

AccessFinance

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Migrant Labour Remittances in the South Asia Region

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At a time of renewed international interest in remittances four countries in the South Asia region stand out in terms of the volume of remittances they receive, the national policies in place to attract increased flows, and the efforts of formal financial institutions to deliver remittances faster and more cost effectively – Bangladesh, India, Pakistan and Sri Lanka. At the end of 2004, their respective remittances of US\$3.4 bn (Bangladesh), US\$23.0 bn (India), US\$4.2 bn (Pakistan), and US\$1.3 bn (Sri Lanka) were among the 20 largest recipients of remittances in the world, collectively making the South Asia region the second largest regional recipient of remittances in the world after Latin America and the Caribbean (Table 1).

Table 1. Estimates of recorded Workers' Remittances (US\$ Billion)

	1999	2000	2001	2002	2003	2004	2003 (per capita US\$)
Total	14.0	16.0	15.9	21.4	25.9	31.9	
Bangladesh	1.8	2.0	2.1	2.8	3.2	3.4	23.2
India	11.1	11.7	11.1	13.7	17.4	23.0	15.8
Pakistan	0.1	1.1	1.5	3.6	4.0	4.2	27.0
Sri Lanka	1.0	1.2	1.2	1.3	1.3	1.3	67.7

Source: World Bank (2005)

The potential for remittances to reduce poverty and economic vulnerability, improve family welfare, and stimulate local economic development in the face of much lower, sometimes temperamental, foreign direct investment flows and declining overseas development assistance (ODA), is special interest to governments in the region.

To encourage higher flows, governments in all four countries have established public infrastructure to support the search for employment abroad, the migration of successful applicants, and their subsequent remittances. The public infrastructure includes emigration legislation, government departments, and a plethora of fiscal incentives.

- **Legislation:** Legislation such as the Emigration Act of 1983 (India) and the Emigration Ordinance of 1979 (Pakistan) form the legal basis for today's migration practices and influence the ease and convenience of dealing with the resulting government ministries and departments.
- **Government departments:** The Bureau of Manpower Employment and Training (Bangladesh), the Bureau of Emigration and Overseas Employment (Pakistan), and the Bureau of Foreign Employment (Sri Lanka) provide a range of pre- and postmigration services and facilities notably premigration training, and work permit processing.
- **Incentives:** Incentives that have been announced in successive budgets targeting migrants include special access to public educational institutions; generous duty-free import limits for items of personal

convenience; eligibility for special lotteries for prime plots in public housing schemes at attractive prices; and tax exemptions.

While dedicated public institutions and incentives aimed at facilitating and providing support for temporary migration and remittance inflows has helped the region address some of the basic challenges of facilitating large employment migration flows, and encouraging remittances back to the region, there remain more serious long term challenges.

First, the specific development impact of remittances is still unclear and many questions remain, including: What proportion of remittance monies is spent on consumption versus investment? Does the proportion vary with the income and educational level of the remittance-receiving family? What kinds of productive investment activities are remittances spent on? How does this vary by setting (urban or rural), and by district, region, or country?

Second, the region has a large state bank branch networks with immense potential for a more effective and efficient remittance financial market. How can public policy encourage a more active use of the formal remittances infrastructure and, how can the formal financial sector compete effectively with the trade-related informal remittance channels used by both legal and illegal migrants?

The recently published *Migrant Labor Remittances in South Asia* makes a start at addressing some of these questions. Its authors, Samuel Munzele Maimbo, Richard Adams, Reena Aggarwal and Nikos Passas, emphasize that this publication is only a start, as many research challenges remain with respect to understanding the development impact of remittances, and identifying ways in which to strengthen the remittance infrastructure.

Development impact of remittances

Addressing the first set of questions is methodologically challenging because of three factors. The most important of these is that remittance income is fungible which this makes it very difficult to associate remittances with any specific changes in household patterns of consumption or investment. Second, remittances have multiple effects on the local economy. For example, an increase in the volume of remittances in a community may lead to higher spending on housing, which in turn helps to generate more income and employment opportunities for unskilled construction workers. Third, a robust theoretical and analytical framework for determining the development impact of remittances is largely absent. Because remittance research is often based on data collected at just one point in time, it is difficult to measure how remittances change patterns of investment over time.

This study analyzes the impact of international remittances on poverty using a growth-poverty model. This model, which has been used by a host of poverty researchers, assumes that economic growth—as measured by increases in mean per capita income—will reduce poverty.

The results are interesting. The analysis finds that, when the estimated values for unofficial remittances are added to official remittance figures, total remittances (official and unofficial) reduce the level of poverty in South Asia. On average, the point estimates for the poverty headcount measure suggest that a 10 percent increase in total remittances (official and unofficial) will lead to a 0.9 percent decline in the level of poverty in South Asia. This means that for a “representative” country where exactly one-half of the population lives below the poverty line, a 10 percent increase in total remittances will bring the proportion living in poverty down to about 0.48 percent.

Formal Remittance infrastructure

The second set of questions pose less methodological hurdles, and commenting on the state of the formal remittance infrastructure, the authors find the following:

State banks: The South Asian remittances market is unique for the presence of an extensive branch network of state commercial banks which have long dominated the official remittances business through monopolistic national foreign-currency legislation and large bank branch networks. Today, India has over 32,000 rural commercial bank branches; Bangladesh has four nationalized banks with at least 3,346 branches in total; and Sri Lanka’s largest state bank alone has 326 branches, 81 counter services, and

188 pawning centers. Physically, the infrastructure for an active far-reaching remittance network is already present. The challenge lies in making it more effective and efficient.

Foreign Banks: Foreign banks have also noted the huge remittance potential in the region. Previously reluctant participants, they are slowly investing in this business, albeit largely for the higher-income migrants—doctors, accountants, lawyers, and other professionals. Foreign banks have hitherto largely been inhibited by their limited branch networks, which are primarily centered in major cities. They have also been careful about heightened anti-money laundering and counter-terrorist financing standards.

Local Banks: It is largely the local banks that are taking the lead in the remittance service market. Investing heavily in various remittance application technologies—credit cards, debit cards, Internet banking, and expanding the ATM networks. In Sri Lanka for example, the number of ATMs increased to 705 (2003) from 622 (2002). But, the potential for the ATMs to act as remittance conduits is yet to be realized. Most ATM transactions are cash from ATMs of the clients own banks. Until this changes, the possibility of using the networks for remittance purposes will remain limited.

Money Service Businesses: The strongest remittance competition in the market comes from the emergence of licensed money service businesses (MSBs)—nonbank financial institutions that accept cash, checks, or other money instruments, or “stored value,” in one location and pay the equivalent amount in another. Leading MSBs such as Western Union and Money Gram have extensive agent locations in the region that support their operations. However, Internet-based businesses such as C-Sam, are having a positive impact on the way business is managed.

Post Offices: Long used to delivering money orders to rural families, post offices are now investing in electronic money orders, partnering with money service businesses, and investing in Internet-based technology. The potential benefits for postal involvement are substantial. With 154,149 postal offices and 554 sorting offices, India Post has the most extensive postal retail network in the world. Sri Lanka Post has 625 main post offices, 3,423 sub-post offices, and 632 agency post offices. However, as long as they remain plagued with operational losses, the absence of management information systems, limited access to funds for investing in technology, client demand and usage will remain low. Reliability, credibility, and efficiency are essential ingredients to a remittance business.

Informal remittance infrastructure

Informal remittance systems—courier services, in-kind remittances, and *hawala* systems (also referred to as *hundi* or *chit*, *hawala* systems)—have a long history in the region. Originally developed at a time when conventional banking instruments were either absent or weak, informal channels such as *Hawala* offered a speedy, low-cost, convenient, accessible, and (when necessary) anonymous option. The convenience of door-to-door collection and delivery services is invaluable to migrants working long shifts and recipient families in communities with absent or weak formal financial services. Unfortunately, the informal system’s success—speedy transactions with minimal or no documentation—has also been its undoing. The anonymity associated with such transactions has long raised concern with law enforcement communities. This has led some countries to issue an outright ban on these systems; others have proceeded to or are considering issuing new regulations in an effort to improve the transparency of the sector.

Conclusion and Recommendations

The study concludes that remittances from migrant workers are increasingly important and are a stable source of financing for development related activities. With an extensive state and private bank network already in the region, a key component of the requisite building blocks for an effective remittance industry is already in place. However, much more needs to be done to maximize the network’s full potential. The study makes the following recommendations:

- *Shared payments systems platforms:* Greater investment in open architecture payments system information technology is required. Recipients should increasingly be able to receive remittances from any state or private bank branch or ATM machine, whether or not they hold an account with that institution be it a bank, post office or other non-bank financial institution.

- *Public-private partnerships:* Strategic partnerships between the public and private sectors across infrastructure, products, and services are necessary for countries in the region that seek the types of gains attained elsewhere.
- *Cross-selling:* As the profitability of the conventional formal financial sector remittance business model continues to decline, formal financial institutions invest in cross-selling complementary financial services and products. Encouraging recipients to open and maintain bank accounts that might lead to short- and long-term auto and housing loans, for example, should be part of a business strategy for banks.

In the long run, strengthening the formal financial sector for remittance purposes will facilitate the move away from informal remittance systems, which, though beneficial to the direct users, may not have as effective an impact on the macro level as formal remittance transfers. High transaction costs, long delays in transferring remittances, foreign currency controls, and overly bureaucratic policies and procedures for simple money transfers have no place in a vibrant and still-growing remittance industry.