Briefing Paper

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Remittances: Travails of the Migrants

Thousands of migrants across the world transfer money to their families abroad. The World Bank estimates that a total of US$483bn was remitted in 2011. In the year 2009, 75 percent of such remittances[1] were to developing countries. In many of these countries such funds meet basic needs at home.

India has more than 25 million migrants living across 110 countries. Their remittances to India totalled US$55bn in 2010 – 25 times the amount of foreign aid. However, migrants face a number of problems in effecting such remittances: high costs (up to 10-20 percent of the amount to be remitted); adverse exchange rate, delays etc. arising out of lack of information, inadequate infrastructure, etc.

This briefing paper examines major issues related to international remittances from a consumer perspective and suggests improvements.

Background

Many people, for survival or for seeking improved living conditions for themselves and their families migrate within and across national borders. Such migrations, particularly cross border, have a significant impact on the economies of both the host and the guest countries in terms of transfer and receipt of knowledge, values, behaviour and funds. Over time, a significant impact on the economy, society and politics of both countries has been seen and is important in context of development. There are more than 200 million migrants around the world and total number of migrants from India is about 25 million. These migrants transfer huge resources. International migration is important, since it is influencing economic relations between the developed and developing countries.

Transfer of money to households back home called 'remittance' is the most important exchange which plays a major role in development, technological advancement and economic development. It also plays an important role in developing countries like India in terms of net inflow of foreign exchange amount, which increases the volume of national income and enhances the livelihood of families associated with migrant workers. India was ranked at the top position in the world among the recipient countries of international remittance in 2010 and its total international remittance of US$55mn constitutes around five percent of the national income.

It is generally assumed that in a large economy like India's, the impact of remittances is negligible. But, compared with some important economic and fiscal indicators, its relative importance is significant. The sheer size of these transfers could be understood from the fact that even in 2007-08 when India had record net foreign direct investment (FDI) inflows, private transfers still accounted for over 1.2 times the net FDI to India. Transfer of such a huge amount of money certainly requires involvement of consumers, service providers and certain polices to regulate the service providers to further facilitate this process.

In the last three decades of the 20^{th} century, however, the character of the migrant worker has transformed from unskilled workers to highly skilled professionals but even now a large number of workers in the Gulf and the West Asian region have inadequate labour security arrangements and work as highly underpaid professionals. In most of the cases, the money sent by them covers day-to-day living expenses and provides a cushion against emergencies at home.

Table 1: Countries with highest remittance to India (2010)			
Country	***Amount (in US$mn)***	***Number of emigrants***	***Remittance per emigrant (US$)***
UAE	15,879	21,85,919	7,264
US	15,279	16,54,272	9,236
UK	4,629	6,57,792	7,037
Saudi Arabia	3,339	14,52,927	2,298
Kuwait	2,025	3,93,210	5,150
Australia	1,906	2,09,908	9,080
Singapore	1,167	1,57,114	7,427
Qatar	1,033	2,50,649	4,121
Oman	1,021	4,47,824	2,279
Source: http://www.tehelka.com/			

In 2007-08, the Reserve Bank of India (RBI) recorded US$43.5bn as 'private transfers to India.' Of this, 50 percent was classified as remittances towards 'family maintenance', 43 percent as 'local withdrawals/redemptions from Non Resident Indian (NRI) deposits' and another six percent were classified as personal gifts/donations to charitable/ religious institutions in India (RBI 2010). The data above also indicates that these remittances are small and involve people with low education, income and with capacities often not competent to complain against the service providers, if the services are found poor.

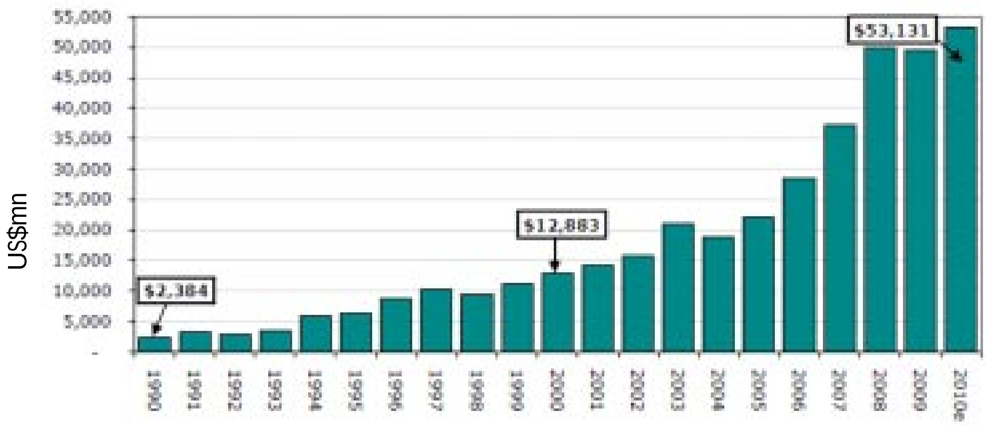
Definition, Process and Types of Remittances

Remittance is the act of transmitting money to a distant place, as in satisfaction of a demand, or in discharge of an obligation. Remittance may be domestic or international. Domestic remittances occur, for example, when there is transfer of funds from urban to rural areas or one part to the other within a country. To a large extent, issues are similar in case of domestic remittances. In this paper, the focus is only on international remittances.

There are different ways through which remittance transfers can be made, including cash-based services offered by individuals, services from specialised global money transfer operators, services offered by card schemes, bank-to-bank and mobile transfers. This process can be more or less complex, convenient, secure or speedy.

However, in all cases some kind of network is required. The network consists of the access points, where consumers of remittance services pay and receive funds and infrastructure to link these access points for message transfer. There are mainly four types of remittances based on the network

Figure 1: Formal Remitances Inflows in India



Source: Remittances data, Development Prospects Group, World Bank, 2011

Unilateral Services

In a unilateral service, a single Remittance Service Provider (RSP) performs the role of both capturing and disbursement agents. This becomes possible when the RSP itself has physical access points in both sending and receiving countries or the network is internet-based. Global or other banks that have set up branches abroad provide unilateral services and/or have correspondent arrangements with other banks.

Franchised Services

A franchised service (for example Global Pinoy Remittance and Services Inc.-GPRS) is where a central provider builds infrastructure to support the service and obtains the necessary access points through franchisee building. Services are partly franchised also when services involves other RSPs infrastructure who is not the franchisee.

Negotiated Services

In a negotiated service (for example bilateral arrangements between banks), an RSP negotiates with a number of other institutions in other countries in order to create an adequate network of access. In this kind of arrangement, the service may be offered through involvement of multiple remittance passages. For example, a bank in India having linkage with its Integrated Treasury Branch and Authorised Forex Branches and other leading banks in important cities for the purpose of international banking.

Open Services

In an open service, an RSP uses an open network to which any RSP can have direct or indirect access. This network makes it possible to send a payment from any bank offering cross-border payment services to virtually any other bank in the world.A recent example is Muthoot Finance launching Western Union money transfer services from its country wide network of 2,800 locations linking them to Western Union's network of more than 4,00,000 locations in over 200 countries aimed at capitalising the huge potential of the money transfer business in India.[2]

Consumer Issues

Pricing

There are several consumer issues connected with the foreign inward remittances ranging from expensive to unreliable to inconvenient to uncompetitive. Migrants face charges of 10 to 20 percent on each of such remittances, with the result that for every ₹100 sent home their families may receive only ₹80 or 90. Figure 2 shows price of remittance from G 20 countries. South Africa and Japan are the costliest remittance sending countries in the G20 group, with an average of respectively 17.73 and 16.84 percent. The cheapest sending countries, together with Russia, are Saudi Arabia (4.13) and Korea (6.36), followed by the US (6.93).

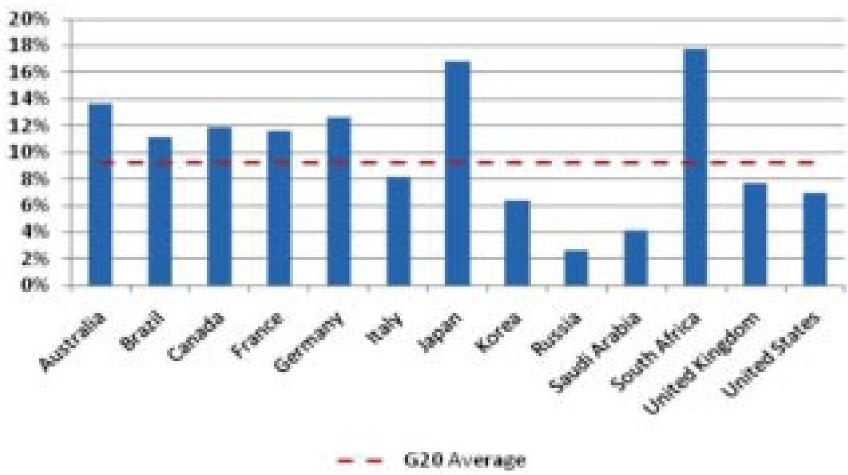
The World Bank estimates that a five point price reduction in remittance costs could result in US$15bn saved annually for immigrants and their families. The social angle of such high costs is two-fold: less money available for use by the migrant in the host country and less money for consumption in the home country.

Some other major issues are:

Lack of Information

Availability of information enables individuals to make informed decisions in any market. This is particularly important in a financial market, related to remittance, as information on exchange rate and other fees is required in order to calculate the cheapest and quickest service. Exchange rates are one of the key factors that consumers consider in choosing RSPs for remittance. As a result, information about exchange rates has the potential to help remitters make well-informed choices about the services which best meet their needs, and to facilitate competition among RSPs.

Figure 2: Average cost of remitting from G20 countries in 3Q 2011



Source: remittanceprices.worldbank.org

Adequate consumer protection is also important because many remitters find difficulties in understanding the foreign language and/or in providing adequate identity proof for opening a bank account. They also lack required financial literacy and time to search and compare different remittance services.

Inadequate Infrastructure

Proper remittance services require support of a well-developed and efficient financial infrastructure or the network of access points. It may not always be easy for service providers to identify suitable partners in other countries particularly in receiving countries, where domestic financial infrastructure is underdeveloped. This has caused slow, insecure and unreliable transfer of funds.

Less Competitive Market for RSPs

The efficiency of remittance services depends on existence of a competitive business environment for RSPs. In general, an RSP allows its agents or other RSPs to offer its remittance service only on condition that they do not offer any other remittance service. Due to this exclusivity condition[3], competition does not flourish in RSPs market and lead towards monopolistic practices of high price and poor services.

Poor or Disproportionate Regulation

The remittance industry needs a sound regulatory framework where the contracts are most likely to be enforced because parties are in different jurisdictions. The regulation should also address concerns of money laundering activities and terrorist financing

Risks

Losing funds (due to the bankruptcy or error of the RSP or one of the intermediaries, or because of fraud) in transit is one of the potential risks for money senders or receivers. The extent of the risk depends on the nature of the contract between the remitter and the RSP and where the problem occurs. The contract between the remitter and the RSP is likely to be to get the funds to the disbursing agent and it will be the RSP's responsibility if this fails to happen. With negotiated and open networks, it may be less clear-cut: at some point in the transaction, responsibility may transfer from capturing to disbursing RSP.

The extent of the risk of loss of funds in transit depends on the nature of the remittance service. For example, the extent and duration of its exposure to the possibility of failure by the disbursing agent depends whether or not it has provided liquidity to the agent. Further, the direct credit or liquidity risk of loss in transit, or the operational risk of a failure on its own part, the RSP also faces reputation risk unless it has adequate arrangements to ensure receivers get their funds on time even when there has been a loss in transit. Reputation risk could also arise from misuse of the service for illegal purposes such as money laundering. Lack of sound governance and risk management practices on the part of RSPs can exacerbate such problems. Add to this the possibility of poor exchange rates offered at the point of origin and delays and charges sometimes levied at the receiving end and one has a murky scenario.

Recommendations

Transparency

Transparency enables an individual to make an informed decision about the services offered in the market. This is particularly important in case of total package (exchange rate applied, direct fee charged, any tax levied) demanded and the time taken.

- RSPs should therefore be encouraged to proactively provide relevant information about their services

Case of State of Kerala: Benefits of Remittance and Problems of Remitters

Kerala is a tiny state on the south west corner of India. As per the census 2011, Kerala has a population of 33.3 million. Kerala leads many other Indian states and territories in terms of per capita GDP and economic productivity and its Human Development Index (HDI) is the best in India and is comparable to Europe. Around three million Keralites are working abroad mainly in the Persian Gulf. Its economy is largely dependent on remittances. In a State of 33 million where unemployment approaches 20 percent, one out of six employed Keralite now works overseas.

As of 2008, the Gulf countries altogether have a Keralite population of more than 2.5 million, who send home annually a sum of US$6.81bn, which was more than 15.13 percent of remittances to India in 2008. Foreign inward remittances augment the state's economic output by nearly 25 percent. Migrants' families are three times as likely as those of non-migrants to live in superior housing, and about twice as likely to have better living conditions having telephones, refrigerators, cars etc. Many migrant workers, working in middle east are unskilled workers, who make small remittances frequently. Though the remittances supplement the economy of the State, the biggest problems faced by the Kerala migrants are high cost of small amount of remittances, loss due to exchange rate fluctuation, delays in payments etc. Those located in an underdeveloped country, further land up in paying exorbitant charges for remittances without having any option of choosing alternatives.

(particularly pricing, processing and timelines) in easily accessible and understandable forms. Authorities and other organisations may also provide comparative price and remittance process information.

- The sector could be encouraged to agree on a common reference exchange rate to be used as a basis for calculating the price of the remittance service.

- Sufficient background knowledge to understand the remittance process with senders and receivers can help them make informed choices.

- As part of financial literacy campaigns, authorities or other organisations may undertake educational campaigns and knowledge dissemination on the characteristics of remittance services.

Appropriate Financial Consumer Protection

- Availability of clear and easily applicable procedures in cases of fraud and disputes should be built up. At least, RSPs can establish their own procedures on independent basis that consumers can follow. An entity, such as an Ombudsman, that could help RSPs and their customers resolve problems might be helpful.

- Some RSPs may consider offering some guarantee, so that if a remittance fails to reach the receiver (because of operational loss in transit or the bankruptcy of one of the parties involved), the sender would get back the money.

Improving Infrastructure

Expanding the payment system infrastructure in rural and under-served areas is a way forward for improving access to financial services of all kinds, including remittances.

- Central banks should initiate and provide leadership, where necessary, in developing the domestic retail infrastructure.

- Business models that profitably support the expansion of the branch of existing RSPs into rural or smaller urban areas, especially in receiving countries, could be encouraged.

- Increased inter-operability of networks can provide increased access to remittance services.

- Organisations having large branch networks, widely accessible in many countries, could be encouraged to play a bigger role in providing remittance services.

Regulatory Frameworks

- At the international level, authorities could assess whether the relevant legal frameworks are consistent and complete and whether undesirable barriers to entry or obstacles to competition exist.

- RSPs should disclose all information related to the remittance and provide a report to the remitter and receiver. They should apply registering and licensing procedures that are proportionate to the service provided, and fees (if any) that are at a reasonable level.

- Consult the remittance industry and other stakeholders when preparing relevant regulation.This will help ensure that their legitimate concerns are considered and that the regulation is as effective as possible without imposing unnecessary costs.

Increasing Competition

Competition can be enhanced by restricting RSPs from imposing exclusivity conditions on their agents. This is important at the source as well as in remittance receiving countries as number of potential agents to provide remittance services is limited in receiving countries involving more cost in the receipt of remittance delivery.

It would be helpful if the regulatory structure for remittances support competitive market conditions. The appropriate authorities may wish to monitor mergers or alliances that could significantly reduce competition for a relevant part of the market.

Payment system operators and their overseers may want to check whether their direct access requirements are consistent with international principles to ensure payment system safety and soundness. Access criteria should be clear, well defined and fair; and access should be granted to all entities, including RSPs, which comply with such requirements.

It may be helpful to improve potential RSPs' awareness of the remittances market. For example, unless they understand the scale of the flows in particular remittance corridors and the possibilities for cross-selling products, financial institutions may view remittance senders and recipients as low-balance, high-risk customers, unlikely to use other services, making them less willing to offer remittance services. General publicity about the scale and importance of remittance flows (e.g. in trade journals or at trade conferences, or through general publicity about any of the other actions taken to implement the Principles) may therefore be useful, particularly for remittance corridors with few existing RSPs. RSPs could also be assisted in their communications with key migrant groups.

Governance

The remittance industry, perhaps in cooperation with the relevant authorities and consumer groups, may wish to establish guidelines for good governance and the management of risks to enhance confidence in remittance services and protect consumers. Such guidelines could be based on those already used in the financial sector but should recognise the diverse nature of RSPs.

The industry might also like to develop ways to help RSPs assess the nature and level of the risks they face, and thus to help RSPs implement any guidelines in a way that is appropriate for their business.

Given the particular importance of Anti-money laundering (AML)/Combating the financing of terrorism (CFT) regulations, the authorities and the industry may want to cooperate in order to develop guidelines on how to meet such regulations in a way that is effective and appropriate for different types and sizes of RSPs.

Where RSPs outsource functions to those who provide services in the RSP's name (eg capturing and disbursing agents), they should satisfy themselves that those carrying out the outsourced functions also meet appropriate governance and risk management standards and comply with relevant regulations.

Conclusion

Indians remitting funds from abroad back home are facing numerous obstacles in getting a fair deal. Research indicates that a large number of remitters is illiterate and has no education beyond the secondary level and generally do not understand the language of the host country. Most of them do not have a commercial bank account also and are very likely to be earning below the average per capita earnings per household for the host nation. In a 2010 survey of 1,000 remittance senders living in the US, 90 percent utilised cash-to-cash remittance transfer method. Only three percent used banks, two percent utilised the internet and four percent used other means. In contrast to the low incomes of many of their customers, market leaders, Western Union and MoneyGram earned profits of 7 and 15 percent respectively in the Q2 of 2011 based on the Q2 of 2010 earnings.

Like any consumer of financial services, those who are making such remittance also have a right to make an informed choice from a range of products and services offered at competitive price so that they can transfer the money safely. For ensuring all the consumers' of remittance a fair and secure service, the government need to do the needful to ensure adequate transparency, competition, regulatory measures, improved infrastructure and governance.

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ENDNOTES

1. A remittance is a transfer of money. In this paper it refers to transfer of money to the home country by migrants working overseas.
2. The Hindu, June 04, 2011
3. Exclusivity conditions are where an RSP allows its agents or other RSPs to offer its remittance service only on condition that they do not offer any other remittance service.

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