

4

REMITTANCES



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Introduction

Migrant economic remittances¹ are an important and growing source of foreign funds for several developing countries. At present, these flows are more than double the official aid received by developing countries. According to the World Bank and the IMF, if remittances sent through informal channels are included, total remittances could be as much as 50 percent higher than the official record (World Bank 2010, IMF 2009). In 2010, officially recorded remittances to developing countries reached \$334 billion (World Bank 2010).

For many developing countries, remittances constitute a large source of foreign income relative to other financial flows. In 2009, in some countries economic remittances have “become as large as foreign direct investment” and, in a large group of developing countries, remittances represent a resource inflow that often exceeds a variety of other balance of payments flows (IMF 2009).

Although remittances are accounted for as a component of PCF — unlike FDI and PI, which tend to be highly volatile — remittances are much more stable and even countercyclical in the face of external economic shocks (Mohapatra et al. 2010, UNESCAP 2007, Gabel 2008).

Moreover, since remittances are largely personal transactions from migrants to their friends and families, they tend to be well targeted to the needs of their recipients. Their ability to reduce poverty and to promote human development is well documented and often reported as beneficial to overall development: “Remittances directly augment the income of recipient households. In addition to providing financial resources for poor households, they affect poverty and welfare through indirect multiplier effects and also macroeconomic effects” (Ratha 2007).

Regression analyses across countries worldwide indeed show significant poverty reduction effects of remittances. For instance, household survey data show that remittances have reduced the poverty headcount ratio significantly in several LICs: by 11 percent in Uganda, 6 percent in Bangladesh and 5 percent in Ghana. In Nepal, remittances may explain a quarter to a half of the 11 percent reduction in the poverty head count ratio (Ratha 2007).

Furthermore, remittances have been associated with increased household investments in education, health and entrepreneurship — all of which have a high social return in most circumstances. For instance, studies based on household surveys in El Salvador and Sri Lanka find that children of remittance-receiving households have a lower school drop-out ratio and that these households spend more on private tuition for their children. In Sri Lanka, the children in remittance-receiving households have higher birthweight and studies also indicate that remittances provide capital to small entrepreneurs, reduce credit constraints, and increase entrepreneurship.

At the macro-economic level, the relationship between economic growth and remittance receipts has come under renewed scrutiny. Although the empirical evidence on the impact of remittances on economic growth appears to be mixed, it is nonetheless recognized that, since remittance flows are used either to increase consumption or investment, they have the potential to become an important tool for economic development (Fayissa and Nsiah 2008, UNESCAP 2007, Ratha 2007). More recently, it has been noted that “a significant portion of remittance flows are used to service debt, and increase foreign exchange reserves” (Das and Serieux 2010). In other words, such flows can also be used to cushion the impact of external economic shocks.



Given the size and stability of remittance inflows as well as their countercyclical behaviour in the face of external shocks, recent policy attention has focused on mobilizing remittances to leverage growth and poverty dividends as well as utilizing remittances to cushion the impact of economic shocks. Specifically, policy measures have focused on:

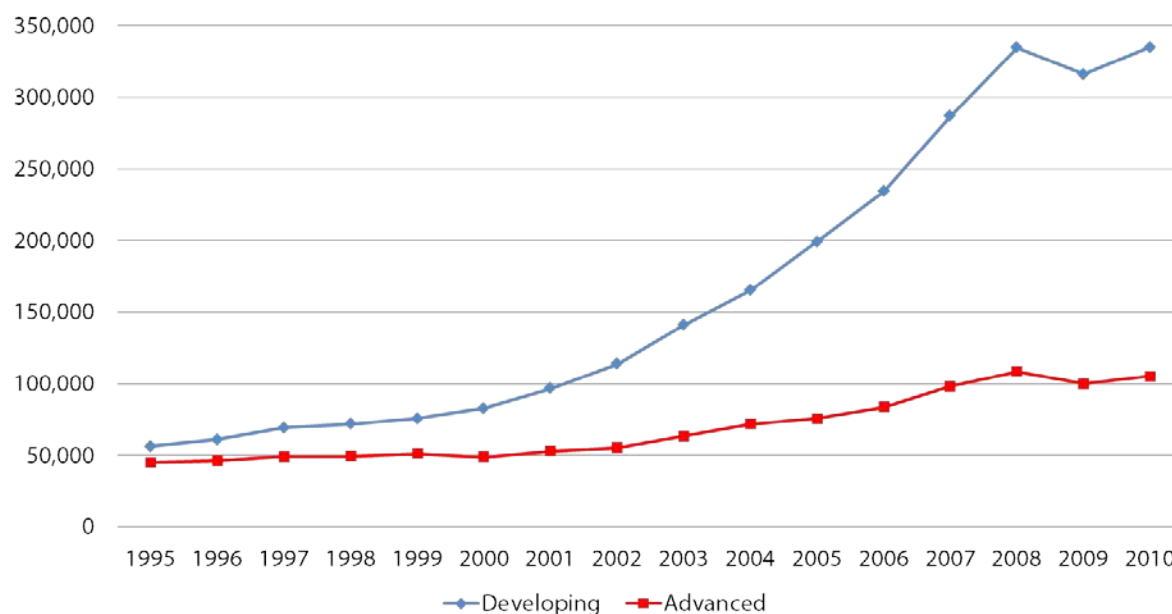
- Monitoring, Analysis and Projection of Remittance Inflows
- Developing Retail Payment Systems for Remittance Transfers
- Reducing the Costs of Remittance Transfers
- Improving Financial Access of Individuals and Households
- Leveraging Remittances for Capital Market Access of Financial Institutions or Countries

Trends in Remittances

Over the past 15 years, the inflow of remittances to developing economies has grown sixfold, from \$56 billion in 1995 to \$334 billion in 2010 (Chart 4.1). The significant increase in remittance flows also means that it is becoming an increasingly important component of PCF. In 1995, remittances constituted 24 percent of total PCF;² by 2008, their share in total PCF had increased to 33 percent (Annex 4.A).

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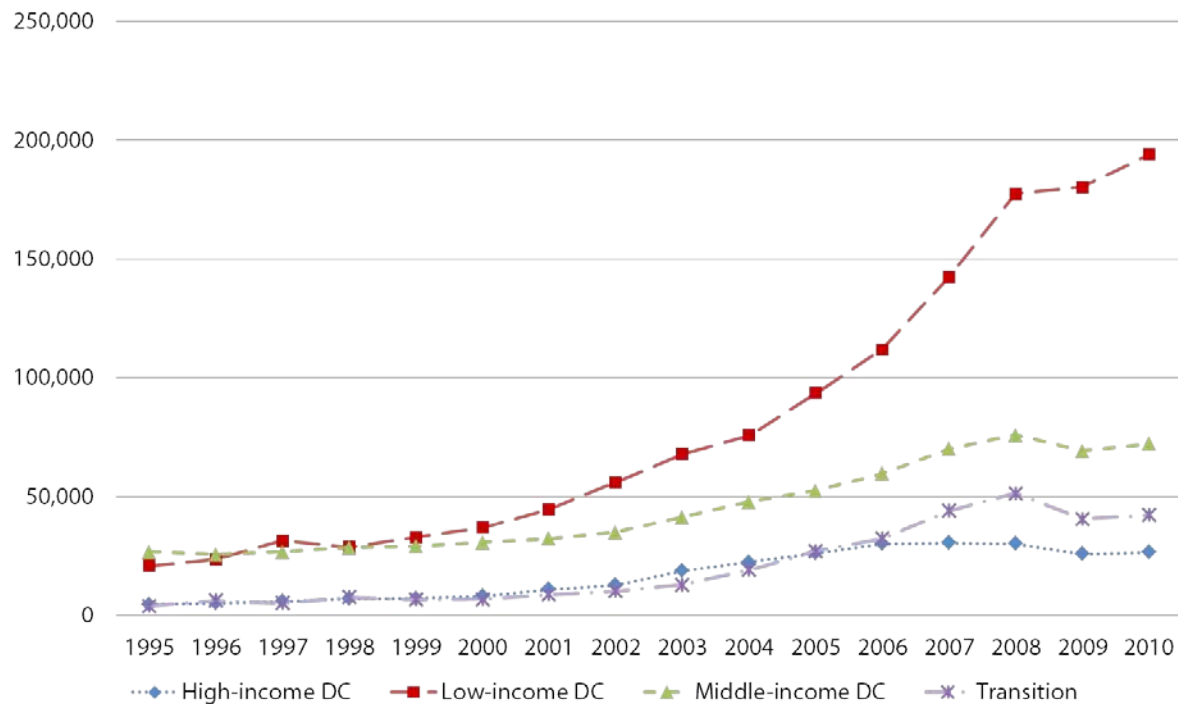
Chart 4.1: Remittances received by advanced and developing countries, 1995–2010 (US\$ millions)



Source: Calculated using data from World Bank, *Migration and Remittances Fact Book 2011*



Chart 4.2: Remittances received by development status, 1995–2010 (US\$ millions)



Source: Calculated using data from World Bank, *Migration and Remittances Fact Book 2011*

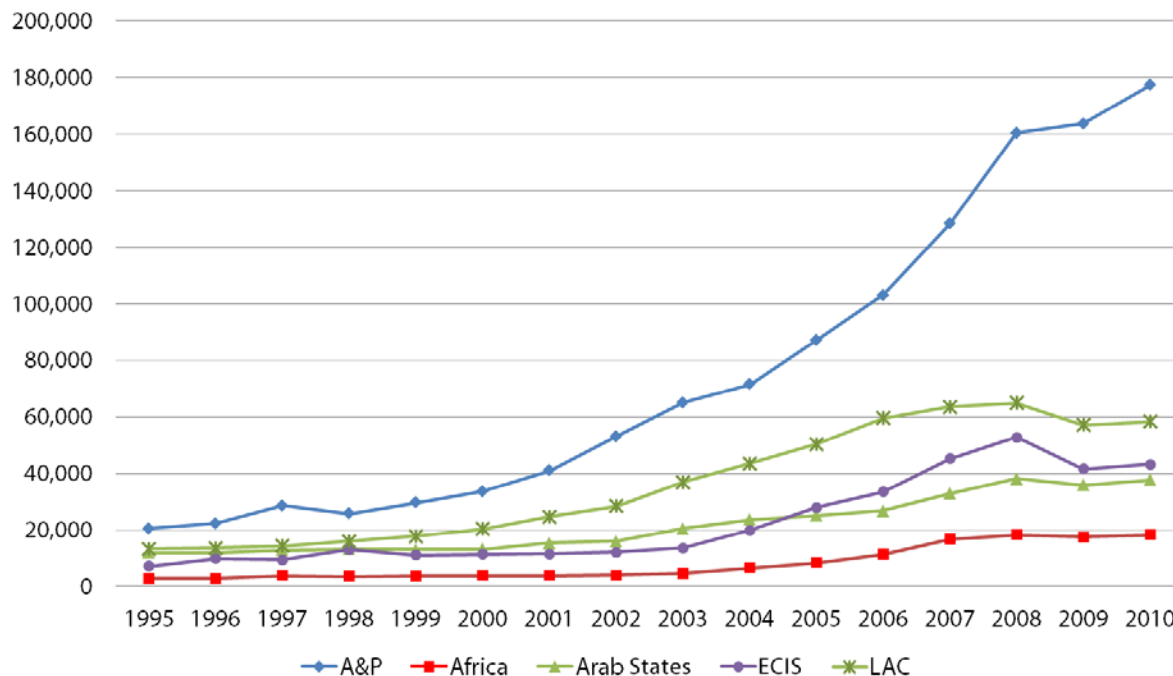
Poorer countries receive relatively larger remittances (Chart 4.2): the lower the average income in a country, the more likely that its citizens will seek to migrate and therefore the higher its remittance inflows will be. As of 2010, LICs received \$194 billion in remittances—that is, 58 percent of total remittances received by all developing countries in that year. Middle-income countries received \$72 billion (or 22 percent of total remittances), followed by transition economies (\$42 billion). High-income countries received only \$26 billion—or 8 percent of total remittances in 2010.

The group of transition countries experienced the biggest increase in remittance inflows during this period: remittance inflows rose from \$4 billion in 1995 to \$42 billion in 2010—a staggering 940 percent increase. The growth in remittances in LICs was also striking, increasing from \$21 billion in 1995 to \$194 billion in 2010 (an 830 percent increase).

By region (Chart 4.3), it appears that all developing regions received higher remittances between 1995 and 2010. The largest recipient region was Asia and the Pacific. In 2010, the region received \$177 billion (or 53 percent of total global remittances received by developing economies that year), followed by Latin America and the Caribbean, which received \$58 billion (or 17 percent of total global remittances to developing economies). The ECIS region received \$43 billion (13 percent of total global remittances) and the Arab States \$38 billion (11 percent of total global remittances). Africa received only \$18 billion (5 percent of total global remittances) in 2010.



Chart 4.3: Remittances received by region, 1995–2010 (US\$ millions)



Source: Calculated using data from World Bank, *Migration and Remittances Fact Book 2011*

The growth in remittances between 1995 and 2010 has been the fastest in Asia and the Pacific. From 1995 to 2010, remittances to the region increased by 763 percent, from \$21 billion in 1995 to \$177 billion in 2010. The second fastest growing region in terms of remittances inflows is Africa. Despite their relatively small share in total remittances, remittances to Africa increased by 545 percent from 1995 to 2010. The Arab States had the slowest growth in remittances among all developing region. Remittances to the Arab States increased by 213 percent, from \$12 billion in 1995 to \$38 billion in 2010. As a result, the Arab States region's share in total remittances was nearly halved during the period, from 21 percent in 1995 to 11 percent in 2010.

The Growing Economic Importance of Remittances

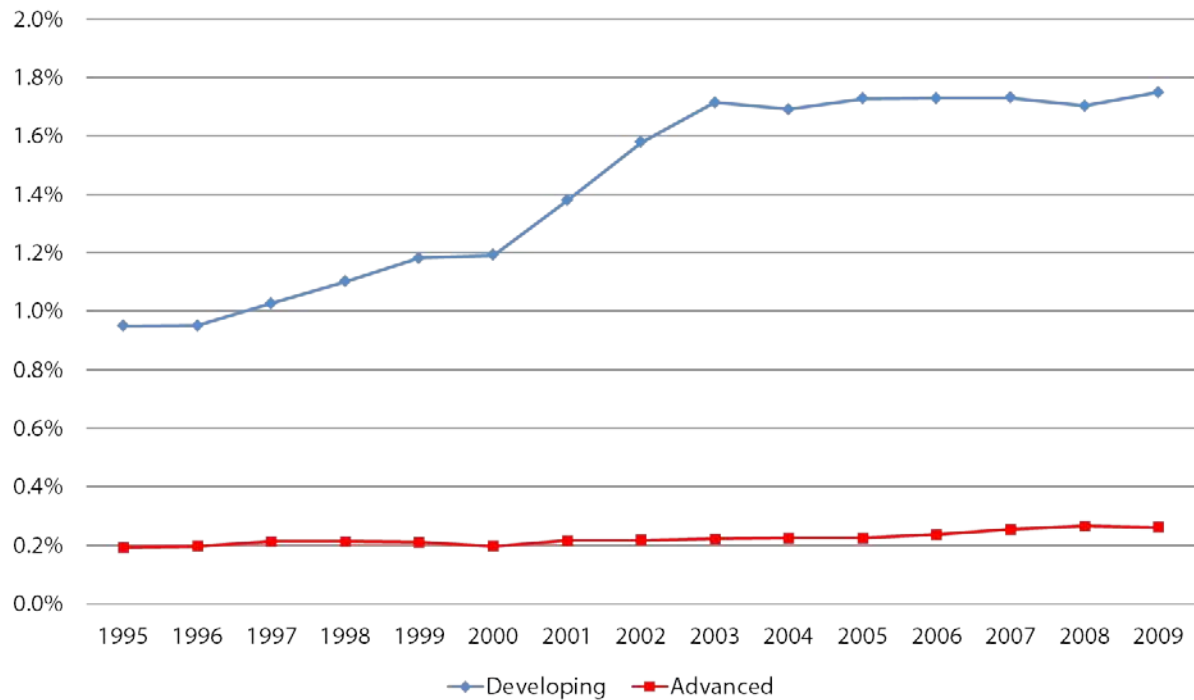
Not only have economic remittances increased in importance as a source of PCF, but they have also grown in importance relative to the size of the economy. As a share of GDP, remittances rose from 0.95 percent in 1995 to 1.75 percent in 2010, with much of the increase occurring between 1996 and 2003 (Chart 4.4).

Moreover, remittances as a share of GDP nearly doubled in all regions except for the Arab States (Annex 4.B). The biggest increase was in Africa, where remittances as a share of GDP increased from 0.9 percent in 1995 to 2 percent in 2009.

The Arab States had the highest remittance-to-GDP ratio during this period. As of 2009, remittances as a share of GDP were 3.1 percent in the Arab States region, 2 percent in both Africa and Asia and the Pacific and 1.4 percent in the ECIS region. In Latin America and the Caribbean, remittances represent only 1 percent of GDP.



Chart 4.4: Remittances received as a share of GDP for advanced and developing countries, 1995–2009



Source: Calculated using data from World Bank, *Migration and Remittances Fact Book 2011*

The relative importance of remittances to the receiving economies is strongly correlated with the development status of each country. As Annex 4.C shows, low-income developing countries are more dependent on remittances, while high-income developing economies are less dependent. As of 2009, remittances represented 2.2 percent of GDP in low-income developing countries, 1.5 percent in MICs and 0.8 percent in high-income developing countries. In transition economies, remittances represented 1.7 percent of GDP.

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Remittances continued to increase in importance throughout the period in all developing groups, with the smallest increase in MICs and the biggest increase in transition economies. In transition economies, remittances as a share of GDP increased from 0.6 percent in 1995 to 1.8 percent in 2009; they were followed by the high-income countries, where remittances as a share of GDP increased from 0.3 percent to 0.8 percent in 2009. In low-income developing countries, remittances as a share of GDP increased from 1.3 percent in 1995 to 2.2 percent in 2010.

MICs are the only exception to the trend. After a period of rising relative importance of remittances from 1.4 percent in 1995 to 2 percent of GDP in 2003, remittances as a share of GDP declined to 1.5 percent in 2009.

**Table 4.1: Remittances as a Share of GDP, 2009**

Country	Region	Development Status	Remittances as a share of GDP, 2009 (%)
Tajikistan	ECIS	Transition	35.1%
Tonga	A&P	Middle-income DC	27.7%
Lesotho	Africa	Low-income DC	24.8%
Moldova	ECIS	Transition	23.1%
Nepal	A&P	Low-income DC	22.9%
Lebanon	Arab States	Middle-income DC	22.4%
Samoa	A&P	Middle-income DC	22.3%
Honduras	LAC	Middle-income DC	19.3%
Guyana	LAC	Low-income DC	17.3%
El Salvador	LAC	Middle-income DC	15.7%
Jordan	Arab States	Middle-income DC	15.6%
Kyrgyzstan	ECIS	Transition	15.4%
Haiti	LAC	Low-income DC	15.4%
Jamaica	LAC	Middle-income DC	13.8%
Bosnia and Herzegovina	ECIS	Transition	12.7%
Serbia	ECIS	Transition	12.6%
Bangladesh	A&P	Low-income DC	11.8%
Philippines	A&P	Low-income DC	11.7%
Albania	ECIS	Transition	10.9%
Togo	Africa	Low-income DC	10.3%

Source: Calculated using data from World Bank, *Migration and Remittances Fact Book 2011*

Since 2003, the share of total remittances in GDP of all developing countries has stabilized at around 1.75 percent. Yet, data at the national level reveals the extent to which several economies are highly dependent on such inflows. In 2009, remittances exceeded 10 percent of GDP in 21 developing economies (Table 4.1).

The Stability and Countercyclicality of Remittances in the Context of External Economic Shocks

Historically, remittances have been stable and even countercyclical, tending to rise during times of financial crisis and natural disasters because migrants living abroad send more money to help their families back in places of origin.³ “There is unambiguous, plentiful evidence that remittances function as a shock-absorber in low-income countries by providing critical income support after economic shocks, natural disasters and civil conflict” (Kapur 2004, World Bank 2006).



Indeed, much evidence points to the fact that remittances are less volatile to economic downturns as compared to FDI or Portfolio Equity. For instance, during the 2001 economic downturn, only remittances kept growing, whereas both FDI and portfolio equity declined. Evidence from Asia and the Pacific indicates that remittances in the region are relatively stable sources of external finance, compared with exports and non-FDI private capital inflows. “Throughout the 1990s, the standard deviation of the ratio of remittances to GDP is around 0.88 while that of exports and non-FDI PCF are 7 and 13 respectively” (UNESCAP 2007).

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Country-specific evidence validates these findings. For instance, remittances to Philippine households increased after the 1997 financial crisis (Yang 2003). They rose as a share of personal consumption in response to the financial crisis in Mexico in 1995 and in Thailand in 1997 and continued to rise as a share of personal consumption after natural disasters in Bangladesh, the Dominican Republic, Haiti and Honduras (Gabel 2007). They increased in Albania shortly after the economic and political crisis of 1997 and fuelled a recovery in the economy by 1998 (Korovilas 1998). Remittances also increased during Hurricane Mitch in Central America, and they were a critical means of support for the vulnerable during Lebanon’s civil war (Ratha 2007, Kapur 2004).

In fact, for the first time since the 1980s, remittances to developing countries declined in 2009.⁴ In the aftermath of the global economic crisis, remittances declined by 5.5 percent in 2009 from their 2008 peak of \$324 billion. Still, the decline in remittances during the global financial crisis was modest, compared to a 40 percent decline in FDI between 2008 and 2009 and an 80 percent decline in private debt and portfolio equity flows from their peak in 2007 (Mohapatra et al. 2010). According to World Bank estimates, remittances were expected to totally recover by 2010.

Strikingly, the recession in 2009 did not cause a decrease in remittances to Asia and the Pacific. Despite the overall 5.5 percent decline in remittances between 2008 and 2009, remittances to Asia and the Pacific actually increased by 2 percent. On the other hand, remittances to Latin American and Caribbean countries declined by 12 percent between 2008 and 2009. The degree of resilience to the crisis is dependent on the source countries that the migrants are sending money from. Most Latin American and Caribbean remittances come from migrants in the United States, where the crisis originated and was most severe. On the other hand, migrants from Asia and the Pacific are sending remittances from many source countries, including countries from the rich oil exporters of the GCC, Europe and North America.

Another example of concentration in the source of remittances can be found in the ECIS region, where remittances declined by 21 percent between 2008 and 2009 on account of the crisis. Most ECIS remittances came from the Russian Federation and Europe, the economies of which were disproportionately affected by the economic crisis of 2007–2008. In other words, a diversification in the destination of migrants increases the resilience of remittances to economic downturns.

The relative resilience of remittance flows in the context of economic crises has also been noted for Africa. “The crisis threatens to reverse the continent’s recent progress in attracting public and private capital inflows. While private financial flows held their ground in 2008, the continent will see a substantial decline in 2009



due to the economic downturn. The one relatively bright spot in this picture is that remittances appear to be relatively more resilient to the economic downturn” (AfDB 2009).

Remittances, Economic Growth and Poverty Reduction

Given the growing importance of remittances as a source of PCF, these flows could potentially become an important tool for economic development, especially if they can be channelled into productive investment (Ratha 2007).⁵ From a macro-economic perspective, it is increasingly accepted that remittances can generate output growth either by increasing consumption or by increasing investment.⁶ In this context, the positive multiplier effects of remittances may well promote growth, as, for instance, when remittances are used to purchase domestically produced goods and services (Stahl and Arnold 1986, Stahl and Habib 1989, Glytsos 1993, Das and Serieux 2010).⁷ The ability of households to spend on health, housing and nutrition can also enhance their productivity and spur economic growth over the longer term.

Other studies have shown that remittances have been important in generating output growth by increasing investment in countries with less developed financial sectors. The reason for this is that many migrants invest their savings in small businesses, real estate or other assets in their own countries and therefore support local markets. In economies where the financial system is underdeveloped, remittances may alleviate credit constraints and act as a substitute for financial development (Giuliano and Ruiz-Arranz 2006, UNESCAP 2007). In other words, remittances in these countries have provided an alternative means for financing investment and reducing liquidity constraints. “Remittances make a significant contribution to savings and investment in island economies such as Samoa and Tonga” (Brown 1994); in Tunisia, workers who have limited access to the financial market tend to use such remittances to invest (Mesnard 2004). In short, to the extent that economic remittance transfers finance health, education and increase investment, they could have a positive effect on economic growth.

Given the growing importance of remittances as a source of private capital flows, these flows could potentially become an important tool for economic development, especially if they can be channelled into productive investment.

However, large remittance inflows, like any other foreign currency inflows, can cause an appreciation of the real exchange rate and raise the price of traditional exports, while making imports more expensive. Although empirical evidence of such ‘Dutch Disease’ effects of remittances is still lacking, the impact is likely to be large in small economies. For instance, some countries, including El Salvador, Kenya and Moldova, are worried about the effects of large remittance inflows on currency appreciation. Several studies have suggested that, since workers’ remittances are mainly used for consumption purposes, they have a minimal impact on investment.

To date, the empirical evidence of the impact of remittances on economic growth appears mixed and is difficult to predict *a priori*. For instance, results for a sample of 39 developing countries covering the period 1980–2004 indicate a positive impact on economic growth (Pradhan et al. 2008). A study examining the aggregate impact of remittances on the economic growth of 18 Latin American countries for the period 1980–2005 found that remittances positively and significantly affected the growth of Latin American economies where the financial systems are less developed by providing an alternative way to finance investment and helping overcome liquidity constraints (Fayissa and Nsiah 2010). There were similar results for 37 African countries for the period 1980–2004 (Fayissa and Nsiah 2008).



On the other hand, empirical assessments on the impact of workers' remittances on growth and poverty reduction in developing Asia-Pacific countries for the period 1993–2003 found that, “while remittances do have a significant impact on poverty reduction through increasing income, smoothing consumption and easing capital constraints of the poor, they have only a marginal impact on growth operating through domestic investment and human capital development” (UNESCAP 2007). While not denying the poverty-alleviating and consumption smoothing effects of remittances on recipient households, other studies find no impact on economic growth (IMF 2009).

More recently, it has been suggested that, by boosting foreign exchange receipts, remittances have allowed LICs to maintain adequate foreign reserves and service debt.⁸ “Remittances have helped to build up international reserves and have contributed to reducing current account deficits in many developing countries. This has provided a cushion against external shocks during the global crisis. In LICs, the current account deficit as a percentage of gross domestic product (GDP) would have more than doubled in the absence of remittances in recent years. For some large remittance recipient countries such as the Philippines, Bangladesh, Nepal, remittance flows have offset large trade deficits and enabled these countries to maintain a current account surplus” (Mohapatra et al. 2010).

Further, remittances are now factored into sovereign ratings in MICs and in the debt sustainability analysis⁹ for LICs. For instance, in large remittance recipient countries, country creditworthiness analysis by major

Box 4.1: Diaspora Bonds as a Source of Financing during Difficult Times

In the current environment of a severe crisis of confidence in debt markets, several developing countries are encountering great difficulty in obtaining private financing using traditional financial instruments. This scarcity of capital threatens to jeopardize long-term growth and employment generation in developing countries, many of which have limited access to capital even in the best of times. Official aid alone will not be adequate to bridge short- or long-term financing gaps. Ultimately, it will be necessary to adopt innovative financing approaches to target previously untapped investors. Diaspora bonds are one such mechanism whereby developing countries turn to borrowing from their expatriate (diaspora) communities. A diaspora bond is a debt instrument issued by a country — or potentially, by a sub-sovereign public or private entity — to raise financing from its overseas diaspora. In the past, diaspora bonds have been used by India and Israel to raise over \$35 billion of development financing. The proceeds from these bonds were used to support balance of payments needs and finance infrastructure, housing, health,

and education projects. Several countries — for example, El Salvador, Ethiopia, Nepal, the Philippines, Rwanda and Sri Lanka — are considering (or have issued) diaspora bonds recently to bridge financing gaps.

Diaspora bonds are a stable and cheap source of external finance for countries, especially in times of financial stress. For the diaspora investors, these bonds offer the opportunity to help their country of origin while at the same time offering an investment opportunity. In addition to being motivated by patriotism, diaspora members are usually more interested than foreign investors in investing in the home country. However, in countries that have weak governance and high sovereign risk, diaspora bonds may require support for institutional capacity-building and/or credit enhancement from multilateral or bilateral agencies. Compliance with securities and exchange regulations overseas can also be cumbersome in some migrant-destination countries.

Source: Mohapatra, Sanket, Dilip Ratha and Anil Silwal, 2010, ‘Outlook for Remittance Flows 2011-12: Recovery after the crisis, but risks lie ahead’, Migration and Development Brief 13, Migration and Remittances Unit, World Bank, Washington, DC.



rating agencies such as Standard & Poor's (S&P) and Moody's often cite remittances as a factor in their rating decisions. The stability of remittances to the Philippines was an important factor in its ability to issue a \$750 million bond despite the global financial crisis. Bangladesh was rated for the first time in 2010, receiving a BB rating from S&P, similar to that of many emerging markets. Again, the rating agencies cited the high share of remittance flows in GDP and their high growth rate as one of the important factors for their rating decisions.

As countries have become aware of remittances functioning as a stable source of foreign currency earnings, many countries have started looking at their diaspora for potential sources of capital that could be tapped through the issuance of diaspora bonds. Countries such as El Salvador, Ethiopia, Nepal, the Philippines, Rwanda and Sri Lanka have issued or are considering the issuance of diaspora bonds (Ratha 2007, Mohapatra et al. 2010).

Policy Options for Building Resilience: Leveraging Remittances for Development

Given the size and stability of remittance inflows as well as their countercyclical behaviour in the face of external shocks, recent policy attention has focused on mobilizing remittances to leverage growth and poverty dividends and also to cushion the impact of external shocks. Specifically, the focus has been on policies to monitor and analyse the impact of remittance receipts, to develop retail repayment systems, to reduce transactions costs for remittance transfers, and to develop strategies to intermediate these resources through the formal financial system and channel them into productive investment.

The Monitoring, Analysis and Projection of Remittance Inflows

Monitoring and analysing remittance inflows includes understanding the size, corridors, channels and costs of remittance flows and the cyclical behaviour of these flows, analysing remittances' impact on poverty, inequality,

Box 4.2: Monitoring Remittance Inflows

Governments in every geographical region face increasing pressure to better monitor the transfer of economic remittances from and into their countries. On the one hand, it is ever more important to impede the flow of money that may be laundered or used to fund terrorist activities. On the other hand, flows of foreign funds should be facilitated to reach impoverished communities and protected from undue restrictions, high fees, and delays. Central banks across the world have invested in making the process more transparent and ensuring that proper channels exist for all communities to increase the ability of remittances to promote development and to save families from extreme poverty.

For instance, examples from Malaysia show that opening the banking system to immigrants and implementing legislation that protects consumers and banks is good policy in legalizing transfers from the country and therefore preventing money-laundering. At the same time, Indonesia has created legislation to help banks to receive remittances and to discourage the use of money-changers, who may not act fully within the law or may charge high fees. Similarly, the United Republic of Tanzania has started to monitor remittances more carefully while making the process more transparent and making the information available to the public in order to ensure that there is sufficient collaboration between different parts of national



Box 4.2: Monitoring Remittance Inflows (contd.)

administration; consequently, the system is more reliable and secure for all. In October 2010, the Bank of Tanzania released information for the 2005–2008 fiscal years.

Elsewhere in Africa, the Bank of Uganda, in partnership with the Uganda Bureau of Statics, announced in 2011 that it has started the third national household survey to collect data on money and other items remitted from workers in the diaspora. In 2006 and 2008, Uganda also conducted comprehensive National Household Workers' Remittances Surveys on money sent home by Ugandans living and working outside the country. The survey, published in 2009 with information from the previous year, covered 4,080 households located throughout the country. The Surveys measure remittances with regard to, *inter alia*, value, type (cash or kind), amounts, source countries, transmission channels and flow patterns. "The latest survey found that

remitters cut across all age groups, but are mainly in the 20–49 years age range. The majority of remitters (69.6%) have lived abroad for periods of 10 years and less. The bigger proportion of remitters (64%) was married, while 29.6% were in the never married category. Most remitters (86.2%) attained a qualification of secondary school level and beyond. The bigger proportion of households (36.9%) indicated that remitters were based in Europe, which was followed by Africa (29.0%) and North America (24.5%). 93.0% of remitters are in the 'working' category." Already in 2010, the Bank of Uganda had forecasted an increase of over 16 percent in remittances into the country, most of them specially coming from immigrants in the United Kingdom, the United States and South Africa, in which the World Bank has denominated the strongest remittances corridors into Uganda.

Source: Hernandez-Coss, Raul, 2008, 'The Malaysia-Indonesia Remittances Corridor: Making formal transfers the best option for women and undocumented migrants', World Bank Working Paper No. 149, World Bank, Washington, DC.; Information on Uganda's household level surveys can be found online on the Bank of Uganda website: www.bou.or.ug/bouwebsite/opencms/bou/rates_statistics/statistics/trade_remittances.html; World Bank, 2010, *Uganda's Remittance Corridors from United Kingdom, United States and South Africa: Challenges to Linking Remittances to the Use of Formal Services, 2010*, World Bank, Washington, DC.; Bank of Uganda, 2008, *Uganda: Workers' Remittances Report*, Inward Remittances 2008, p. iv.

education, health care and investment in remittance recipient countries and analysing policy factors that affect remittance costs, such as entry barriers and exclusivity contracts affecting market competition.

Developing Retail Payment Systems

Changes in the payment system relating to personal remittances impact all retail or small-value payments. Items in this category include new payment platforms or instruments (including card-based, cell phone-based, or internet-based remittance instruments), prudential capital requirements and regulations governing access of remittance agents to clearing and settlement systems, and the disclosure of remittance fees. Interestingly, Africa is now at the forefront of mobile money transfer technologies. For instance, Kenya's M-Pesa now has more than 9 million subscribers. While M-Pesa is mostly focused on domestic money transfers in Kenya, with a small pilot scheme for UK-Kenya remittances, a Kuwaiti mobile operator Zain has expanded to 15 African countries and now has 42 million subscribers. It offers Zain Zap, or mobile remittance service, which offers, in addition to money transfers, other services such as payment for bills and groceries (Mohapatra et al. 2010).

New remittance technologies are also being adopted in South Asia. In Bangladesh, Banglalink, the second largest mobile operator in Bangladesh, is launching a mobile remittance services in partnership with several



Box 4.3: Developing Retail Payment Systems

Partnerships between banks and telecommunication companies have the potential to give millions of mobile subscribers access to national banking systems. The development of more secure, faster and reliable technologies increases the capacity of companies to provide services to people who previously have been disenfranchised due to inflexibility in the banking system. By bringing the bank into the mobile device, it is possible to integrate rural residents as well as urban customers who otherwise have no access to a bank.

Since 2010, Banglalink, the second largest mobile operator in Bangladesh, has partnered with banks, providing services to immigrant Bangladeshi nationals in Europe, the Gulf States, the United States and Australia to send remittances back home for easy access by family members at one of the company's thousands of 'cash points' in Bangladesh. The service reduces the transfer time from the current four to five days to just one day.

This example of partnership extends beyond the use of new technologies and has the potential to curtail money-

laundering and other illicit activities, such as the need to use informal channels for exchange of foreign currency. The money that is remitted back to Bangladesh is conveniently stored in an e-wallet that can then be accessed to withdraw cash or be used for online payments.

Bangladesh is one of the largest exporters of manpower resources, with an expatriate population of 7 million people as of 2010. Money remitted back home by migrants is one of the largest sources of foreign currency. Barriers to financial services for the rural population, who are the major beneficiaries of the migrant workers' earnings and who constitute 90 percent of the population, hinder remittance inflows through formal money transfer channels. In 2010, remittance inflows contributed \$10 billion in foreign exchange annually, or 9 percent of Bangladesh's GDP. However, 40 percent of remittance inflows bypass formal channels primarily because of asymmetries in access to retail payment infrastructure.

Source: Rahman, Atiur, 2010, *Inauguration of Dhaka Bank-EBL-Banglalink: Mobile Phone Based Remittance Service*, 13 April, Bangladesh Bank.

Bangladeshi banks. These banks will offer 'mobile wallet' accounts through Banglalink and Banglalink distribution outlets will be used as remittance disbursement cash points.

Reducing Transactions Costs for Remittance Transfers

Reducing remittance fees would increase the disposable income of migrants, boost their incentives to send money home, and encourage the use of formal remittance channels. The cost of sending remittances tends to be high and regressive. Although a typical poor migrant sends about \$200 or less per transaction, the average cost through the top three money transfer operators (such as Western Union) can be as high as \$18. In other words, these fees are highly regressive because the smaller remittances sent by poor migrants cost more per dollar sent. Although remittance costs have been declining in recent years, they have remained sticky since 2006. However, the recent global crisis has intensified efforts to reduce remittance costs and leverage remittances for improving financial access. As a result, many banks and operators are cutting fees (Ratha 2007).

Furthermore, South-South remittance costs are higher than North-South remittance costs, even though nearly half of the migrants from the South live in the South. Yet, South-South remittances remain costly due to capital and exchange controls or because currency conversion charges are payable at both ends.



Box 4.4: Lower Transactions Costs for Remittances

The call to lower fees for monies being remitted has been at centre stage of discussions on South-South migration. This is to be expected, as costs of South-South remittances are even higher than those of North-South remittances because of a lack of competition in the remittance market, a lack of financial development in general, and high foreign exchange commissions at both ends of the transaction.

On average, the cost of sending money to Latin America and the Caribbean has been cut in half since 2000 due to greater competition and the adoption of new technologies for this

service. The average total costs for migrant remittances are higher than the global average in countries in East Asia and Pacific, sub-Saharan Africa, and the Middle East and North Africa (MENA) regions.

While countries such as China, Nicaragua, Bangladesh and Costa Rica have established mechanisms to target these issues, the vast majority of remittances from migrants residing in other countries of the global south still face onerous charges on their transactions.

Source: World Bank, 2001, *Migration and Remittances Factbook 2011*, World Bank, Washington, DC.; Monge-González, Ricardo, Oswald Céspedes-Torres and Juan Carlos Vargas-Aguilar, 2009, *South-South Remittances: Importance of the Costa Rica-Nicaragua Corridor*, Academia de Centroamérica, San Jose, Costa Rica.

Financial Access of Individuals and Households

While financial intermediaries like banks, credit unions and savings banks can help deliver remittances, they can also benefit by offering remittance services that may attract new customers and then encourage them to save and invest. Besides encouraging savings from remittances, these financial intermediaries can develop remittance-linked consumer or housing loans and insurance products.

Encouraging remittances through banking channels can improve the impact of remittances on development by encouraging more savings (cash remittances are less likely to be saved than direct bank deposits) and enabling better matching of savings with investment opportunities. For many poor households, remittances are the only point of contact with the formal financial sector. Both sending and receiving countries can give migrants more access to banking by allowing country of origin banks to operate overseas and by providing identification cards (such as the Mexican Matricula Consular) that are accepted by banks to open accounts. Access to remittance services in rural and remote areas can be improved by encouraging the participation of savings banks (including postal savings schemes) and credit unions in the remittance market. Existing regulations may need to be amended to allow these institutions to more fully participate in the provision of remittance services.

Leveraging Remittances for Capital Market Access of Financial Institutions or Countries

Large and stable remittance inflows undoubtedly improve a country's creditworthiness and thereby the creditworthiness of sub-sovereign entities as well. Hard currency remittances, properly accounted, can significantly improve country-risk rating and thereby lower the cost of borrowing money in international markets. The ratio of debt to exports of goods and services (a key indicator of indebtedness) would increase significantly if remittances were excluded from the denominator.



Box 4.5: Access to Financial Services

In the last 20 years, it has become increasingly important to improve access to financial services for migrants abroad while ensuring that their remittances are captured within the national financial systems to impede money-laundering and other illegal activities. Governments in countries of origin and destination have set up regulations that give migrants access to savings and banking systems. Innovative examples can be found around the world, but practices involving countries of origin that help their migrants abroad to better navigate host country institutions are particularly noteworthy.

Since 1969, the Government of Morocco, in conjunction with the Banque Centrale Populaire, increased its presence abroad, particularly in France, to give Moroccan migrants access to financial services. Under the scheme of 'Bancarization' — to engage the diaspora and provide better options abroad — the bank opened branches in the suburbs of Paris and also institutionalized the use of 'post office checks' that were easily accessible in French post offices for the transmission of remittances to the migrants' communities of origin.

Most recently, the governments of Mexico and other Central American countries have also initiated programmes to ensure that their migrants abroad, especially in the

United States, have access to the banking systems of the host countries. The Government of Mexico, through its vast network of consulates in the United States, has been issuing high-security identifications to its nationals for the past 10 years. This identification, known as *Matricula Consular*, is a means of identification for a population that otherwise may not have any proof of citizenship, name, age, or address.

Some financial institutions recognize the *Matricula Consular* as a valid form of identification to open checking and savings accounts. This gives Mexican nationals access to banking services and enables them to benefit from financial instruments that cater especially to migrants. It also increases the potential of those new customers to build credit histories and eventually benefit from loans to open businesses and/or to buy property. The Mexican *Matricula Consular* has also benefited migrants by giving them a means of identification that is widely recognized by law enforcement, government institutions, and businesses as a secure and reliable document backed by the Mexican government.

Other governments, including El Salvador, have created similar identification cards that can be used in the country of destination, but also in El Salvador, as a proof of foreign residency.

Source: Délano, Alexandra, 2011, *Mexico and its Diaspora in the United States: Policies of Emigration since 1848*, Cambridge University Press, New York; Iskander, Natasha, 2010, *Creative State: Forty Years of Migration and Development Policy in Morocco and Mexico*, Cornell University Press, New York.

Banks in many countries have used future remittances as collateral for raising significant bond financing from international markets. The interest spread on these bonds was lower and the tenor was higher than comparable plain sovereign bonds. Some estimates show that the potential for such bond financing remains untapped, especially in many poor countries that also receive significant remittances. The funds raised from these bonds can be targeted to specific development projects.

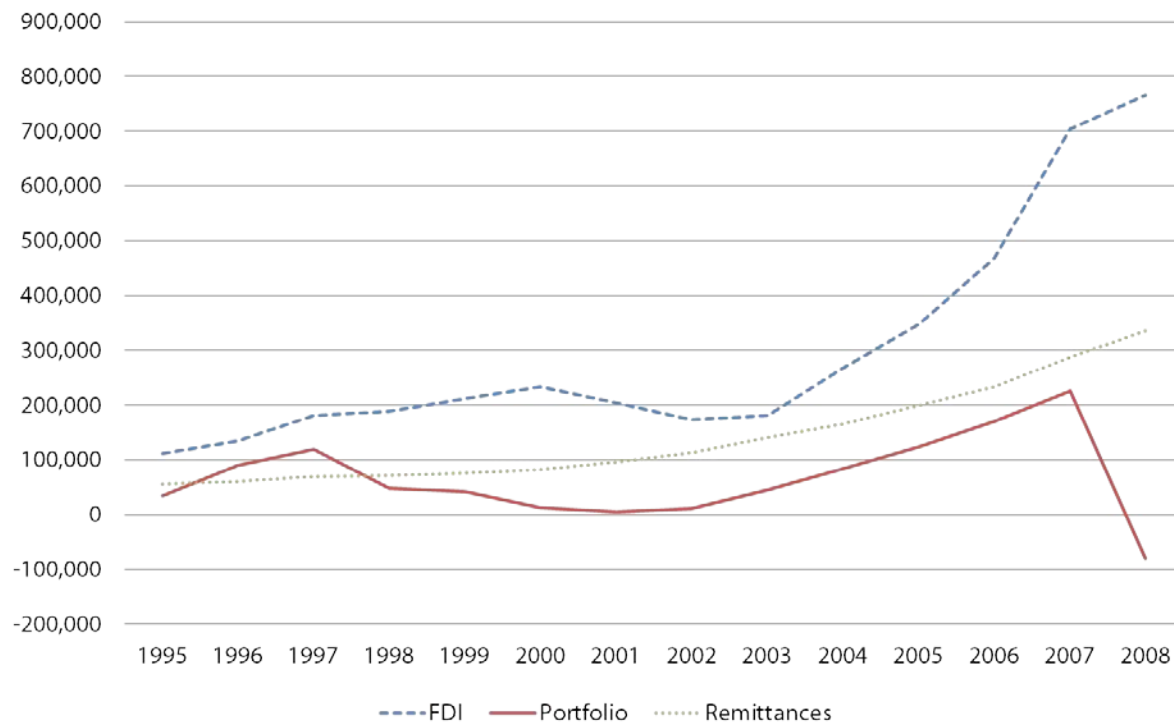


Notes

1. Remittances are the sum of workers' remittances, compensation of employees and migrants' transfers. They are classified as current private transfers from migrant workers resident in the host country for more than a year, irrespective of their immigration status, to recipients in their country of origin; compensation of employees is the income of migrants who have lived in the host country for less than a year; migrants' transfers are defined as the net worth of migrants who are expected to remain in the host country for more than a year (IMF 1993).
2. Defined as the sum of FDI, PI and remittances.
3. Remittances tend to rise when the recipient economy suffers a downturn in activity, an economic crisis, natural disaster or political conflict, as migrants may send more funds during hard times to help their family and friends.
4. It has been argued that the decline in remittances has both short- and longer-term effects on poverty and growth. Over the longer term, a fall in workers' remittances has an adverse direct influence on domestic demand. For instance, in LDCs, "the average income of families whose source of income is remittances is often higher than the average family income of workers who are engaged in the domestic sector or are unemployed. Thus, the reduction in remittances directly affects the domestic demand for manufactured goods" (Shaffaeddin 2009).
5. The traditional 'sterilization' techniques used to prevent currency appreciation due to natural resource windfalls, however, is not appropriate for addressing currency fluctuations due to remittances. The reason for this is that, unlike oil windfalls, remittances persist over long periods. Trying to sterilize their impacts year after year can be very costly.
6. However, large outflows of workers (especially skilled workers) can reduce growth in the country of origin; remittances may also induce recipient households to choose more leisure than labour, with adverse effects on growth. Since the effects of remittances on human and physical capital are realized over a longer period of time, in the short to medium run, the effect of remittances on growth may be mixed.
7. On the other hand, if remittances are used to purchase imported goods, the impact of remittances on economic growth may be limited.
8. However, remittances that are used to finance reverse flows are no longer available for consumption or investment. This would appear to limit the potential growth effect.
9. The joint WB/IMF low-income country Debt Sustainability Framework now allows for a more explicit consideration of remittances in evaluating the ability of countries to repay external obligations and their ability to undertake non-concessional borrowing from private creditors. The debt-to-export ratio, a key factor in sovereign ratings, would be lower if foreign exchange revenues from remittances were factored into calculations. Many IMF Article IV assessments of countries' economic performance now include remittances as a variable alongside FDI and portfolio flows.



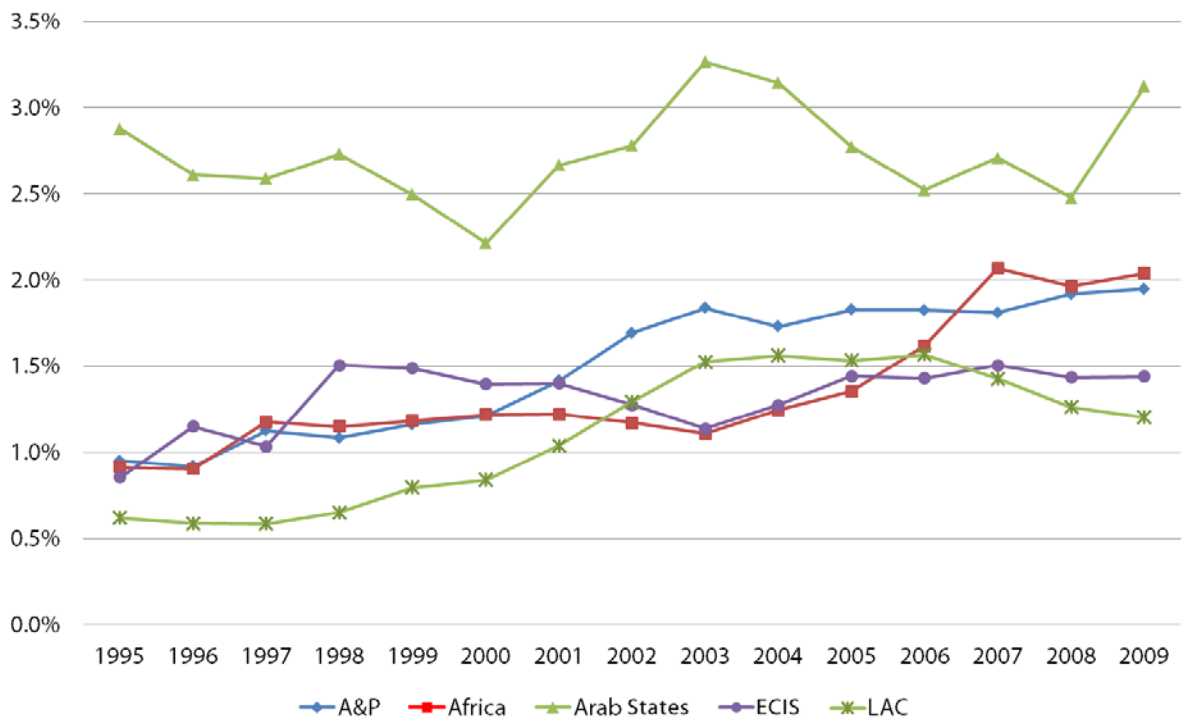
Annex 4.A: FDI, Portfolio and Remittances Inflows to Developing Countries, 1995–2008 (US\$ millions)



Source: Calculated using data from World Bank, *Migration and Remittances Factbook 2011*



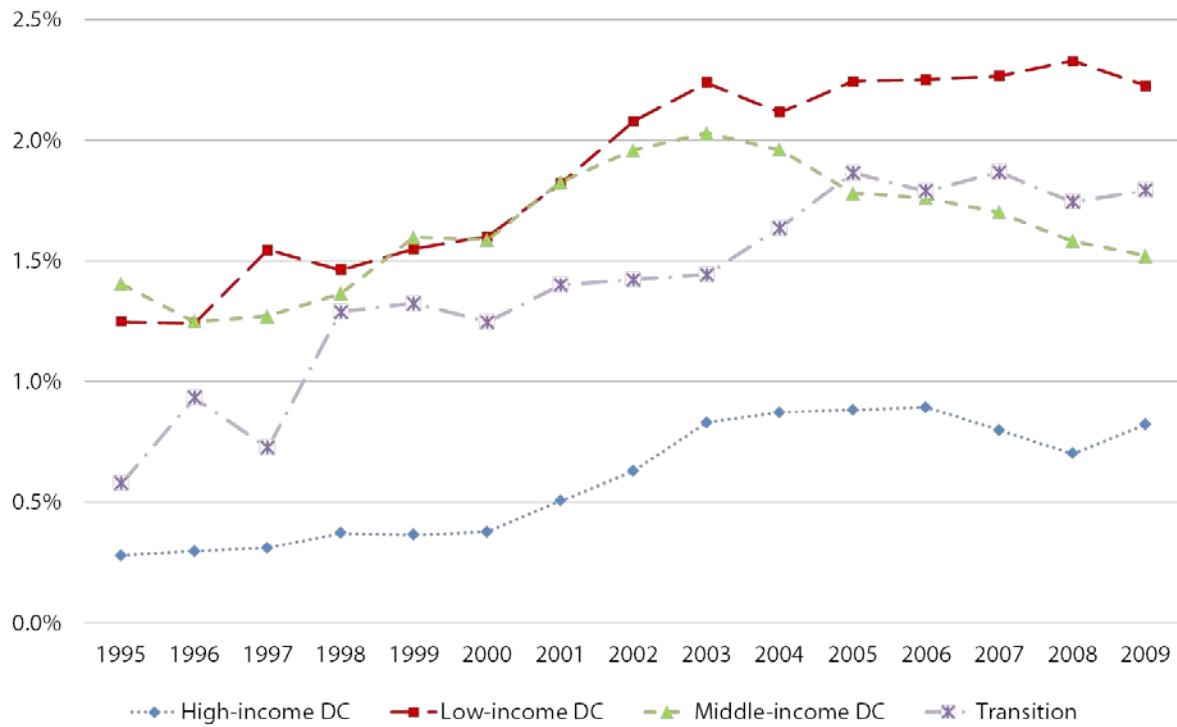
Annex 4.B: Remittances Received as a Share of GDP by Region, 1995–2009



Source: Calculated using data from World Bank, *Migration and Remittances Factbook 2011*



Annex 4.C: Remittances Received as a Share of GDP by Development Status, 1995–2009



Source: Calculated using data from World Bank, *Migration and Remittances Factbook 2011*



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