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DETERMINANTS OF REMITTANCES: THE CASE OF KOSOVO

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Abstract

What drives remittances is one of the most important questions in the migration literature. However, there is no systematic theory that explains such behaviour and the statistical evidence is scarce, especially for the case of Kosovo. Using the data from a survey conducted in Kosovo in 2006, this paper is an attempt to find the main determinants of remittances. The results suggest that, among others, the motive to invest and perceptions about the business environment are significant determinants of remittances. Testing the link maintenance theory through the migration duration, the results also suggest that remittances grow at a decreasing rate and the evidence for the aspirations to inherit assets in home country exists and affect remittances positively. These findings show that there is room for policy-makers to improve the business environment by investing in infrastructure, fight corruption, etc., which would affect perceptions of migrants and, hence, increase intentions to remit more.

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I. Introduction

Kosovo migration was caused by both, political and economic reasons. Some estimates show that the current number of migrants is around 20 percent of total population (Bush 2006, Riinvest 2007). The surge of migration from Kosovo was recorded in 1990s with more than 60 percent of migrants migrating in that period, especially during the war in 1998-1999. This wave of migration was caused by the systematic repression from the Serbian regime and a large number of Kosovar refugees were settled in high-income countries of Western Europe and in the U.S. In addition, due to the differences in income, migration was a solution to economic problems for many in Kosovo – a country with the rate of unemployment at around 40 percent – and a significant number of migrants have not returned to their home country ever since. For example, around 30 percent households living in Kosovo are willing to consider migration for economic reasons. The migration on a such large scale enables a relatively large inflow of remittances, which is a very important source of income for the economy of Kosovo. For instance, the inflow of remittances in Kosovo was euro 535 million in 2008 (CBK 2008), which accounts for 14.1 percent of GDP, making Kosovo one of the largest recipients of remittances in the region (Albania 12.8 percent of GDP, Bosnia and Herzegovina 17.0 percent of GDP, Macedonia 4.0 percent of GDP, Serbia 11.8 percent of GDP). However, almost half of remittances are sent through informal channels and policies aiming at identifying incentives of migrants to remit more and channelling remittances through formal channels are important questions for investigation.

What are the motives to remit is the most common question in the migration literature. However, there is no systematic theory that explains such behaviour and the evidence is scarce. This paper tries to fill the gap in the empirical literature, especially for the case of Kosovo, by providing evidence on the main determinants of remittances. Based on the findings, some policy recommendations are derived which may contribute in attracting higher inflows of remittances, especially through formal channels.

The paper is organized as follows. In the next section, the review of theories and empirical work on the motives to remit is provided. Section III describes the data and the methodology used in this study. The regression results are presented in Section IV. Conclusions and some policy recommendations are derived in Section V.

II. Review of theory and evidence

Migration itself is viewed as a strategy of a household to minimize the income risk or a strategy of an individual to maximize income (Garip, 2006). If the argument of minimizing the income risk holds, then it is expected that migrants will remit relatively more. On the other hand, if the income-maximization strategy of an individual holds, migrants will be motivated to remit less. The main theories on motives to remit can be listed as follows:

- a) Altruistic motive
- b) Inheritance-seeking motive
- c) Maintaining links and intentions to return motive
- d) Investment motive
- e) Loan repayment motive

Altruistic motive hypothesis claims that migrants enjoy sending money to their relatives in their country of origin by valuing both, their own utility and the utility of their relatives in home country (Lucas and Stark 1985, Rapoport and Docquier 2005). Funkhouser (1995) in his behavioural model of remittances suggests five testable implications under the altruistic assumption: (i) migrants with higher earnings potential (e.g., higher human capital and/or work status) will tend to remit more; (ii) households with lower income will receive more remittances; (iii) remittances depend on the migrants' marital status – remittances will tend to increase if the migrant is married and his spouse and/or children are in the country of origin. As a corollary, intentions to return are positively related with the tendency to remit more; (iv) the amount that migrant sends to relatives in home country is negatively related to the number of migrants from the same household; and (v) the time profile of remittances depends on the relative size of discount factors and the earning profile of the migrant, e.g., migrants who stay longer abroad tend to remit at a decreasing rate due to weakened links with relatives in host country. Related to these testable implications, Funkhouser (1995) finds that migrants who have relatives in their home country remit more and remittances increase at a decreasing rate, consistent with the testable implication (v) which suggests that the time profile of remittances depends on the relative size of discount factors, in this case, years since migration. In addition to this, Holst and Schrooten (2000) find that remittances are positively related with income, while the number of

dependants in host country affects remittances adversely. These findings are consistent with Funkhouser's testable implications of altruism.

Bulk of theoretical work suggests that the altruistic motive is among the most important factors driving remittances. However, empirical evidence does not support this assertion always, given problems in measuring the altruism. In addition, theory recognizes altruism as the motive that leads to stable remittances over time (Bougha-Hagbe 2006). As there is no direct measure for altruism, indirect measures could be used as a proxy. For instance, the level of income and the number of dependants and relatives in home country could impact the altruism of the migrant towards households. Furthermore, despite the distinct theoretical background between the link maintenance and altruism, the first could be related to the altruism of the migrant towards relatives in home country, that is, weaker links with households in home country decreases the altruism of the migrant towards households.

Migrants driven by the *inheritance motive* send remittances to support their families in order to ensure the right of inheriting assets in their country of origin. This is often called the self-interest motive. Under this hypothesis, remitters are expected to have a higher chance to inherit assets, whereas the higher the value of assets to be inherited is likely to be associated with the higher remittances. For instance, Osili (2004) finds that migrants remit more in wealthier areas. Similar findings can be found in, Hoddinot (1994), de la Briere et al (1997), Chavez (2004) and Schreider and Kneerr (2000). In addition, bulk of the literature found that male emigrants remit significantly more compared to female emigrants and this may be considered as the inheritance seeking motive (Garip 2006, Holst and Schrooten 2006).

Maintaining links theory implies that migrants are likely to remit when they are willing to return in their country of origin. They send remittances so that they can show their intentions to return and to maintain links with their family. This behaviour possibly generates investments from migrants, such as buying a house or investing in a business. However, the pure reason why this group of self-interest migrants sends remittances is to "buy" what Lucas and Stark (1985) called the social assets – the relationship with their family members and friends. Using a gravity model with macroeconomic variables, most of the variation in remittances can be explained by the distance between home and host country. For example, Leuth and Ruiz-Arranz 2006 find that the distance is negatively related to remittances. In addition to distance, another measure which

possibly can capture the effect of links between migrant and households in home country is the years spent in migration. Literature is mixed regarding this measure, some of them finding only positive relationship when measured in terms of the level of remittances, e.g., Durdand et al. (1996), Guber (2002). Using probability models, the positive relationship between years since migration and remittances is found by Agarwal and Horowitz (2002), Konica (2006), etc. However, some of these studies suggest that the impact of years since migration on remittances is positive, nevertheless, at decreasing rate (inverse-U-shaped function). Distance between the home and host country and years since migration have a negative effect on intentions to return, and hence on remittances, as a result of weakening links. Consequently, the distance and the years spent in migration may lower the remittances sent to household in home country. This is because migrants may establish their new social environment, which would decrease their intentions to return as well as weaken the links with their relatives in home country.

Investment theory of remittances claims that migrants who seek investments and whose perceptions about the business environment in their country of origin are favourable will remit more, as they plan or already have undertaken an investment; hence, migrants' motive to remit is driven by the incentives to secure assets that they have invested or plan to invest in future (Lucas and Stark, 1985). Related to this, Garip (2006) found that investment environment in home country plays an important role for the decision to remit and the amount of remittances. If the business environment is considered by the migrant as favourable, the amount of remittances is expected to be higher.

Loan repayment motive is another explanation why migrants remit. Under this theory migrants send remittances to repay their previous implicit loans from their families for expenses in education, financing migration, etc. Under this assumption, educated migrants are likely to be those that remit more. For instance, Hoddinot (1994), Ilahi and Jafarey (1999) found that education of migrant and the amount remitted are positively correlated.

III. The data and methodology

The data used in this study are from the Riinvest Institute survey conducted with migrants in Kosovo in 2006. Riinvest Migrant Survey (RMS), among others, asked migrants whether they remit or not, the amount of remittances, the frequency of sending money, etc. In the RMS sample, around 14 percent of migrants did not remit. Other variables that will be used in this study consist of data on personal characteristics such as age of the head-household of migrant family, gender, education level (measured by years of schooling) and marital status of the migrant. In addition to the personal characteristics, other variables such as the perceptions of the migrant about the business environment in Kosovo, whether the migrant has undertaken an investment in Kosovo, the family earnings and years since migration are to be included in this study. Furthermore, the geographical distance between Kosovo and countries where migrants are settled will be included in the model as well as if the migrant has close relatives and dependants living in Kosovo. The model will also have the location that migrant lived prior to migration, that is, urban or rural. Table 1 summarizes the descriptive statistics. As it can be observed, there is enough variation among the data.

Table 1: Summary statistics

Variable		<i>Obs</i>	<i>Mean</i>	<i>Std. Dev.</i>	<i>Min</i>	<i>Max</i>
Monthly remittances/€	<i>Continuous</i>	1055	268.78	262.23	0	1250
Monthly earnings/€	<i>Continuous</i>	1048	2989.84	2737.942	550	17258
Age of migrant-HH	<i>Continuous</i>	1055	34.75	9.741	17	76
Gender of HH (male=1)	<i>Dummy</i>	1055	0.76	0.425	0	1
Years of schooling	<i>Continuous</i>	951	11.97	1.675	0	17
Perceived Business Environment	<i>Dummy</i>	1055	0.26	0.437	0	1
Investment (yes=1)	<i>Dummy</i>	1055	0.23	0.422	0	1
Married (yes=1)	<i>Dummy</i>	1055	0.78	0.414	0	1
Close relatives (yes=1)	<i>Dummy</i>	1055	0.74	0.44	0	1
Distance of Home and Host country	<i>Continuous</i>	1054	1357.69	1074.899	527	7800
Dependents in Kosovo	<i>Continuous</i>	1055	0.35	1.089	0	9
Location (urban=1)	<i>Dummy</i>	1055	0.41	0.492	0	1
Years since migration	<i>Continuous</i>	720	8.56	3.965	1	28

The general model that will be used to examine the determinants of remittances for the case of Kosovo is:

$$\begin{aligned} R = & \beta_0 + \beta_1 Y + \beta_2 Age + \beta_3 Sch + \beta_4 Be + \beta_5 Inv \\ & + \beta_6 M + \beta_7 Dep + \beta_8 Cr + \beta_9 YSM + \beta_{10} G \\ & + \beta_{11} L + \beta_{12} D + \beta_{13} Age^2 + \beta_{14} YSM^2 + ui \end{aligned}$$

where R is monthly amount of remittances sent by a migrant (in euros); Y represents the reported migrant income in euros. In addition, the model also includes the Age of the head-household migrant, Sch is years of schooling of the migrant; Be is migrant perceptions on the business environment in home country, taking value of one if favourable and 0 otherwise. Whether the migrant has invested in any property or business in Kosovo is also included in the model and depicted by the dummy variable Inv (if invested it equals 1 and zero otherwise). The marital status of the migrant is represented by the dummy variable M ; Dep for the number of dependents of the migrant (spouse and/or children) in their home country; Cr represents whether the migrant has other close relatives residing in the country of origin (dummy variable). YSM is the years since migration (migration duration). The gender of migrant is represented by G (male being base=1). Location (L) takes the value of 1 for urban migrants and 0 otherwise. The distance from home country is represented by D and measured by kilometres.

Determinants of the size of remittances will be estimated initially by OLS. The dependent variable in the OLS model will be the reported amount of remittances by migrants, in euros. However, there are around 14 percent of migrants that do not remit. Hence, estimating this model by OLS provides unbiased and consistent but not fully efficient estimates (Gujarati 2003). The best method to estimate the model is the Tobit corner solution response if normality assumption will hold (Wooldridge 2006). As the sign and significance of both methods should be comparable, both OLS and Tobit model will be estimated. As the dependent variable is left-censored, Tobit corner solution is another estimation method which will be used, while again in the Tobit model, the dependent variable will be as reported by migrants (in euros).

Another possible estimation method is the Probit model. In addition to estimating the probability of sending remittances by the migrant, Probit also will be used as a diagnostic test for the Tobit model. The Probit model is a bivariate model with a dummy dependent variable – those

who remit and those who do not remit. In addition, Ordered Probit model will be estimated to check for the robustness of the results.²

IV. Results

Four estimation techniques are used in estimating the model on the determinants of remittances, namely the OLS, Tobit, Probit and Ordered Probit. The normality test is crucial to interpret these results with Tobit estimation. When the normality test was performed by comparing the ratio of Tobit coefficient to the standard error of the regression with the coefficient of Probit ($\hat{\beta} / \hat{\sigma}$), it turned that such problem is not present, meaning that the results of Tobit estimation are unbiased and consistent. As expected, for the OLS model the data are non-normally distributed given that around 14 percent of migrants do not remit. However, the estimates of OLS regression under the normality problem are still unbiased and consistent, but not fully efficient (Wooldridge 2006). The explanatory variables are jointly significant in all estimation methods. The results of the models are presented in Table 2.

The age of a migrant has positive and significant effect on remittances at five percent level of significance. However, this seems to be at a decreasing rate as indicated by the negative coefficient of Age-squared. The inclusion of the age-squared is explained by the migration practice of the 90s. This is because at that time, most of the migrants were around 20-30 years old, and hence, it can be assumed that since then, different developments could have affected their lives (such as migration of other members of their family and in such cases one would expect lower amounts of remittances). Age is found by many authors to affect positively remittances, e.g., Gubert (2002), Konica (2006), Merkle and Zimmerman (1992), etc. The inclusion of years since migration (YSM) and its squared value, affected the significance of the variable Age and Age-squared turning them insignificant. This could have been caused by the multicollinearity between age and years since migration; however, dropping one of the variables

² The dependent variable for the Ordered Probit is defined as follows: at the category of zero are those migrants who do not send remittances. Category one consists of migrants who send less than 100 euros of monthly remittances. Three includes migrants who remit amounts between 100 and 500 euros, on monthly basis. Fourth category consists of migrants who send more than 500 and less than 1000 euro of remittances. The fifth category includes migrants who send between 2000 and 3000 euros of remittances, while the last category (sixth) includes migrants who send more than 3000 euros of remittances.

is not the best choice since different theories can be tested through age as well as through years since migration.

In line with expectations, income has a positive effect on the amount remitted at one percent level of significance. This is mostly in line with the previous empirical literature where almost all research papers having income as independent variable find it highly correlated to remittances. It is reasonable to suggest that the higher the income of the migrant, the higher the remittances will be since income itself generates potential to send remittances suggesting that income as a variable is related to all motives to remit.

Income has been found positively related to remittances in almost all studies on remittances. The gender is highly significant in all the models and male migrants remit more. This could be explained by inheritance-seeking motive as well as the selection of males for migration. This is based also in the culture and tradition in Kosovo which recognizes males as the inheritors of the family assets. This is also in line with findings from other studies such as Ameudo-Dorantes et al. (2006), Konica 2006, Merkle and Zimmerman 2006, Hoddinot 1994, where male migrants remit significantly more than female migrants and often is explained by the tradition in these countries recognizing males as inheritors. Despite its relation to the inheritance seeking aspirations, this behaviour could also be as a result of the selection of males to join labour force as well as to migrate. For instance, males in Kosovo compose around 70 percent of the labour force (SOK 2007), therefore, it is expected that males are selected to migrate at a higher rate compared to females.

Table 2: The Determinants of Remittances

Independent Variables	<i>Dependent variable Monthly Remittances</i>							
	<i>OLS</i>		<i>Tobit</i>		<i>Probit</i>		<i>Ordered Probit</i>	
	<i>(I)</i>	<i>(II)</i>	<i>(III)</i>	<i>(IV)</i>	<i>(V)</i>	<i>(VI)</i>	<i>(VII)</i>	<i>(VIII)</i>
Age	11.99** (2.43)	5.67 (0.97)	23.60*** (3.68)	15.49** (2.0)	0.107*** (3.2)	0.06 (1.49)	0.096*** (3.96)	0.06** (2.18)
Age ²	-0.16** (-2.68)	-0.075 (-1.04)	-0.33*** (-3.96)	-0.21** (-2.17)	-0.00146*** (-3.51)	-0.0009* (-1.74)	-0.001*** (-4.25)	-0.0009*** (-2.38)
Log-income	41.85*** (3.6)	46.28*** (3.41)	49.175*** (3.46)	58.125*** (3.47)	-0.017 (-0.2)	0.094 (0.9)	0.16*** (3.09)	0.21*** (3.18)
Gender (Male=1)	72.04*** (3.89)	61.86** (2.95)	102.31*** (4.45)	91.86*** (3.47)	0.3127** (2.54)	0.29* (1.94)	0.45*** (5.17)	0.43*** (4.1)
Years of Schooling	5.39 (1.16)	8.004 (1.47)	1.35 (0.24)	1.175 (0.17)	0.018 (0.57)	0.031 (0.73)	0.007 (0.34)	0.003 (0.14)
Perceived business environment (Favourable=1)	58.49*** (3.32)	90.65*** (4.52)	50.834** (2.37)	91.32*** (3.67)	0.29** (2.1)	0.55*** (2.82)	0.24*** (2.91)	0.40*** (4.02)
Investment (Yes=1)	38.77* (2.09)	40.03* (1.95)	72.24*** (3.23)	61.58*** (2.44)	0.44*** (2.75)	0.31* (1.64)	0.34*** (3.95)	0.31*** (3.04)
Marital status (Married=1)	18.75 (0.88)	15.52 (0.56)	23.807 (0.91)	15.65 (0.44)	0.33** (2.32)	0.28 (1.35)	0.12 (1.24)	0.06 (0.48)
Close relatives (Yes=1)	87.14*** (4.86)	101.9*** (4.97)	113.14*** (5.1)	112.25*** (4.37)	0.44*** (3.68)	0.57*** (3.74)	0.50*** (5.94)	0.52*** (5.02)
Distance between home and host country	-0.0051 (-0.70)	-0.014* (-1.88)	-0.002 (-0.23)	-0.012 (-1.28)	-7.3E-05* (-1.76)	-0.0001** (-2.38)	-2.3E-05 (-0.69)	-6.3E-05* (-1.66)
Number of dependants in home country	7.305 (1.03)	-8.905 (-0.84)	7.791 (0.9)	-12.55 (-0.95)	0.078 (1.11)	-0.02 (-0.26)	0.03 (0.98)	-0.03 (-0.66)
Location (urban=1)	-22.022 (-1.41)	-31.023* (-1.77)	-36.46* (-1.91)	-60.83*** (-2.79)	0.007 (0.06)	-0.22* (-1.62)	-0.09 (-1.34)	-0.2** (-2.3)
Years since migration		11.89* (1.77)		9.45 (1.13)		0.020 (0.39)		0.04 (1.16)
Years since migration ²		-0.82** (-2.5)		-0.725* (-1.79)		-0.0014 (-0.56)		-0.002* (-1.69)
Observations	932	633	945	646	945	646	945	646

Note: ***, **, * denote the level of significance at 1, 5 and 10 percent. T-Ratio and Z-statistics are shown in parenthesis.

Years of schooling has a statistical insignificant effect on remittances. An explanation may be that the education of migrants does not match the job requirements and the diplomas obtained in Kosovo are not recognized by host countries. The evidence on the impact of education on remittances is mixed. For example, Agarwal and Horowitz (2002), Hoddinot (1994) and Holst and Shrooten (2006) found a positive correlation; Osaki (2003) and Durand et al. (1996) found a negative correlation; while some studies found insignificant impact of education on remittances.

An important finding of this paper is that investments by migrants in Kosovo and their perceptions about the business environment are of high importance in determining the amount of remittances. If migrant perceptions about the business environment are favourable, it affects positively the amount of remittances. This may reflect future investment opportunities of migrants. The results also suggest that investment in any property or business by the migrant has a positive effect on the amount remitted at 10 percent level of significance. This evidence suggests that investment itself is also a generator of remittances. This is explained by the behaviour of migrant and households in home country. Households in home country are usually those who take care and ensure the investment of the migrant, as well as managing with the investment.

The dummy variable indicating that migrant has close relatives in home country is positive and highly significant at one percent level of significance. This variable can be a proxy to test the link maintenance theory and also can indicate the altruism of migrants towards members living in home country. The first indicates that migrants wish to maintain links to other members living in the home country, while the second motive can be explained by the utility of the migrant being affected by the utility of the members in home country. Another measure regarding the relation of migrant with relatives in home country is the number of dependants (children in our case) but it turned to be statistically insignificant. This also could have been due to multicollinearity between relatives and dependants. The coefficient of the distance between home and host country is statistically significant in the second specification and the overall effect on remittances is very low. This can be explained by the advances in technology for transferring remittances as well as communication from host to home countries and, hence, removing the impact of the distance in links maintenance.

Regarding the location prior to migration, the result suggests that migrants from rural areas remit more. For the case of Kosovo, this can be explained through the families in rural areas being more dependent on migrants. Rodriguez (1995) suggests that migrants from urban areas remit more due to higher living expenses of households in urban areas. However, population living in urban areas may have more opportunities, e.g., higher chances of getting a job. For the case of Kosovo, as results indicate, rural families are involved in agriculture not generating employment in Kosovo and, thus, are more dependent on remittances.

As expected, the effect of years since migration on remittances is positive at decreasing rate. Additional year on migration is positively related to remittances at 10 percent level of significance. This effect seems to be at a decreasing rate (inverse U-shaped function) indicated by the squared value of years since migration, suggesting that after some period of time, additional year affects remittances adversely. In other words, as the migrant gains more experience, he/she remits continuously more. However, at some point the migrant establishes social network in host country and the links of the migrant and intentions to return may weaken. At this point, remittances will start to decrease which is consistent with many studies, e.g., Benarjee (1984), Durand et al. (1996), etc.

V. Conclusions

This paper provides micro-level evidence on the determinants of remittances in Kosovo. The findings suggest income of the migrants affects remittances significantly. Furthermore, male migrants are found to remit significantly more than female migrants. Aspirations to inherit assets in the home country are another factor affecting remittances. Results suggest that education of migrant does not have an explanatory power for remittances. The perception of migrants about the business environment has a significant effect on the amount remitted and migrants' investments in the home country play a significant role on the amount remitted. In addition, the evidence supports the link maintenance theory in the cases when in home country the migrant has close relatives. As for the duration of stay, the findings suggest that the longer the stay abroad the higher the remittances are and this relationship is an inverse U-shape function consistent with the link maintenance theory. As for the distance, even though the coefficient is

statistically significant, its impact on remittances is very small. Related to location, the evidence suggests that rural migrants remit more.

Based on the findings, policies that can be addressed are, for instance, improvement of business environment in the country of origin, re-assessing taxation policies for migrant investments which would facilitate the capital inflow, new labour market experiences (brain gain) and new technologies. In addition, improving the infrastructure and fighting corruption may improve the perceptions of migrants about the business environment. Such policies would have important implications. First, for those having good perceptions about business conditions, it will be more likely to invest and also remit more. Second, such policies make it more likely that migrants will return in their home country for investing and bringing new technologies and experiences in Kosovo.

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