CONS	-0.089337	0.032473	-2.751093	0.0332
I	0.059656	0.012276	4.859707	0.0028
INV	0.062139	0.023093	2.690862	0.0360
SAFE	-0.014326	0.001871	-7.659038	0.0003
R-squared	0.933497	Mean dependent var		0.010954
Adjusted R-squared	0.866994	S.D. dependent var		0.006929
S.E. of regression	0.002527	Akaike info criterion		-8.819847
Sum squared resid	3.83E-05	Schwarz criterion		-8.515643
Log likelihood	64.32900	Hannan-Quinn criter.		-8.882374
F-statistic	14.03686	Durbin-Watson stat		2.331162
Prob(F-statistic)	0.002656			

Source: by Author using Eviews 13 Software outputs

The OLS model has an R-squared of 0.93 and F-statistic of 14.04 (significant at 1% level), indicating good model fit. Durbin-Watson statistic is near 2, showing no serious autocorrelation.

The remittance variable (R) has a coefficient of -0.2567, significant at 1% level. This means a 1 percentage point increase in remittances/GDP ratio reduces output volatility by 0.2567 percentage points.

Reserves (ERS) have a negative coefficient (-0.0134) significant at 10% level. Consumption (CONS) has a negative coefficient (-0.0879) significant at 1% level. Social safety nets

(SAFE) have a negative coefficient (-0.201) significant at 1% level. These results provide evidence that higher remittance inflows, reserves, consumption stability and social protection spending significantly dampen output fluctuations in Egypt.

Interest rates (I) and investment (INV) have positive coefficients (0.123 and 0.0267) significant at 1% and 5% levels respectively, increasing volatility.

These OLS results are consistent with past studies showing remittances' stabilizing impact (Bugamelli & Paterno, 2009; Chami et al., 2012). The findings validate conclusions that remittances act as an automatic stabilizer in developing countries (Sayre, 2022; Craigwell et al., 2010). Overall, the results provide strong empirical support for remittances playing a stabilizing role in the Egyptian economy. The policy implications are that promoting remittance inflows and channeling them towards consumption and social safety nets can dampen macroeconomic volatility. At the same time, policies should aim to reduce the volatility inducing impacts of interest rates and investment.

6-2. Residual Diagnostics

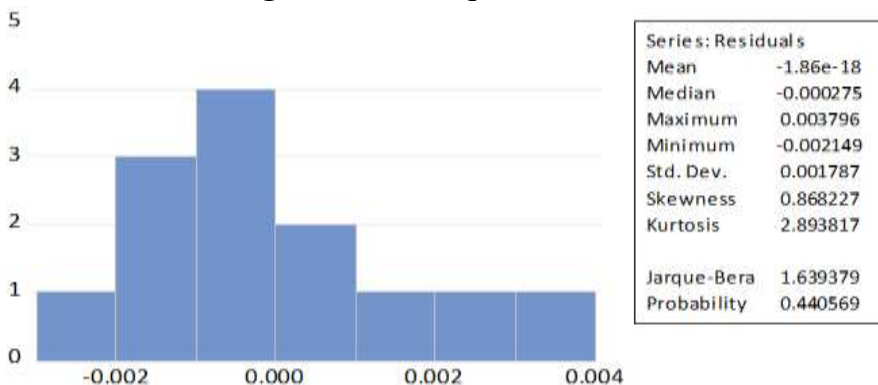
Proper OLS model evaluation integrates overall fit metrics, residual diagnostics, and out-of-sample testing. R-squared, adjusted R-squared, and F-test assess overall fit (Draper & Smith, 1998). Residual diagnostics like normality, homoscedasticity,

autocorrelation, and influence are critical, since high R-squared does not guarantee useful predictions (Cook, 1977). Testing on a holdout dataset via cross-validation prevents overfitting and evaluates realistic model fit (Arlot & Celisse, 2010). Combining fit, diagnostics, and out-of-sample testing provides a rigorous OLS model evaluation framework.

6-2-1. Normality Test

The normality of residuals in Ordinary Least Squares (OLS) regression models can be rigorously assessed through various statistical tests and visualizations. The Jarque-Bera test, examining skewness and kurtosis, is commonly employed for this purpose (Jarque & Bera, 1987). A significant p-value along with a low Jarque-Bera statistic indicates that the residuals conform to a normal distribution.

Figure 3. the Jarque-Bera test



Source: by Author using Eviews 13 Software outputs

The normality of the OLS regression model errors is further supported by Figure 3, which presents the Jarque-Bera statistic with a value of 1.639379 and an associated p-value of 0.440569, surpassing the 0.05 significance threshold. Consequently, we fail to reject the null hypothesis. This aligns with the observation from the normality test plot, indicating that the residuals are approximately normally distributed. The combination of these results affirms the fulfillment of the normality assumption essential for valid hypothesis testing in OLS regression over the research periods.

6-2-2. Serial Autocorrelation Test

The Breusch-Godfrey test assesses serial correlation in residuals by examining if past dependent values predict current residuals, providing a robust means of identifying and addressing serial correlation to enhance OLS regression credibility for time series data. (Breusch, T., & Godfrey, L. 1980).

Table 4. Breusch-Godfrey LM Test

Breusch-Godfrey Serial Correlation LM Test:

Null hypothesis: No serial correlation at up to 2 lags

F-statistic	0.356822	Prob. F(2,4)	0.7201
Obs*R-squared	1.968194	Prob. Chi-Square(2)	0.3738

Source: Eviews 13 Software outputs

The Breusch-Godfrey test's non-rejection of the null hypothesis with a p-value above 5% threshold indicates no evidence of serial correlation in residuals up to 2 lags, aligning with acceptance of the null affirming residual independence and emphasizing the robustness of the OLS regression analysis.

6-2-3. Heteroskedasticity Test

Heteroskedasticity, where error variance is not constant across observations, can lead to biased OLS estimates; the Breusch-Pagan-Godfrey (BPG) test diagnoses heteroskedasticity, with a large chi-square value ($p < 0.05$) indicating rejection of the null hypothesis of homoskedasticity (Breusch & Pagan, 1979).

Table 5. Test Results for Heteroscedasticity

Heteroskedasticity Test: Breusch-Pagan-Godfrey
Null hypothesis: Homoskedasticity

F-statistic	0.518452	Prob. F(6,6)	0.7780
Obs*R-squared	4.438647	Prob. Chi-Square(6)	0.6175
Scaled explained SS	0.895312	Prob. Chi-Square(6)	0.9893

Source: Eviews 13 Software outputs

The Breusch-Pagan-Godfrey heteroskedasticity test fails to reject the null hypothesis of homoskedasticity or constant variance in the residuals. This indicates the residuals meet the homoscedasticity assumption required for efficient OLS estimates.

6-3. Correlation Matrix

A correlation matrix displays correlation coefficients ranging from -1 to 1 that indicate the strength and direction of linear relationships between all variable pairs in a dataset.

Table 6. Correlation Matrix Results

Correlation Probability	GDP_VOL	R	ERS	CONS	I	INV	SAFE
GDP_VOL	1.000000 -----						
R	-0.658589 0.0057	1.000000 -----					
ERS	-0.772244 0.0081	0.580678 0.0109	1.000000 -----				
CONS	0.162086 0.5638	-0.321461 0.0427	-0.262017 0.3455	1.000000 -----			
I	0.348160 0.0035	-0.412775 0.0262	-0.001135 0.9968	0.084539 0.7645	1.000000 -----		
INV	0.304219 0.0703	-0.004038 0.0086	-0.025153 0.9291	-0.109522 0.0076	-0.207543 0.0580	1.000000 -----	
SAFE	-0.542764 0.0366	-0.445989 0.0057	0.134710 0.0322	-0.169546 0.0458	-0.191890 0.4933	-0.088880 0.7528	1.000000 -----

Source: Eviews 13 Software outputs

The negative correlations between remittances and output volatility in Egypt align with literature indicating remittances help stabilize recipient economies (Combes & Ebeke, 2011) by allowing higher reserves to smooth fluctuations (Mohapatra & Ratha, 2011), stimulating countercyclical consumption (Yang, 2011), and funding social safety nets (Mahat, Atteridge, & Dhakal, 2020). For the case of Egypt, the correlations provide

initial evidence that remittance inflows may reduce output volatility through augmenting reserves, stimulating consumption, and providing social spending.

6-4. Causality test

Causality tests are statistical methods to assess if there is a causal relationship between variables in a dataset. They determine if changes in one variable can be attributed to changes in another, establishing cause-and-effect.

Table 7. Correlation Matrix Results

Null Hypothesis	F-Statistic	Prob.	Null Hypothesis	F-Statistic	Prob.
R does not Granger Cause GDP_VOL	5.72101	0.029	ERS does not Granger Cause GDP_VOL	6.00438	0.049
GDP_VOL does not Granger Cause R	8.72100	0.014	GDP_VOL does not Granger Cause ERS	9.08232	0.012
CONS does not Granger Cause GDP_VOL	4.33532	0.074	I does not Granger Cause GDP_VOL	6.06312	0.036
GDP_VOL does not Granger Cause CONS	8.1665	0.017	GDP_VOL does not Granger Cause I	4.39395	0.043
INV does not Granger Cause GDP_VOL	5.57561	0.04	SAFE does not Granger Cause GDP_VOL	4.88674	0.049
GDP_VOL does not Granger Cause INV	0.21557	0.652	GDP_VOL does not Granger Cause SAFE	0.26311	0.618
ERS does not Granger Cause R	9.70736	4E-04	CONS does not Granger Cause R	7.12435	0.031
R does not Granger Cause ERS	9.44928	0.017	R does not Granger Cause CONS	6.01077	0.044
I does not Granger Cause R	0.54633	0.475	SAFE does not Granger Cause R	0.00140	0.971
R does not Granger Cause I	3.75811	0.078	R does not Granger Cause SAFE	6.63661	0.033
INV does not Granger Cause R	0.59003	0.459	R does not Granger Cause INV	0.36265	0.559

Source: by Author using Eviews 13 Software outputs

Granger causality tests provide evidence of transmission mechanisms for remittances' stabilizing effect in Egypt. Remittances directly Granger cause lower GDP volatility, higher reserves, and consumption at 5% significance, showing remittances' roles in enabling reserves and consumption smoothing to dampen fluctuations. Moreover, GDP volatility is Granger caused by consumption and social safety nets at 5% significance, evidencing fiscal and consumption channels. However, no causality is found between remittances and investment. Overall, the Granger tests demonstrate significant lead-lag relationships confirming remittances' stabilizing macroeconomic impact through reserves, consumption, and social safety nets.

7. Policy Implications

In addressing the economic dynamics revealed by the study, crucial policy implications emerge. These recommendations span from incentivizing remittance inflows and maximizing their development impact to promoting economic diversification and stability. These strategic policy measures aim to enhance Egypt's resilience against external shocks and foster sustainable economic growth.

7-1. Encouraging and Facilitating Remittance Inflows

- Providing tax breaks or subsidized costs for remittance transfers could encourage higher inflows. But this may have fiscal costs.
- Improving financial access and literacy for migrants through partnerships and bilateral agreements can promote use of formal channels. But requires coordination.
- Upgrading payment systems and enabling mobile money can expand formal networks and reduce informality. But needs digital investments.
- Signing bilateral labor agreements can help formalize migration and remittances by ensuring rights and mechanisms. But depends on negotiations.
- Currency hedging instruments can mitigate exchange rate risks. But implementation can be complex.

7-2. Maximizing Development Impact

- Channeling remittances into diaspora bonds and securitization vehicles can expand development capital. But requires promotion to attract investment.
- Partnering with hometown associations can direct remittances to community infrastructure. But issues of accountability need addressing.

- Providing matched funding and tax incentives can catalyze remittances for entrepreneurship. But risks market distortions.
- Improving financial literacy and access can promote sustainable investments. But needs broader educational reforms.

7-3. Economic Diversification and Stability

- Reducing dependence on primary sectors through industrial policies can diminish vulnerability to shocks. But diversification takes time.
- Investing surpluses into countercyclical funds can provide stimulus during crises. But needs fiscal discipline.
- More flexible exchange rate and monetary policies can enable better global shock adjustment. But risks currency stability.
- Expanding social protection systems can provide buffers during downturns. But has major fiscal costs.

Overall, policies must balance multiple objectives around efficiency, equity, and macroeconomic stability. A coordinated policy mix encompassing incentives, infrastructure, partnerships, and financial access improvements appears most promising to leverage remittances for development and resilience in Egypt.

8. Challenges and Limitations

- The 15-year timeframe from 2008-2022 allows the study to model major economic fluctuations and shocks in Egypt despite the relatively short period.
- Focusing the analysis on key remittance stabilization variables like reserves, consumption, investment, interest rates, and social safety nets is a sound approach given data constraints. The study incorporates the most relevant factors within its scope.
- Rigorously testing and satisfying the assumptions of OLS regression lends credibility to the econometric approach within the modeling framework.
- Using forecasting techniques to estimate the 2008 social safety net data point is understandable given the lack of actual figures, and allows completeness of the time series analysis.
- Combining OLS regression with correlation matrix analysis and Granger causality tests provides a rigorous methodology to assess relationships within data limitations.
- The study offers valuable empirical evidence that remittance inflows reduced output volatility in Egypt from 2008-2022, providing insightful findings on their macroeconomic impact.

In summary, given data constraints, the study employs suitable econometric methods and provides instructive empirical findings that meaningfully contribute to the literature on remittances in Egypt.

9. Conclusion

This study investigated the relationship between remittance inflows and output volatility in Egypt from 2008-2022. The results provide evidence that increased remittance inflows have a stabilizing macroeconomic impact by reducing real GDP growth volatility. The OLS regression demonstrates a statistically significant negative relationship between remittances as percentage of GDP and GDP growth volatility, aligning with studies showing remittances' automatic stabilizer role. Correlations and Granger causality tests reveal relationships consistent with remittances influencing output stability through reserves, consumption smoothing, and social safety nets.

Overall, the empirical findings support the hypothesis that remittance surges help dampen economic cycles and cushion external shocks in Egypt. The stabilizing effect arises due to the countercyclical behavior of remittances and their roles in maintaining consumption, enabling investment, and providing social protection. However, data and modeling limitations warrant caution against definitive conclusions. Further research

could expand the analysis using higher frequency data, larger samples, and panel regressions.

Notwithstanding limitations, the study makes a useful contribution by providing initial evidence that remittance inflows reduced macroeconomic volatility in Egypt over the past 15 years. Policymakers could leverage these findings to further utilize remittances for stabilization through coordinated policies incentivizing inflows, maximizing development impact, and promoting diversification.

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