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The Impact of Remittances: Observations in Remitting and Receiving Countries

Raul Hernandez-Coss[1]

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[1] Raul Hernandez-Coss is Financial Sector Specialist of the Financial Market Integrity in the Finance and Private Sector Development Vice-Presidency of the World Bank. The author would like to thank Chinyere Egwuagu Bun, Latifah Merican Cheong and Kamil Borowik , World Bank, for their contributions and comments to this paper. The views expressed in this paper are those of the author and should not be attributed to the World Bank.

Contents

Contents 3
Abbreviations 4
Introduction 5
Bilateral Remittance Corridor Analysis 6
Outline of the paper 7
I. The Development Impact of Remittance Flows 8
Remittances are the economic expression of migration 8
Sending and Recipient countries 9
Remittances Effects 10
Formality of Flows 11
II. Issues Observed in the Remitting Countries 14
Determinants for choosing Remittance Transfers Mechanisms 15
Transfer Cost for Remittances 18
Regulating Remittance Systems 21
III. Issues Observed in the Receiving Countries 24
The Use of Remittances 24
Remittance Distribution arrangements limit market development 26
Using Remittances to Bank the Unbanked 29
IV. Conclusions 30
Bank's Lessons on Bilateral Remittance Corridor Analysis 30
There Is Need for Policies Involving Both Sender and Recipient Countries. ... 31
The Challenge of Converting Remittance Transfers into an Entry for a Broader Access to Finance. 32
Bibliography 33
Annex A 37
Improving Data Recording of Remittance Flows 37
Annex B 38
The CPSS/World Bank Task Force for General Principles on International Remittance Systems 38
Annex C 39
The Requirements of the FATF 40 plus 9 Recommendations for Alternative Remittance Systems (ARS) 39
Annex D 40
Cost of sending US$200 from the U.S. to and Number of Companies Operating Mexico, El Salvador, Jamaica and Gautemala (2001-2005) 40
Annex E 41
Excerpts from BRCA case studies 41

Abbreviations

ADB	Asian Development Bank
AML/CFT	Anti-Money Laundering and Combating the Financing of Terrorism
BDC	Bureau de Change
BRCA	Bilateral Remittances Corridor Analysis
CDD	Customer Due Diligence
CFT	Combating the Financing of Terrorism
CPSS	Committee on Payment and Settlement Systems
DFID	Department for International Development
FATF	Financial Action Task Force
FDI	Foreign Direct Investment
FFT	Formal Funds Transfer
FX	Foreign Exchange
GDP	Gross Domestic Product
IADB	Inter-American Development Bank
IFT	Informal Funds Transfer
IMF	International Monetary Fund
IMO	International Money Order
IOM	International Organization for Migration
ISTAT	Italian Statistical Office
KYC	Know Your Customer
ML	Money Laundering
MTO	Money Transfer Operators
NCCT	Non-Cooperative Countries and Territories
ODA	Official Development Assistance
OECD	Organization for Economic Co-operation and Development
RCP	Remittance Country Partnership
RSP	Remittance Service Provider
STR	Suspicious Transaction Report

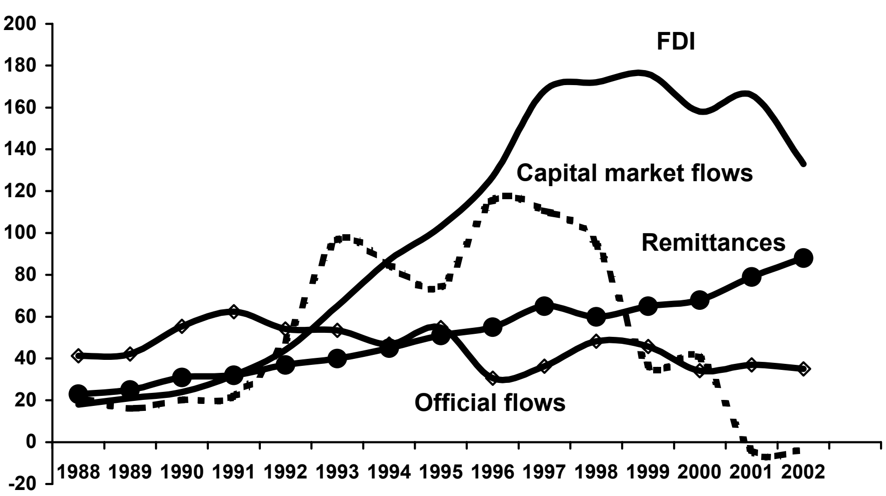
Introduction

Remittance flows are an important source of funds for many developing countries. Worker Remittances have been growing rapidly in the past few years and now represent the largest source of foreign income for many developing countries. It is hard to estimate the exact size of remittance flows because many transfers take place through unofficial channels and therefore are not capture by authorities. Worldwide, officially recorded international migrant remittances are projected to exceed $232 billion in 2005, with $167 billion flowing to developing countries[2]. After 1997, the flow of recorded remittances grew much faster than Foreign Direct Investment (FDI).

Unrecorded flows through informal channels are believed to be at least 50 percent larger than recorded flows. Not only are remittances large but they are also more evenly distributed among developing countries than capital flows, including foreign direct investment, most of which goes to a few big emerging markets. In fact, remittances are especially important for low-income countries.

Remittances account for a major – and increasing – proportion of financial flows to developing countries. Rising international migration in part accounts for increased global remittance flows, though a number of other factors, including a reduction in remittance costs and increased recording of flows after September 2001, are also responsible for the trend captured in **Figure 1** below

Figure 1. Remittances Flows and Other Capital Flows (1988-2002)



Source: World Bank. Global Economics Prospect Report 2006.

[2] World Bank estimates.

Bilateral Remittance Corridor Analysis

The analysis of remittance corridors is one of the ongoing efforts to better understand and monitor the size and nature of these flows, the incentives that influence them, and the mechanisms through which they are transmitted, in order to develop policies to lower their transaction costs, enhance their developmental impact in the recipient countries, and minimize opportunities for misuse. This analysis is based on the assumption that encouraging senders to channel a growing proportion of remittances through formal financial institutions will further all of these objectives.

The "formalization" of remittance flows can open the access of both senders and receivers to other financial services, providing both additional income-earning opportunities and enhanced capacity to manage their financial risks. An important objective of the Bilateral Remittance Corridor Analysis (BRCA) has been to develop a better understanding of the incentives and other factors that shape the remittance markets in sender and recipient countries in order to promote effective policies for inducing that shift. Given resource limitations, the paucity of remittance data and the desire to catalyze an expanded research effort across a broad range of countries, an important short-term objective of the BRCA studies is to identify the most important information gaps that require follow-up work. These studies on individual corridors have served to confirm many of the tentative conclusions reached by more global-level analysis, as well as fleshing out the incentives that shape remittance decisions at the micro level[3].

A comparison among the case studies is currently under preparation and will be presented in early 2007. It will discuss findings from the cases studies on remittance corridors and map common issues present throughout sender and recipient countries. First, it will examine the issues surrounding the demand for such services. Then it will analyze how the Remittance Service Providers (RSPs) respond to the demand for the use of transfer mechanisms in the corridors. Finally, the paper will present best practices for policy makers that facilitate the efforts of RSPs to meet the demand of both senders and recipients.

Table 1. World Bank's Bilateral Remittance Corridor Analysis (BRCA), 2006[4]

Published	*Completed / Under Review*	*Underway*
US - Mexico	U.K. – Nigeria **	U.K./ U.S. / South Africa – Uganda ***
Canada – Vietnam	Netherlands – Suriname*	
Germany - Serbia	Qatar – Nepal	Malaysia / Country in the Gulf Region – Indonesia
U.S. – Guatemala	Italy – Albania	

[3] When studying the impact of remittances it is important to rely on recipient households. In some cases, BRCAs relied on existing surveys and interviews with local experts, market participants, and other secondary sources.

[4] * Conducted by the Ministry of Finance of the Netherlands, ** Partnership with DFID, *** Partnership with Central Bank of Uganda.

Outline of the paper

The World Bank's Financial Market Integrity Unit, in keeping with the Bank's development mandate, has been studying remittance flows through ongoing bilateral remittance corridor analyses. This paper presents preliminary findings from 9 bilateral remittance corridors and the World Bank's 2006 Global Economic Prospects Report on Migration and Remittances.

This paper presents lessons learnt when conducting bilateral analysis of remittance flows and is organized around fours sections:

- Section I or *The Development Impact of Remittance Flows,* focuses on the development impact of remittances flows based on the main findings from the World Bank's Global Economic Prospect Report 2006 on Migration and Remittances.
- Section II or *Issues Observed in the Remitting Countries* focuses on the motivations and deterrents for remittance senders in choosing whether to use formal or informal transfer mechanisms, their cost and regulatory framework affecting them in remittance sending countries.
- Section III or *Issues Observed in Recipient Countries*, focuses on the microeconomic impact of remittances for the individual beneficiaries in the developing countries describing the use of remittance flows, their distribution and how these flows have been linked for banking the *unbanked* for remittance beneficiaries.
- Section IV presents some *Conclusions* for consideration of authorities and policy makers in sending and receiving countries for developing appropriate regulatory and supervisory controls, new remittance products, and payments infrastructure.

I. The Development Impact of Remittance Flows[5]

Workers' remittances are a recognized significant source of external funding for developing countries. They have counter cyclical effects in stabilizing household incomes during periods of economic distress.[6] Therefore, since remittances have tended to be more stable than private capital flows, by strengthening financial-sector infrastructure and facilitating cross-border transfers of funds, countries could increase the development impact of remittance flows.[7] Studies in this area address questions like the effects of remittances on poverty, on financial development and, at a macro level, the impact of remittances on recipient countries.

Remittances are the economic expression of migration

The international migration of workers is driven by economic and demographic trends. Remittances that result from these migration trends have significantly influenced financial development and help the poor to manage adverse effects of financial crises and natural disasters; aggregate markets, such as the exchange rate markets and international trade, are also affected by remittance flows. Rising international migration accounts for increased global remittance flows, along with other factors, including a reduction in remittance costs and better recording mechanisms for remittances[8]. Recent World Bank regional studies for the Middle East and North Africa and Latin America highlight the importance of remittances for the regions, estimating that they are four to five times larger than ODA, respectively.[9]

Policies implemented in remittance sending countries, as well as the degree of formality for remittance transfers, can affect the development impact of these flows in recipient countries. High-income countries are the main source of remittances, but it is possible that considerable amount of remittances are also transferred among developing economies. Some studies demonstrated that corridors in which Informal Funds Transfer (IFT) systems were prevalent have shifted to a market now dominated by formal mechanisms.[10] Formalization of remittance flows open the possibility of approaching remittances from a banking perspective that can offer a range of financial

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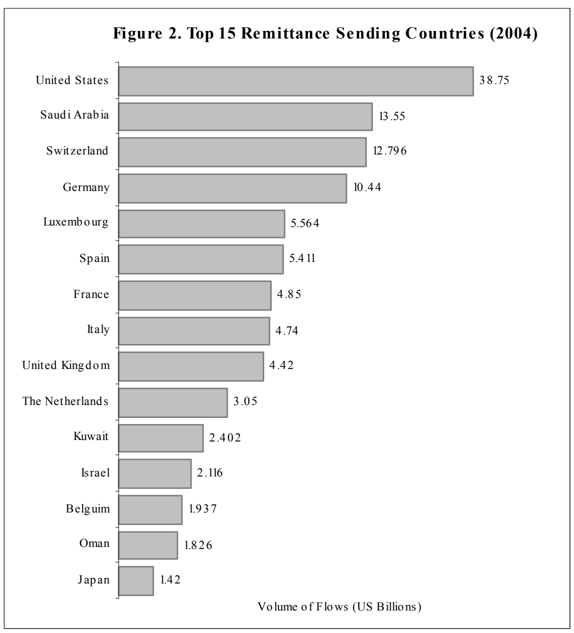
[5] This section was prepared with guidance from Dilip Ratha. .
[6] IMF Staff Papers. Vol. 52, No.1, 2005. The authors confirmed the countercyclical effect of remittances flows based on aggregate data on remittances, but imply that remittances do not act like a source of capital for economic development.
[7] Dilip Ratha. 2003. "Workers' Remittances: An Important and Stable Source of External Development Finance." *Global Development Finance, Chapter 7.*
[8] For example, central banks in Mexico and Guatemala have improved the recording of remittance flows in recent years coinciding with implementation of new AML/CFT legislation.
[9] "The Development Impact of Remittances in Latin America" (2006) and "Middle East and North Africa Migration: Stakes, Outcomes and Prospects". Regional Study. Human Development Department MNA. World Bank (2006, forthcoming).
[10] Examples are the US-Mexico and US-Guatemala remittance corridors.

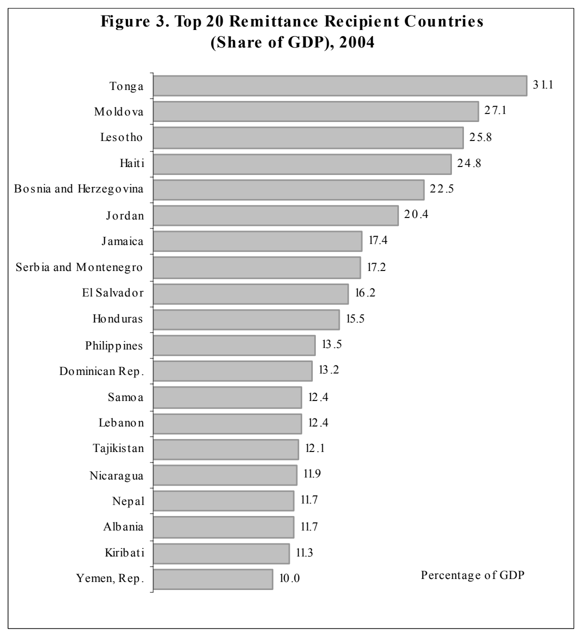
services to migrant households beyond the *cash-to-cash* transaction offered traditionally by banks [11].

Sending and Recipient countries

In recent years, China, India, Mexico, Pakistan, and the Philippines have witnessed a remarkable increase of remittance inflows. Even though most top recipient countries are large, remittances in many small developing countries (e.g., Lebanon, Lesotho, Tajikistan, and Tonga) are significant as a share of GDP or in per capita terms.

High-income countries are the main source of remittances. In 2004, the United States was by far the largest source, with $39 billion in outward flows. Saudi Arabia was the second largest, followed by Switzerland and Germany. However, when expressed as a share of GDP, outward remittances were the largest in the upper middle-income countries (0.7 percent of GDP compared to 0.2–0.4 percent of GDP in other countries). Although it is conventionally believed that migration flows are South-North, and remittance flows North-South, South-South migration is estimated to be at least as large as South-North migration and South-South remittances are 30–45 percent of the remittances received by the South[12].





Source: World Bank. Global Economics Prospect Report 2006.

[11] This trend is observed in corridors that originate in Spain, where banks and cooperative banks have developed a range of financial services that include mortgages, insurance products and banking accounts,
12. World Bank (2005).

Remittances Effects

Studies suggest that remittances may raise per capita income and reduce poverty in some countries.[13] For instance, a 10 percent increase in the share of remittances to GDP in a given country would lead to a 1.6 percent decline in the share of people living in poverty[14]. Remittances may have reduced the share of poor people in the population by 11 percent in Uganda, 6 percent in Bangladesh, and 5 percent in Ghana.[15] In China, where more than 150 million people are internal migrants, the second most important factor for lifting a household out of poverty is, precisely, the reporting of a migrant in the family.[16] However, this is not the rule: in the Latin American and the Caribbean region, remittances have been found to reduce poverty headcounts in only 6 out of the 11 countries for which data is available.[17] But even where remittances do not pull households out from below the poverty line, the severe effects of poverty are reduced. For instance, among Guatemalan households in the poorest 10% of the population that also receive remittances, they account for a very large share of the total income (up to 50-60 percent) of those households.[18]

Remittances also improve human development outcomes. Generally, remittance recipient households spend more on health care and have higher school attendance rates. Studies based on household surveys in El Salvador and Sri Lanka show that children from remittance receiving households have a lower school dropout rate and that these households spend more on private tuition for their children. In the Philippines, a 10 percent increase in remittances leads 1.7 percent increase in school attendance, and a 0.35- hour decline in child labor per household per week.[19] In Guatemala and Nicaragua, children whose parents receive remittances exhibit higher health outcomes than those from non-recipient households, with similar demographic and socio-economic characteristics.[20] Human capital improvements are not associated with the sending of remittances alone. Remittances assist the poor during macroeconomic shocks. In many cases, remittances are counter-cyclical, as migrants are prone to send more money to help their families and friends during crises.

There is evidence that remittances can have negative effects, making recipients dependent on these flows without leveraging them to generate additional income. Remittances have been used to substitute low levels of income resulting from scarce and low wage jobs, but have not resulted in significant increases of other sources of financing

[13] The assessment of the impact of migration and remittances on households' income (or poverty) is plagued by selectivity and endogeneity problems that are addressed in some studies (Adams, 2006) but do require further refinements.
[14] Adams, R and J. Page, 2003.
[15] World Bank (2005).
[16] World Bank (2006).
[17] World Bank (2006).
[18] Cheikhrouhou, Hela; Jarque, Rodrigo; Hernandez-Coss, Raul; and El-Swaify, Radwa. 2006. 'The US-Guatemala Remittance Corridor: Understanding Better the Drivers of Remittances Intermediation". World Bank.
[19] World Bank.(2005).
[20] Controlling for income and demographic characteristics – results are robust of 6 of the 11 countries – showing that access to remittances is positively and significantly associated with higher educational attainment in Nicaragua, Guatemala, Honduras, Ecuador, Haiti, and El Salvador. (LAC)

in most the corridors analyzed. Families can tend to take these resources for granted and grow dependent on them; undermining the motivation to develop additional work skills or make investments to generate additional income. For example, in Guatemala there is a perception that migration and remittances are leading young people to drop out of school and aspire to migrate[21]. Many youth do not study or work, but rather wait until they are old enough to migrate to the U.S. Moreover, it is estimated that the average stay of migrants in the U.S. is on the rise.

However, the effect of remittances on labor force participation rates varies between countries. Research conducted by the World Bank in the Latin American and Caribbean region shows that remittances have the effect of reducing both labor force participation rates and the number of hours worked per week in most countries for which data is available, though the reduction in labor supply caused by remittances is much lower among individuals with higher levels of schooling.[22] But a much more positive effect of remittances on labor supply has been detected in the Philippines, where an increase in remittance flows in the wake of the Asian financial crisis led to reduced child labor (and increased schooling) and an increase in adult employment in entrepreneurial and capital-intensive activities.[23]

Formality of Flows

Informal Funds Transfer (IFT) systems have provided valuable efficient services at low cost. These systems are important transfer mechanisms in places where conflict, poverty, or remote geography have prevented formal financial infrastructure from being built, for example in rural areas throughout Latin America and Asia. The formal sector can learn and adapt their practices to provide similar services. Several initiatives have explored ways to shift legitimate IFT flows into formal sector channels, where these legitimate money flows can have a positive impact on the formal financial sector[24]. At the same time, law enforcement can better focus their efforts on the illegitimate flows left in the informal sector.

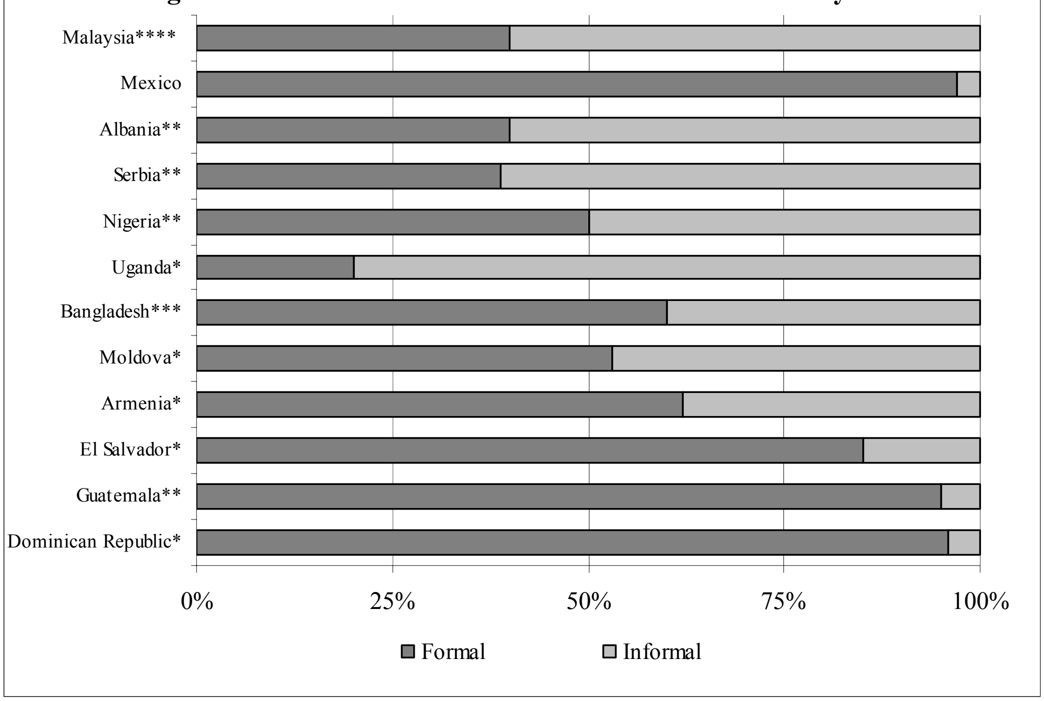
So far a handful of private sector entities and governments have been collaborating to promote a shift from informal to formal transfer mechanisms. New products, incentives and policies to encourage individuals and institutions to use formal remittance systems include card-based programs, international networking initiatives, and banking- and account-based programs. In most cases governments focus on regulating the financial sector, relying on market participants to devise creative ways to stimulate the formal remittances market. Private institutions, however, tend to be more concerned with

[21] The tangible "benefits" of leaving hometowns seems to overshadow the challenges and poor conditions in which migrants cross the borders. Cheikhrouhou, Hela; and Etal. 2006. 'The US-Guatemala Remittance Corridor". World Bank.
[22] World Bank 2006.
[23] Yang, D. 2005 (b).
[24] The APEC Remittances Initiative set of priority policy action areas aim to build on the lessons learned throughout the course of the initiative, as well as through international and bilateral activities on remittances. These actions were intended to guide APEC member economies on how to maximize the potential development impact of remittance flows, while ensuring the integrity, and to facilitate the provision of higher quality and lower cost remittance services.

regulatory compliance, rather than responding to market demands for creating innovative remittances products. This is in large part due to the lack of a business model that can guaranty returns in the short term while addressing the overarching reputational risk associated with money laundering and terrorist financing; a risk inherent in any venture that involves the international transfer of funds.

A reliance on informal channels has implications at the household, country and international levels. First, a lack of competition results in high transaction costs and erodes the income of migrants and remittance recipients. While informal channels operate on the basis of trust, it is not uncommon for remitters to become victims of fraud, depriving households of income. Second, developing countries do not benefit from the financial deepening effects associated with formal remittance channels. Finally, it is difficult to track money used for illegal purposes, such as money laundering or terrorist financing.

Figure 4. Estimated Use of Formal Vs. Informal Transfer Systems



Source: * GEP 2006, ** BRCA, *** ADB

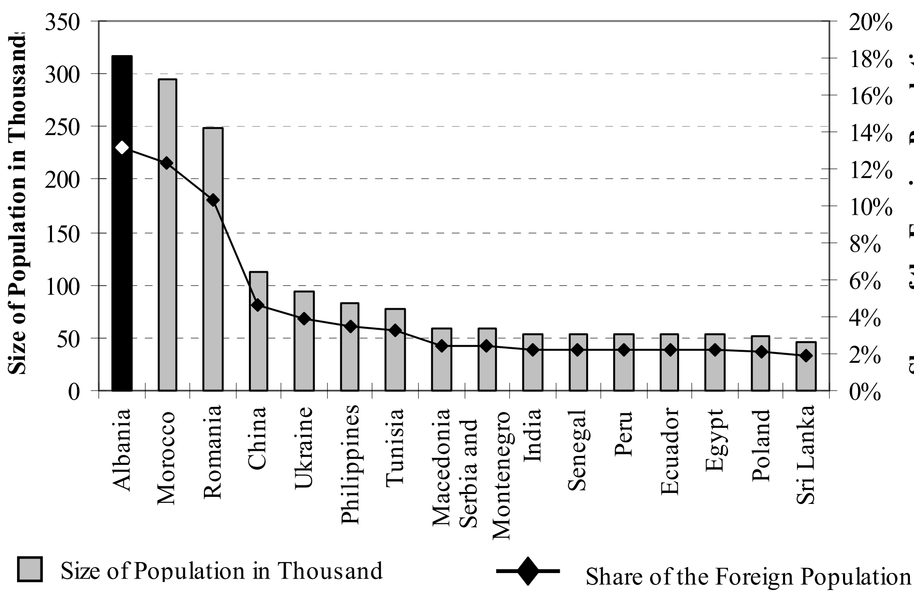
An easing of remittances flows need to be carefully balanced with tightening regulations to control money laundering. The goal of improved market contestability is often times perceived by policymakers as being at odds with security concerns and, in particular, post-September 2001 regulations for countering money laundering and the financing of terrorism. Constant vigilance is necessary to strike the correct balance between enabling market entry and ensuring international security. However, the two goals are not mutually exclusive. As a greater number of RSPs enter the regulated market at competitive levels, they will eventually do away with the shadier world of informal remittance services, which often exist when formal options are absent or prohibitively expensive.[25]

[25] World Bank 2005 (b).

II. Issues Observed in the Remitting Countries

The determinants for choosing a remittance transfer mechanism, its cost structure and the regulatory framework applied to this type of operation are affecting the development impact of remittance transfers. In each remitting country, there are remittance corridors that reflect migration flows. In the European Union, most migrants live in Germany, France, the Netherlands, Spain and Italy[26]. Just in the case of Italy, there are at least seventeen remittance corridors making the country one of the 10 largest remittance providers in the world and the sixth largest in Europe[27].

Figure 5. Size and Relative Share of the Largest Migrant Populations in Italy (2005)



Source: ISTAT (2005).

The evolution of each remittance corridor is unique, reflecting different historical factors and levels of institutional development at a bilateral level. Each corridor is shaped by the incentives which influence remittance senders' decisions regarding how to transfer remittances (See Annex E.1). In most cases, senders determine which mechanism will be used to send remittances, but this decision is heavily influenced by the circumstances of the recipient; i.e. where are the recipients located and what are the available mechanisms to reach them. The structure of the remittance market in the sending countries impacts recipient countries in terms of access to formal mechanism to the senders, their cost and transparency of the flows.

[26] European Investment Bank. 2005.

[27] Albania, Morocco, Romania, China and Ukraine are main remittance corridors originated in Italy. The Italy-Albania Remittance Corridor. World Bank.

Policy makers in receiving countries have little or no influence on the factors that influence senders to make transfers, how the transfers are processed, the remittance market structure or price determinations. It is at a corridor level, where countries could develop bilateral agreements between the private sector and governments that could serve as a framework to implement specific policies to make more efficient remittance transfers in a corridor[28].

Box 1. Examples of Bilateral Partnerships on Remittances

The Department for International Development (DFID) has initiated Remittance Country Partnerships (RCP) with select countries namely Nigeria, Bangladesh and Ghana, which all receive large volumes of remittance transfers from the UK. These partnerships include a range of measures to remove impediments to remittance flows, improve access, and the terms of that access, for low-income and rural people to remittances and other financial services in both sending and receiving countries, and to strengthen the capacity of the financial sector to provide efficient and widespread transfer payment services. DFID together with other UK partners conducted a UK Remittance Product Survey that provides comparable and accessible information on products and services to remittance senders.

The US and Mexico launched an initiative called "Partnership for Prosperity", a private-public alliance to harness the power of the private sector to foster an environment in which no Mexican feels compelled to leave his home for lack of jobs or opportunity. The Partnership produced a concrete action plan, which includes the objective of lowering the cost of remittance transfers originated in the US to Mexico.

In Southeast Asia, Japan concluded a bilateral agreement with the Philippines and Malaysia to facilitate workers' remittance and improve access to financial institutions in 2004. Malaysia has worked out special institutional arrangements to facilitate remittances transfers to Nepal. Other countries have engaged in a dialogue with their counterparts, but they do not necessarily include issues related to remittances.

Source: World Bank, DFID, ADB

More specifically, policymakers in the sending countries should take note of the incentives that shape senders' choices among the various alternatives for transfer mechanisms. Senders are generally concerned about the cost, speed and reliability of transfers, and authorities in the sender countries should understand how their policies and the existing legal and regulatory frameworks impact on these factors. Sender choices are also shaped, by cultural background, past experiences with financial institutions, legal status in the host country, level of financial sophistication, and by economic policies and the quality of remittance delivery infrastructure in their respective home countries. These factors may vary significantly among migrant groups within the same sender country.

Determinants for choosing Remittance Transfers Mechanisms

Cost, speed, cultural familiarity and service reliability have been identified as the main determinants for choosing transfer methods. However, other incentives may be deemed more important in individual circumstances and particular remittance corridors.

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[28] All of the BRCA studies are composed of "North-South" pairs: that is, remittance flows from advanced, high-income countries to lower-income, developing countries. The UK-Uganda Remittance Corridor Analysis includes also the corridor between the US and South Africa. The latest will represent the first South-South corridor analysis conducted under this initiative.

These incentives may include access to rural areas, confidentiality, confidence in banks, and access for undocumented workers. Not only does choosing a method for remitting money mirror the conditions and surroundings of the remitter, but also the needs of the recipient in order to make the transfer as convenient as possible.

Box 2. Access to Formal Fund Transfer Mechanisms for Undocumented Workers

As in other host countries, undocumented workers in the US appear to have limited access to financial services due to the lack of a proper ID. For example, the same situation is observed in the U.K. among undocumented Nigerians and in Italy when foreign workers' worked permit expiries. For example, estimates indicate that around 70 percent of Guatemalans in the United States do not enjoy a legal migratory status in the host country. This places them in a precarious condition versus immigration authorities and exposes them to the risk of being deported, which further alienates them from access to the formal financial establishment.

In the U.S. the recent acceptance of Consular Identification Cards (CICs) by some banks ha partially mitigate the risk of preventing undocumented migrants' access to banking services. These are issued by consulates regardless of migratory status in the United States. Only the Mexican Consulate in Chicago issued more than 150,000 CICs in 2004, which are accepted by 44 banks in its jurisdiction. Guatemala's Consulates have issued more than 70,000 CICs since it was created six years ago.

In other remittance sending countries, authorities have taken measures to promote greater access by migrant workers to financial services and financial institutions. For example in 2004, Italian authorities formulated an "Action Plan on Remittances", which calls for the expansion of banking services to migrants in Italy*. Among other measures, the Plan encourages market participants to take specific actions to motivate migrants to use regulated institutions to transfer money home.

* The plan was formulated by Italian Ministry of Economy and Finance

Source: World Bank. The US-Guatemala, Italy-Albania, US-Mexico and UK-Nigeria Remittance Corridors.

The sender will choose the method of transfer and, more importantly, whether or not the remittance will be sent by formal or informal means. Senders' decisions will affect the ability to counter the movement of illegal funds, provide greater access to finance for senders and recipients, and assist in the collection of data to better calculate the developmental and financial contributions remittances have to domestic and global economies. Many senders are drawn to the informal systems because they offer cheaper rates, a greater sense of cultural understanding and belonging, and more suitable methods for reaching recipients off the "paved road."[29]

A deterrent to choosing formal systems is a migrant's perception that banks are tied to legal authorities if the worker is undocumented. Internal policies of many banks in remittance sending countries prescribe that only account holders can have access to banks to send and receive money transfers[30]. These internal procedures tend to limit access to banks to the group of migrant workers that are not documented by authorities. For

[29] The US-Mexico Remittance Corridor, pg 71.
[30] France, Germany, Italy, the U.K. are example of countries with these policies, which in many case are not the result of regulations or guidelines from authorities but their own internal compliance procedures.

example, Italian banks usually, however, do not open accounts to foreigners who are unable to provide evidence of their legal residence in Italy.

Table 2. Observed Incentives for Senders and Recipients in Selected Remittance Corridors, 2005-2006

Observed Incentives on Choosing Fund Transfer Systems * Incentives for senders ** Incentives for both senders and recipients ▲ Incentives for recipients which could influence sender's decision		**Remittance Corridors**								
		U.S. - Mexico	**U.S. - Guatemala**	**Canada - Vietnam**	**Germany - Serbia**	**U.K. - Nigeria**	**U.K. - Uganda**	**Italy - Albania**	**Qatar - Nepal**	**Netherlands - Suriname**
Personal Incentives	Anonymity/Secrecy	*		▲		*		*		
	Cultural Familiarity	*		*		*	*	*	*	*/3
	Personal Contacts	**		**		*				
Customer Service Incentives	Dispute Resolution									
	Accessibility	**	*	▲		**			**	**/5
	Class Discrimination									
	Reliability		*					**		*/1
Economic Incentives	Speed	**	*	*	*				*	*/2
	Cost	*	*	*	*			*	*	*/4
	Secondary Benefits	*							*	
	Legal/ Regulatory Environment	**		**		*		*		

Source: World Bank Report on BRCAs *(Forthcoming)*

Banks in the large remittance-sending countries generally do not view remittance transfer services as an attractive line of business. In some countries, consumer loans, mortgages or other kinds of retail banking activities are viewed as more profitable than remittances (See Annex E.2). Nonetheless, with the rapid growth of funds transfers by migrant workers, banks are becoming more aware of the business opportunity in developing financial services, including remittances, specially tailored to the different migrant groups[31]. Although some financial institutions in the various corridors have

[31] Recently for example, the American Bank of Albania, which has a subsidiary in Greece, introduced a mortgage product that allows migrants and beneficiaries of remittances to purchase a house using the regular cash flow from remittances that originate in Greece.

reached out to undocumented workers, the problem still persists[32]. Identification is a requirement in most countries to open a bank account and sometimes to gain access to an MTO or other formal service. In the UK, for example, in order to use banking channels personal ID, such as a passport, driving license, and a utility bill, is required. Because of these regulations, persons that are not of legal status or simply do not have the requisite ID have limited access to formal financial services."[33]

Transfer Cost for Remittances

The cost of sending remittances varies throughout corridors. It is determined by the level of competition, relative size of the remittances volume and reflects the limited expansion of the financial sector in developing countries, particularly among the poor. Determinants of pricing are affected by exchange rates and regulatory barriers for RSPs in both sending and recipient countries. Transaction costs are not usually an issue for large remittances (made for the purpose of trade, investment, or aid), because, as a percentage of the principal amount, they tend to be small, and major international banks are eager to offer competitive services for large-value remittances. But in the case of smaller remittances—under $200, which is the average transfer amount for migrant workers in most corridors — remittance fees can be as high as 10–15 percent of the principal. (See Table 3).

[32] See Annex E.2. for some initiatives that banks have started to attract migrant workers into the formal sector.
[33] The UK-Nigeria Remittance Corridor, (*forthcoming*).

Table 3. Transfer Cost of US$ 200.00 (As percentage of principal), 2005

Remittance Corridor	*Major MTOs*	*Banks*	*Other MTOs*	*Informal Fund Transfer Providers*
Belgium – Nigeria	12	6	9.8	-
Belgium – Senegal	10	-	6.4	-
Hong Kong – Philippines	4.5	-	-	-
New Zealand – Tonga	12	3	8.8	-
Qatar – Nepal	3.4	2	2	1-2
Russia – Ukraine	4	3	2.5	1-2
South Africa – Mozambique	-	1	-	-
Saudi Arabia – Pakistan	3.6	0.4	-	-
UAE – India	5.5	5.2	2.3	1-2
United Kingdom – Philippines	-	0.4 -5.0	-	-
United Kingdom – Nigeria	5	10	-	-
United States – Colombia	-	17	10	-
United States – Mexico	5	3	4.7	-
United States - Philippines	1.2 - 2	4 -1.8	-	-
United States – Guatemala	6-5	4	-	-

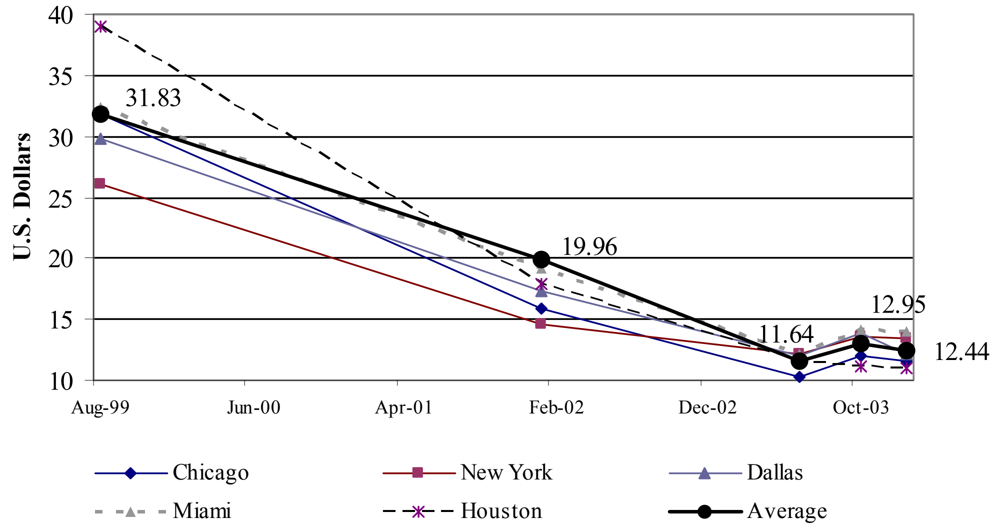
Source: World Bank *Global Economic Prospects 2006: Economic Implications of Remittances and Migration.* World Bank Reports on *Bilateral Remittance Corridor Analysis*.

Cost also varies depending on the remitting institution. For example in the UK-Uganda corridor, banks charge between 7 to 15 percent per transaction, while MTOs (other than Western Union and MoneyGram) charge 3 to 5 percent to East Africa. Western Union charges 14 and 37 pounds for sending 100 and 500 pounds respectively, in addition to less favorable foreign exchange rate. For the ethnic based MTOs fees are normally included in the quoted exchange rate and vary with operator but are usually between 2 to 3 percent per transaction[34]

Generating market competition among RSPs helps reduce remittance costs in a corridor. If a market has a broad array of competing RSPs, this dynamic leads to innovative and cost-effective remittance products. This ultimately drives down prices for the remitter. In the U.S.-Mexico corridor, for example, the steady decline in prices and reduction of business costs followed the increase in the variety of market competitors (See Figure 6).

[34] Preliminary findings from The UK-Uganda Remittance Corridor. World Bank. *(forthcoming)*

Figure 6. Cost Reduction in the US-Mexico Remittance Corridor, 1999-2004

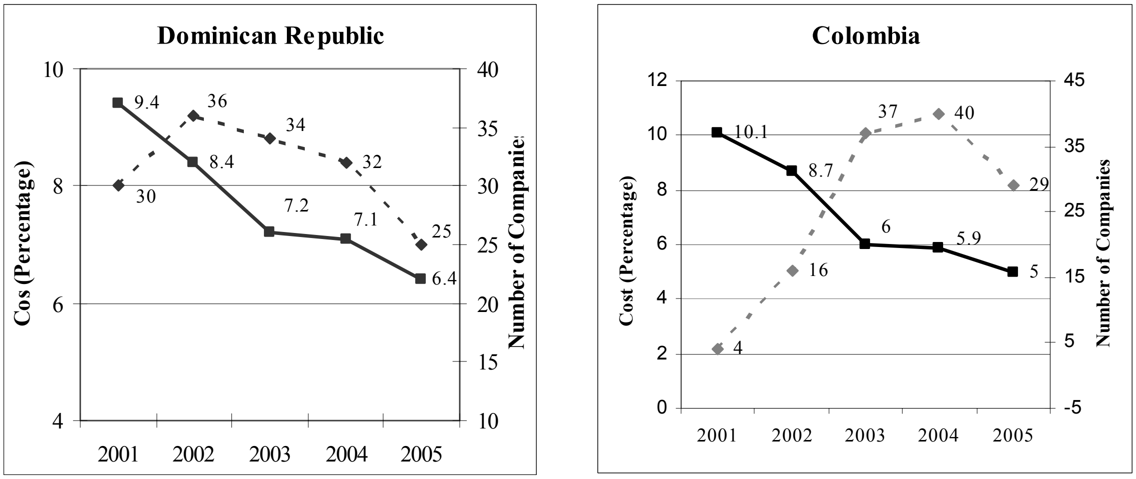


Source: BANSEFI.

This process has also been exemplified in Qatar-Nepal, where competition has driven down the price for formal RSPs. The Inter-American Bank (IaDB) has been actively promoting policies to reduce transfer cost and recently. One IaDB study shows a decline in transaction cost among RSPs over the past five years, the result of which has come from an increase in competition and a growing interest on the part of banking institutions in the sending (mainly the US) and recipient countries in providing financial services to immigrants and their households[35]. (See Figure 7 and Annex D).

[35] According to research conducted by the Inter-American Development Bank, the acquisition and consolidation of businesses reflects the profitability of the remittance industry as well as its competitive environment. This competition has translated into a decline in cost to the consumer. The decline can also be attributed to certain factors such as aggregate remittance volume, the amount sent, or the exchange rate. Orozco. 2006.

Figure 7. Cost of sending US$200 from the U.S. to and Number of Companies Operating Dominican Republic and Colombia (2001-2005)



Source: Data compiled by Manuel Orozco. "International Flows of Remittances: Cost, competition and financial access in Latin America and the Caribbean- toward and industry scorecard". IaDB. 2006

Regulating Remittance Systems

Countries take different approaches when implementing rules that regulate financial market integrity, establish prudential requirements for RSPs, and create consumer protection mechanisms for remittance recipients[36]. In recent years, much attention has been given to AML/CFT regulations while other rules and regulations that could create greater barriers and costs on development have not given the same attention for example consumer protection. In most of the analyzed cases, remitting countries have general concerns about the integrity of remittance systems and their impact on the rest of the financial system - or potential for development in recipient countries -, particularly reputational risks stemming from ML/FT considerations. Recipient countries see regulations as a possible way to complement other policy measures they have in place, e.g. currency restrictions or current and capital account controls[37].

Integrity concerns regarding remittance flows have increased since 2001. Special attention was given to the possibility of funds transfers by terrorist through informal banking systems that lack transparency associated with the formal sector[38]. The heightened scrutiny and increased oversight of the formal sector has increased the propensity for transactional criminals to try laundering their profits via the less regulated underground banking sector.[39]

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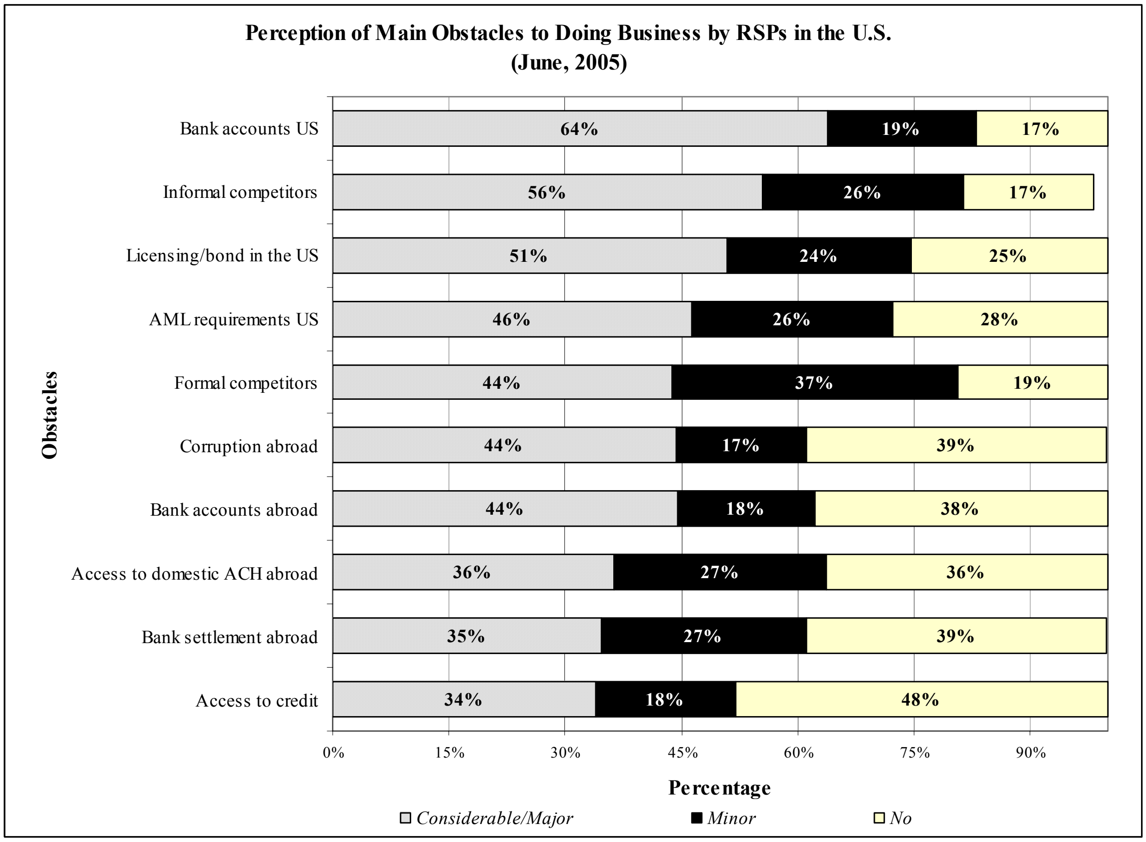
[36] There are at least two elements in the area of consumer protection : 1) deter fraudulent operations or scams and recourse for consumers from insolvency of providers; 2) ensure transparency of transaction fees and exchange rates
[37] IMF. 2005.
[38] In consequence, these concerns were addressed by the FATF while adopting two special recommendations to combat financing of terrorism, which directly involved remittance transfers. See SR VI on Alternative Remittance Systems and SR VII on Wire Transfers.
[39] McCusker, Rob, (2005) Australian Institute of Criminology.

The impact of new regulations, primarily anti-money laundering measures, in the US has supported a shift from informal to formal fund transfers systems. A good example of how regulations have promoted the use of formal transfer mechanisms comes from the US-Guatemala corridor, where before the implementation of new AML/CFT measures senders relied heavily on informal operators. As the scope for these operators was reduced, migrants turned to MTOs[40].

Box 3. Study of Remittance Service Providers in the United States

The World Bank conducted a survey on remittance service providers (RSPs) in selected parts of the U.S. Findings from the survey describe how business environment is perceived by these RSPs. The following figure represents some of the obstacles to doing business listed by the surveyed RSPs. The four largest obstacles are related to their regulatory regime, either directly or indirectly.



Source: World Bank. Andreassen, Ole. "Remittance service providers in the United States."

Developing countries are faced with the challenge of finding the right balance between compliance with international standards on one hand, and domestic developmental goals on the other. Extending access to financial services to the poor and financially excluded is a key goal for developing countries. AML/CFT and other remittance-related regulations must take into account how the legal landscape affects individual ID requirements for opening accounts and plugging migrants and the financially disenfranchised into the formal financial sector, as well as protecting the

[40] The US-Guatemala Remittance Corridor.

consumer (e.g. mandating transparent pricing structures). For market players, regulations impact how financial institutions assess reputation risks when partnering with other remittance businesses, the seriousness of entry barriers to the remittances market, what kind of business partnerships a jurisdiction will allow, who is able to capture/disburse funds, and whether increased regulations significantly affect operating costs for remittance businesses in a way that constricts business growth.

Providing basic financial infrastructure and allowing access to RSPs are important pre-requisites for regulated providers to attract remitters away from informal systems. Access by non-bank RSPs to the payments systems infrastructure, including sharing the benefits of real-time settlements, could facilitate better liquidity management while contributing to lowering the cost of remittances through formal channels.

Box 4. General Principles for International Remittance Systems

Cooperation on payment systems is necessary in order to ensure the safety, efficiency, and transparency of the way payments are processed and of the circuits, which support remittance transactions. The Bank for International Settlements' Committee for Payment and Settlement Systems (CPSS) and the World Bank convened a Task Force, with IMF involvement, to address the needs of international policy coordination for remittance systems. The Task Force includes central banks from sending and receiving countries, international financial institutions, and development banks. The output from this Task Force known as the *General Principles for International Remittance Systems,* issued in May 2006, could be used as a framework for the development and oversight of remittance payment systems in the future and could address market environment, consumer protection and transparency, market infrastructure, and public policy for remittance systems. The general principles are aimed at the public policy objectives of achieving safe and efficient international remittance services. To this end, the markets for the services should be contestable, transparent, accessible and sound.

See Annex A for a description on the principles.

Source: World Bank

Access to banking services for MTOs is essential for their payment settlement in-country and cross border[41]. Traditionally, some informal remittance providers (particularly smaller ones) have had problems with accessing banking services. Some banks may decline such business because they are unwilling to take on extra risks following a due diligence process. If remittance providers are registered/licensed with regulators, this gives assurance to banks that the provider is engaging in legitimate business, and thus opens up to remitters the array of banking services needed to strengthen their activity and may contribute to lowering transaction costs. In main remitting countries, recently there were closures of some MTOs' corresponding bank accounts because of the perception that MTOs are high-risk business entities that require additional monitoring of transactions[42]. For example, some banks interviewed in the U.K. do not conduct business with smaller MTOs that may present ML and FT risks[43].

[41] Access to banking services may make settlement more transparent to the extent that remittance providers settle balances by using their bank accounts and other banking services. This may assure some certainty of payment settlement for the remittance provider to the extent that bank transactions go through the traditional retail payment system and even high value gross real time settlement system. Over time this may reduce costs for remittance flows.

[42] According to Orozco (2006), in 2006 Bank of America decided to cancel all is accounts with MTOs including those with larger international franchises, such as MoneyGram and Western Union.

[43] This is one of the issues driving the development of the U.K. Money Transfer Association of about 500 members, which it explained the development of a similar association in the US.

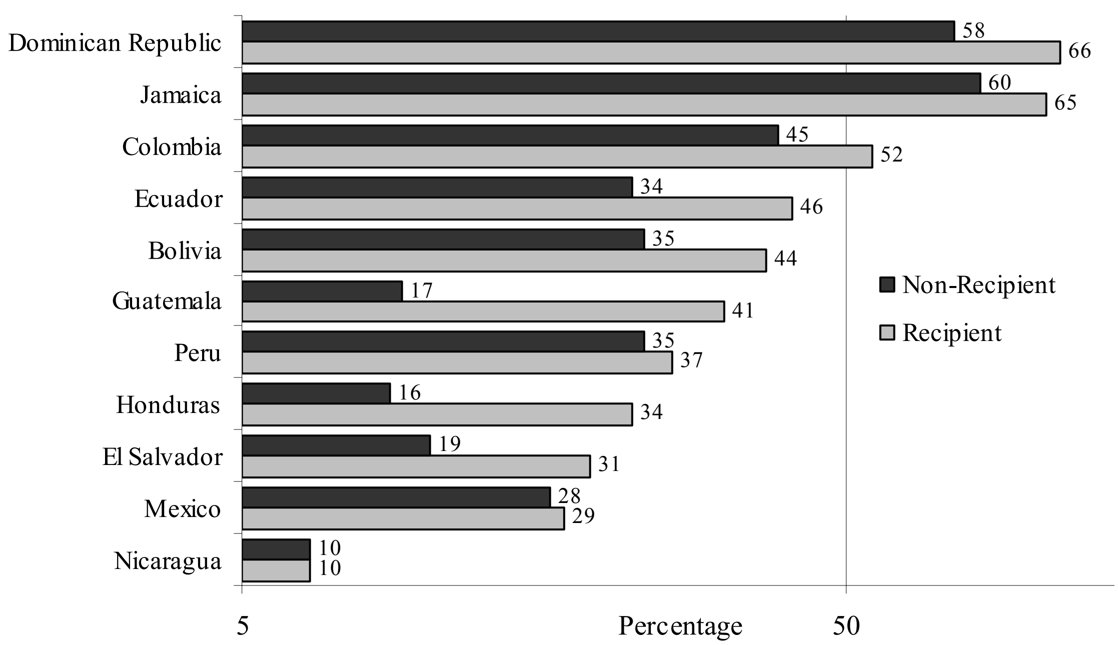
III. Issues Observed in the Receiving Countries

Assessing the development impact of remittances involves examining the remittance market in the receiving country, the institutions that facilitate its development, and how households use remittances. Corridor studies show that providing financial opportunities to the beneficiaries will improve the development potential of remittance flows in the middle and long term. It will also encourage migrants that return to their countries to apply their skills or leverage on savings accumulated overseas[44].

The Use of Remittances

Remittances are personal flows and remitters and recipients decide how to send and spend them.[45] Public policies which encourage households to use remittances productively are difficult to implement and in some cases do not recognize the importance of financial intermediation as a precondition to maximize their development impact. Financial intermediation among remittance recipient households could have greater effects on their quality of life. Savings accounts, credit, insurance and mortgage products have started to emerge in recipient countries as links between remittances and the financial sector. According to the IADB, remittance recipients in Latin American and Caribbean countries are at least ten percentage points above non-recipients in having a bank account[46].

Figure 8. Recipients and Non-recipients with Bank Accounts by Country, Latin America Region (2005)



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[44] The impact of financial opportunities has been observed by Orozco. 2005.
[45] World Bank 2005 (b).
[46] Orozco, 2006, p.5

Source: Data compiled by Manuel Orozco. "International Flows of Remittances: Cost, competition and financial access in Latin America and the Caribbean- toward and industry scorecard". IaDB. 2006.

The bilateral corridor analysis identifies regular support of household expenditures as the primary purpose of remittances. The purchase of basic consumption goods, housing, education and health care have been identified as the main uses of remittances by households in recipient countries. In wealthier households, they may provide capital for small businesses and entrepreneurial activities[47]. Channeling remittances into productive investments could include matching fund programs (such as 3x1 in Mexico), and programs which encourage recipients to save more and spend less (as in Lesotho and Mozambique). Some corridors have a more difficult time implementing these collective remittance schemes. For example, in the UK-Nigeria corridor, the Diaspora HTAs are organized around ethnicity. This makes it difficult to replicate the 3X1 model in Nigeria because the HTA counterparts at home are organized around the traditional authority rather than the local, state or federal government[48].

Besides consumption and community projects, increasingly, senders use remittances to repay debts associated with the migrant's travel. In the US-Guatemala corridor, a portion of the remittance goes to pay the *Coyote*, the person who helps an undocumented migrant cross the US borders, if the migrant has used such means of migration. In the UK-Nigeria corridor, some remittances are returns on loans to family members who financed air travel, initial sustenance income, and school fees in the case of some students. All these arrangements between providers of migration finance or services and the migrants, who later become senders, rely on trust between both parties.

The impact of remittance flows on financial development is not uniform, and depends in part on the initial quality and coverage of financial institutions in the specific country. The World Bank report on the development impact in Latin America and the Caribbean found that remittances have a positive but smaller impact on financial development for the region.[49] According to the authors, the quality and availability of financial institutions could explain the relatively low financial development effects of remittances. These findings are consistent with those from the bilateral corridor analysis in other regions; in most cases remittance recipients feel greater distrust toward financial institutions when there is a history of recurrent financial crises, and will therefore be less likely to rely on them.[50] In addition, the physical access to banking (measured in terms of

[47] IOM's survey in 2004 focused on the link between remittances and micro-enterprises. It is estimated that more than a third of households receiving remittan Same distrust issues have been observed in the corridors Italy-Albania and Germany-Serbia. have their own business (i.e. 300,000).

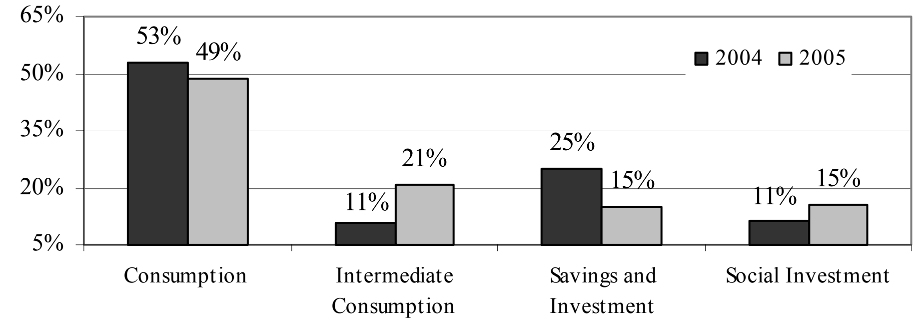
[48] The ethnic subdivisions within the Diaspora community are the basis for HTAs, which organize around the traditional authority, for example the *chief*, *Oba, Eze*, or *Emir* in Nigeria. Usually the traditional authority works in parallel to the institutional levels of government, and social welfare programs are limited to indigenes or subjects of that specific area. For example, if the resident of a town in Nigeria is not originally from that area in terms of ethnicity, the traditional authority or chief would not consider him or her to be a subject and thus there is no obligation to provide for his welfare.

[49] LAC study

[50] Same distrust issues have been observed in the corridors Italy-Albania and Germany-Serbia.

the number of branches per area) is the lowest among all regions;[51] and the costs of maintaining a bank account and the fees associated with loans are relatively high in Latin American countries.[52]

Figure 9. Remittances Uses in Guatemala (2004-2005)



Source: IOM. 2004

Remittance Distribution arrangements limit market development

The type of RSPs, demand, size, volume, and the regulatory framework in the sending and receiving countries shape the remittance marketplace. There are at least two RSPs involved in most of the transactions; one RSP in the sending country (the capturing RSP) and one in the receiving country (the disbursing RSP), who need to agree on a mechanism to work together to provide the overall service. The capturing and disbursing processes involve the transfer of information as well as funds[53].

Banks and Money Transfer Operators (MTOs) are the most active market participants for distribution of remittance funds. Nevertheless, postal services, credit unions, microfinance institutions, exchange houses and other non-bank institutions play an increasingly important role in channeling remittances. In Mexico for instance, remittances are delivered to recipients through a variety of outlets, which also include department stores, small neighborhood shops, and telegraph offices. Though often delivering the same remittance services, market participants respond to market pressures by adopting different strategies.

In several countries, because of regulatory concerns, only banks have authority to provide remittance services. However, the relative small value, of remittance transfers handled by RSPs, are unlikely to be a significant systemic risk[54]. In addition, because banks need

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[51] Beck, T. , A. Demirguc-Kunt and M. S. Martinez Peria. 2005. "Reaching out: Access to and Use of Banking Services Across Countries" World Bank Policy Research Working Paper No. 3754, Washington DC.

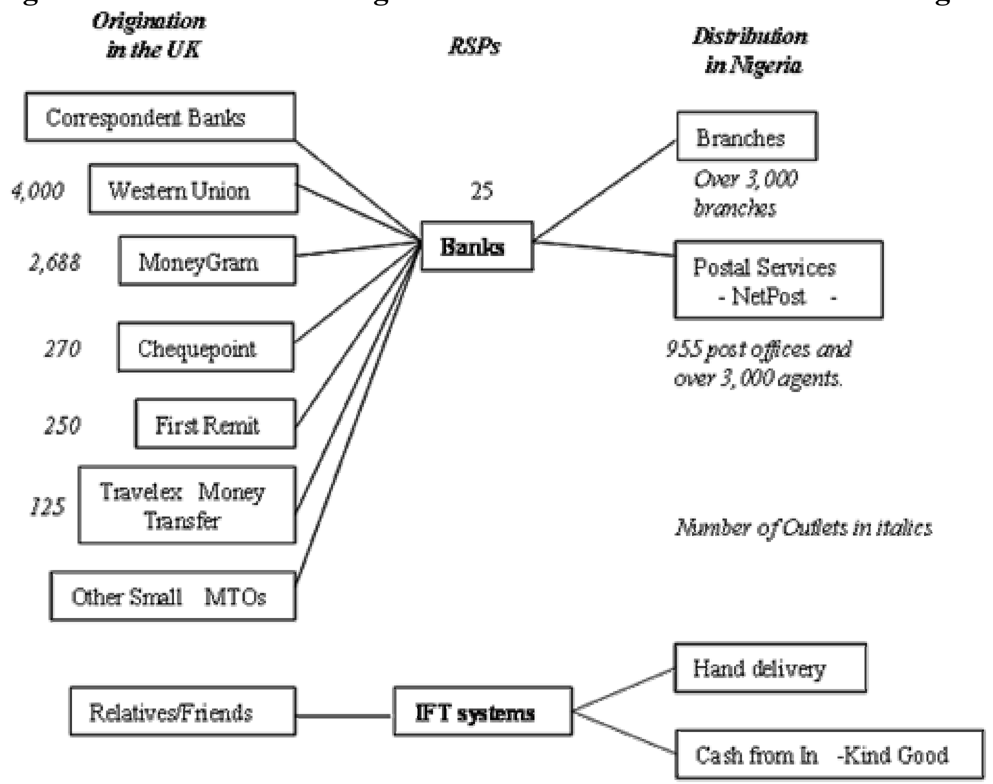
[52] Beck, T. , A. Demirguc-Kunt and M. S. Martinez Peria. 2006. "Banking Services for Everyone? Barriers to Bank Access Around the World", World Bank. Mimeo.

[53] The sender must provide the information to enable the capturing agent to send the funds to the receiver, and the disbursing agent must tell the receiver who the sender is. .

[54] Bank for International Settlements and The World Bank (2006) *General principles for international remittance services. Consultative report*. March 2006. Document prepared by the Committee on Payment

large volumes to make profits from remittance transfers sometimes are able to lobby a monopoly on the distribution of these flows. This practice hurts remittance recipients in countries where the options for formal distribution of remittances are already limited to urban centers.

Figure 10. Channels for Origination in the UK and Distribution in Nigeria



Source: World Bank BRCA Reports

Exclusivity agreements and the failure of banks to view remittances as a profitable venture restrict the growth of distribution networks. Exclusivity agreements limit competition in a corridor, where one dominant market player monopolizes available distribution outlets and locks them into an "exclusive" business relationship. Where recipient-country distribution outlets have broken or moved away from these exclusive relationships, growth and competition have spurred progress toward developing a wider range of remittance distribution networks. For example, recently in Guatemala, financial intermediaries are moving away from the exclusive feature of their partnerships with their US counterparts. Physical outreach is a key success factor for RSPs, and competitors in the US who wish to enter the Guatemalan remittances market need to have a local partner with such a network. If most intermediaries lock into an exclusivity agreement, this becomes a major entry barrier. This trend has enabled increased competition in the corridor and allowed a greater leveraging of the Guatemalan banks' vast presence in both urban and rural areas.

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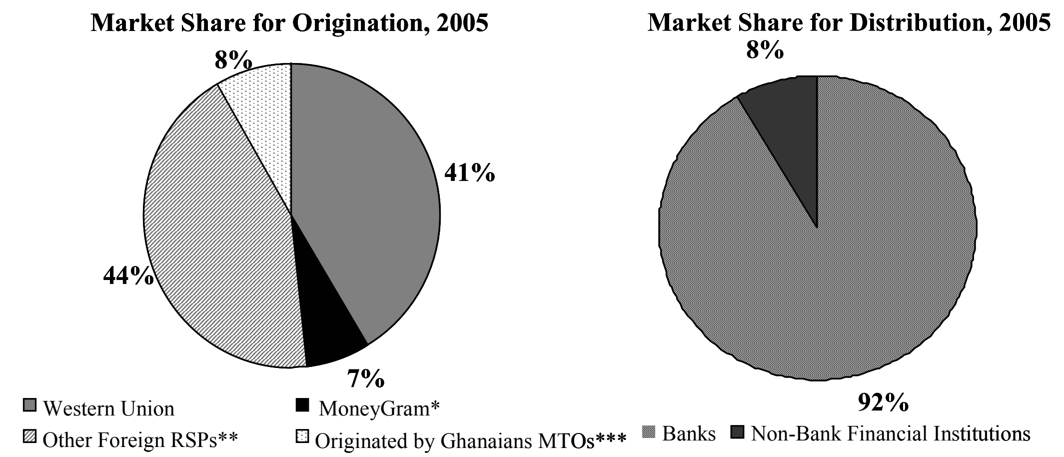
and Settlement Systems. http://siteresources.worldbank.org/FINANCIALSECTOR/Resources/060313CPSSWBfinal.pdf

Figure 11. Market Share for Origination and Distribution in Ghana, 2005



* Flows reported by SG-SSB
** Includes MTOs and banks in sending remittance countries different from Western Union and MoneyGram
*** Refer to remittance flows originated by non-bank financial institutions

Source: BOG, 2005

Banks, even in large remittance corridors and relatively developed financial sectors, have been slow to recognize the potential profitability of providing remittance and other financial services to migrant workers and their beneficiaries. However, there is evidence of their growing involvement in several corridors. The cross selling of financial products to remittance recipients is a real possibility that has encouraged innovation and can attract a growing number of banks and financial institutions into the remittances industry. In some countries such as Mexico, there are higher bank penetration rates among remittance beneficiaries versus the average population. Other innovative programs include remittance-based mortgage products, home-improvement loans, and consumer lending and automobile purchases. Banks that have successfully maintained a presence in the remittances industry, utilize their competitive advantage in offering flexible transfer arrangements such as cash-to-cash, cash-to-account, account-to-account and account-to-cash remittance products.

Proximity, convenience, and user-friendly service are important features for the success of the remittance distribution industry. In Guatemala, remittance distribution is achieved through a combination of banks, non-bank financial institutions, and non-financial partners. Since remittance recipients are mostly segments of Guatemala's rural and unbanked population, remittance distribution networks must be extensive and accessible. A variety of channels such as local banks[55] –whose market share has been

[55]The Guatemalan financial sector includes –among other types of intermediaries- 25 commercial banks, approximately 13 offshore banks, seven-licensed money exchangers although hundreds exist informally, five wire remitters, and around 150 active Savings and Credit Cooperatives, which are non-regulated institutions similar to Credit Unions.

growing with increasing usage of EFTs and reduced activity of *cambistas*-, dedicated franchises/agents of MTOs, exchange bureaus, retail stores, and more recently microfinance institutions make up this network (See Annex E.3)

Using Remittances to Bank the Unbanked

Profit-driven RSPs[56]in many corridors lack the information necessary to adequately size the market, i.e. determining the dollar amount of value that can be generated in the market. Informal remittance flows are not always captured by central banks and reflected in official balance of payments statistics. Also quantifying the customer base for remittance services has its natural challenges. Remittance products appeal to, among others, unbanked, undocumented immigrants and it is difficult to collect reliable demographic data on such customers. Such data would help potential service providers make their investment and marketing decisions. On-going efforts, by national and international institutions, aims to improve the recording and reporting of remittance data:

Partnerships between microfinance institutions and RSPs, mostly through banks, could offer more coverage and access to low income people. Increasing financial access involves more than assessing the existing banking system; it must explore potential partnerships between microfinance and remittances institutions, since they are likely to serve the same clients.[57] In countries, where the remittance market is mature, the paved road for remittances tends to stop in large cities and urban areas with a high population density and established banking presence. Linking these urban centers with microfinance institutions that serve the rural population is an important step for extending formal remittance distribution networks to rural areas.

The issue of low level of access to financial services is not specific to remittances recipients; low intermediation and inappropriate financial markets are noticeable in some developing countries. For example, Guatemala compares poorly with other countries in Central America regarding financial depth, having the lowest percentage of bank credit to the private sector in the region. Access to credit, especially for lower income individuals is limited and most recipients view banks as remittance distribution points only[58]. While there are indications of pockets of initiatives to target unbanked communities, and/or remittance beneficiaries, banks do not generally have a strategic objective to cross-sell financial products to remittances recipients.

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[56] Any person or institution providing such a service as a business is called a remittance service provider.
[57] World Bank 2005 (a) (b).
[58] Of the remittance recipients surveyed by IOM (2004), only 10 percent of households have requested loans to improve their houses and start businesses; the remaining 90 percent did not request loans because they lacked collateral and were afraid that the loan would be denied. The IOM survey also shows that only 3.9 percent of heads of family have a debit card and 2.2 percent a credit card.

IV. Conclusions

This section presents some considerations for authorities and policy makers in sending and receiving countries for promoting the development of appropriate regulatory and supervisory controls that promote transparency increase integrity of remittance flows while improving access to financial services.

Initial lessons from the BRCA suggest the need for policies involving both sender and recipient countries on using remittance transfers as an entry for broader access to the formal financial sector. Maximizing the development impact of remittance flows in recipient economies goes beyond the discussion of reducing the transfer cost and strengthening payment systems. Remittances are an entry point for a broader analysis on how to bring financial services to the *unbanked.* Given the link to migration, it also opens the door to discuss the financial dimension of immigrants in sending countries, and their links with beneficiaries in receiving countries.

The following conclusions have been organized into three sub-sections

- Bank's Lessons on Bilateral Remittance Corridor Analysis
- There is Need for Policies Involving Both Sender and Recipient Countries.
- The Challenge of Converting Remittance Transfers into an Entry for a Broader Access to Finance.

Bank's Lessons on Bilateral Remittance Corridor Analysis

Although the specific dimensions and priorities for action differ from one bilateral remittance corridor to another, recent case studies of a number of corridors have indicated the need for information for all remittance stakeholders.[59]. The first common area of need is to improve data and recording of basic information on remittance flows such as remittance options and the cost to customers, and the current and potential size of the remittance market for regulators and policymakers. Such information is necessary to make informed decisions that balance regulations with policies that encourage the growth of the formal remittances industry. Making information accessible to market participants and individual remitters is also crucial to establish a competitive marketplace for formal remittances.

Case studies show that falling costs and improving services are tied to the proliferation of such information in the market. Governments on both sides of the remittance corridor, as well as migrant worker and community groups, are also finding it useful to provide instruction that increases the financial literacy of remitters. Thus, the remittance consumers are able to discern between better RSPs, prompting RSPs to improve services and decrease prices in a competitive environment.

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[59] The Bank had conducted, in partnership with donors and clients, Bilateral Remittance Corridor Analysis (BRCA) cases studies covering the remittance corridors between The US-Mexico, Canada-Vietnam, The Netherlands-Surinam, Germany-Serbia, Italy-Albania, The U.S.-Guatemala, The U.K.-Nigeria, Qatar-Nepal, and The U.K./U.S.-Uganda.,

The effects of regulations on money remitters require further research and discussion between relevant authorities in both sending and receiving countries. A number of countries treat money remitters like banks and require them to obtain a banking license with relatively high capital requirements, thereby making it very difficult for small providers to operate legally under this environment. This approach limits access to formal transfers for the beneficiaries and maintains a status quo market composed of a few dominant operators in both sending and recipient countries. Other countries have simply prohibited the operations of money remitters who are not registered or licensed.

Capital adequacy and liquidity rules are sometimes disproportionate for RSPs that do not take deposits. Keeping banks as the only authorized RSPs in sending countries not only limits competition but also reduces the effectiveness of promoting formal transfer mechanisms and consequently the potential multiplier effect if transferred by formal financial institutions.

Multi-national efforts are specially needed to develop payment systems infrastructure between sending and receiving countries. As it is recognized by The General Principles for International Remittance Services, national regulations should aim to create a level playing field between equivalent remittance services *(General Principle 3)*. Developing and improving infrastructure networks demand international cooperation and agreement on the basic payment systems building blocks. Such common standards, on software, equipment and instruments (payment cards) are essential to connect payment systems in a seamless and cost-effective manner, leading to reduction in costs and better services.

Given the different characteristics of both remittance sender and recipient countries, problems that may be impeding improvements in the efficiency and integrity of remittance flows may vary significantly from one bilateral channel to another, even where the sending or receiving the country is the same (e.g., U.S. – Mexico, U.S. – Philippines, Canada - Mexico). In order to deal effectively with these issues, the relevant authorities of a number of countries linked by remittance flows are engaging in systematic bilateral dialogues between authorities in both sending and recipient remittance countries that involve the main stakeholders in the remittance market with a view to enhance the efficiency and protect the integrity of remittance markets.

There Is Need for Policies Involving Both Sender and Recipient Countries.

Policymakers in the sending countries need to understand the main incentives that shape senders' choices among the various alternatives for transfer mechanisms. Senders are generally concerned about the cost, speed and reliability of transfers, and authorities in the sender countries should understand how their policies and the existing legal and regulatory frameworks impact on the costs, technological choices, and level of competition among remittance service providers. Sender choices are also shaped, *inter alia*, by cultural background, past experiences with financial institutions, legal status in the host country, level of financial sophistication, and by economic policies and the quality of remittance delivery infrastructure in their respective home countries. These factors may vary significantly among migrant groups within the same sender country.

The Challenge of Converting Remittance Transfers into an Entry for a Broader Access to Finance.

One factor that can significantly increase the developmental impact of remittances is the role they can play in introducing both senders and recipients to other financial services, such as savings accounts, insurance, small business and housing credit. In addition to enhancing the income-earning and risk management capacities of the immediate remittance customers, channeling their savings through the formal financial system can greatly improve the efficiency of their application. There is encouraging evidence in a number of remittance corridors that banks and other financial intermediaries are becoming increasingly interested in using the provision of remittance services as a vehicle for cross-selling other services and broadening their business and customer base. Progress in this regard is limited in some corridors by the irregular legal status of migrant workers in the sending country. At the same time, a common problem in many recipient countries that can limit development impact is the weakness of local financial institutions and infrastructure, including payments systems, particularly in rural areas.

Also important in this regard is a regulatory framework that provides transparency of remittance costs, consumer protection against fraud, and the avoidance of excessive or discriminatory regulations among different types of service providers that unduly increases costs, discourages market entry, or distorts the competitive playing field. In remittance corridors where flows and competition among multiple types of RSPs have been increasing, there is evidence of declining transfer fees and the development of new remittance products to meet the particular demands of specific migrant groups.

Competition between RSPs alone will not be effective in lowering transactions costs in corridors characterized by a small volume, where banks and businesses are hesitant to invest in, along with a lack of technological innovation. If remittance systems remain opaque, authorities can take an active role in disseminating information on the comparative prices of RSPs, and providing financial education to migrants and ultimately creating more transparent services.

Authorities should engage in a private sector consultation before imposing a regulatory regime: establish clear and simple application procedures for registration or licensing and minimum background checks for owners and managers of RSPs, request programs against ML/FT in place by RSPs, conduct onsite and offsite monitoring compliance programs and have the ability to impose sanctions. Providers should also be required to comply with specific AML/CFT requirements, consisting of minimum customer identification, tailored record keeping and reporting of suspicious activity.

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Annex A

Improving Data Recording of Remittance Flows

Remittance flows are recorded in the balance of payments; exactly how to record them is being reviewed by an international technical group which is guided by the UN Technical Subgroup. Work in this area is aimed to improve data collection on estimating flows in countries which currently do not report data on remittances or capture the volume of remittances transferred through IFT systems. In consultation with an even wider cross-section of statistical compilers, this group developed recommendations on improved concepts and definitions.[60] These recommendations will be reflected in revised versions of the IMF Balance of Payments Manual, fifth edition and the 1993 System of National Accounts.

Box A.1. New Definitions for the recording of remittances in the Balance of Payment

Since 2004, the statistical community agreed on several steps to improve concepts and compilations practices on data collection on remittances. A working group was formed jointly by the Eurostat and the IMF Statistics Department to improve compilation guidance based on conceptual improvements, which were development by the UN Technical Subgroup on the Movement of Natural Persons (TSG) and other stakeholders and approved by the INF Committee on Balance of Payments Statistics. In January 2005, there was agreement that the balance of payments statistics are the appropriate framework for collecting, reporting and improving official statistics on remittances[61]. New concepts and definitions proposed by the UN TSG were adopted and now include the following:

- *"Workers remittances"* item in the balance of payment will be replace with a new component "personal transfers", comprising all current transfer in cash or in kind made or received by resident households to or from other nonresident households.
- A new aggregate, *"personal remittances"* should be reported in the balance of payments presenting as a memorandum item comprised of current transfers in cash or in kind, made or received, by resident households to or from nonresident households, and "net" compensation of employees earned but persons working in economies where there are not resident (this concept refers to "compensation of employees"). *"Migrants transfers"* will be remove from the capital account of the balance of payments.
- A new aggregate of "total remittances" should be introduce in the balance of payments as a memorandum item comprised of "net" compensation of employees and current transfers in cash or in kind payable by resident sectors to non-resident sectors to non-resident households and nonprofit institutions serving households (NPISH), and receivable by resident households and NPISH from any nonresident sector.

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[60] Papers of this group are available at its website http://unstats.un.org/unsd/tradeserv/reldocs.asp.

[61] .In January 2005, a meeting to discuss the measurement of remittances was held in Washington D.C. in response to requests from users for improvements in these data, including G-8 Heads of State meeting at Sea Island in June 2004. For additional information, please visit: *http://www.imf.org/external/np/sta/bop/pdf/ao.pdf.*

Annex B

The CPSS/World Bank Task Force for General Principles on International Remittance Systems

The leading forum for international cooperation and policy development in the area of payment systems is the Bank for International Settlements' Committee for Payment and Settlement Systems (CPSS). At the same time, over the last 10 years the World Bank has accrued considerable experience in formulating such policy and supporting the reform of payment systems in more than 65 countries worldwide.

At the end of 2004, the World Bank and the CPSS convened a Task Force to address the needs of international policy coordination for remittance systems*. The task force has issued the consultative version of *General Principles for International Remittance Systems*, with a final version expected in the second half of 2006. The main objective of the *General Principles* is to contribute towards the formation of a competitive and sound remittances market through which remittance services can be offered in an efficient and safe manner, and at the lowest possible cost.

The *General Principles* are expected to become the fundamental framework and key point of reference for authorities, other stakeholders and other international organizations. In particular, public authorities should evaluate what action to take to achieve the public policy objective through implementation of the *General Principles*, while remittance service providers should participate actively in the implementation of these *principles*.

The five *General principles* that the Task Force has detailed are:

1. Transparency and consumer protection. The market for remittances should be transparent and have adequate consumer protection.

2. Payment system infrastructure. Improvements to payment system infrastructure that have the potential to increase the efficiency of remittance services should be encouraged.

3. Legal and regulatory environment. Remittance services should be supported by a sound, predictable, non-discriminatory and proportionate legal and regulatory framework in relevant jurisdictions.

4. Market structure and competition. Competitive market conditions, including appropriate access to domestic payments infrastructure, should be fostered in the remittance industry.

5. Governance and risk management. Remittance services should be supported by appropriate governance and risk management practices.

* The WB co-chairs this Task Force together with the CPSS. Other Task Force members include the IMF, AMF, IADB, ADB, central banks of Germany, Italy, Mexico, Philippines, Sri Lanka, Turkey, Brazil, Hong Kong Monetary Authority, European Central Bank, Federal Reserve Bank of New York, and the Board of Governors of the Federal Reserve System.

Annex C

The Requirements of the FATF 40 plus 9 Recommendations for Alternative Remittance Systems (ARS)

After the events of September 11, 2001 in the Unites States, the FATF issued eight special recommendations (SR) to combat the financing of terrorism.[62] The FATF has drafted SR VI specifically to regulate (alternative) remittance systems: "*[e]ach country should take measures to ensure that persons or legal entities, including agents, that provide a service for the transmission of money or value, including transmission through an informal money or value transfer system or network, should be licensed or registered and subject to all the FATF Recommendations that apply to banks and non-bank financial institutions. Each country should ensure that persons or legal entities that carry out this service illegally are subject to administrative, civil or criminal sanctions*."

SR VII, and SR IX also cover aspects of (alternative) remittance systems as well as applying more broadly to other areas.

SR VI and the related Interpretative Note to SR VI essentially have three core elements:

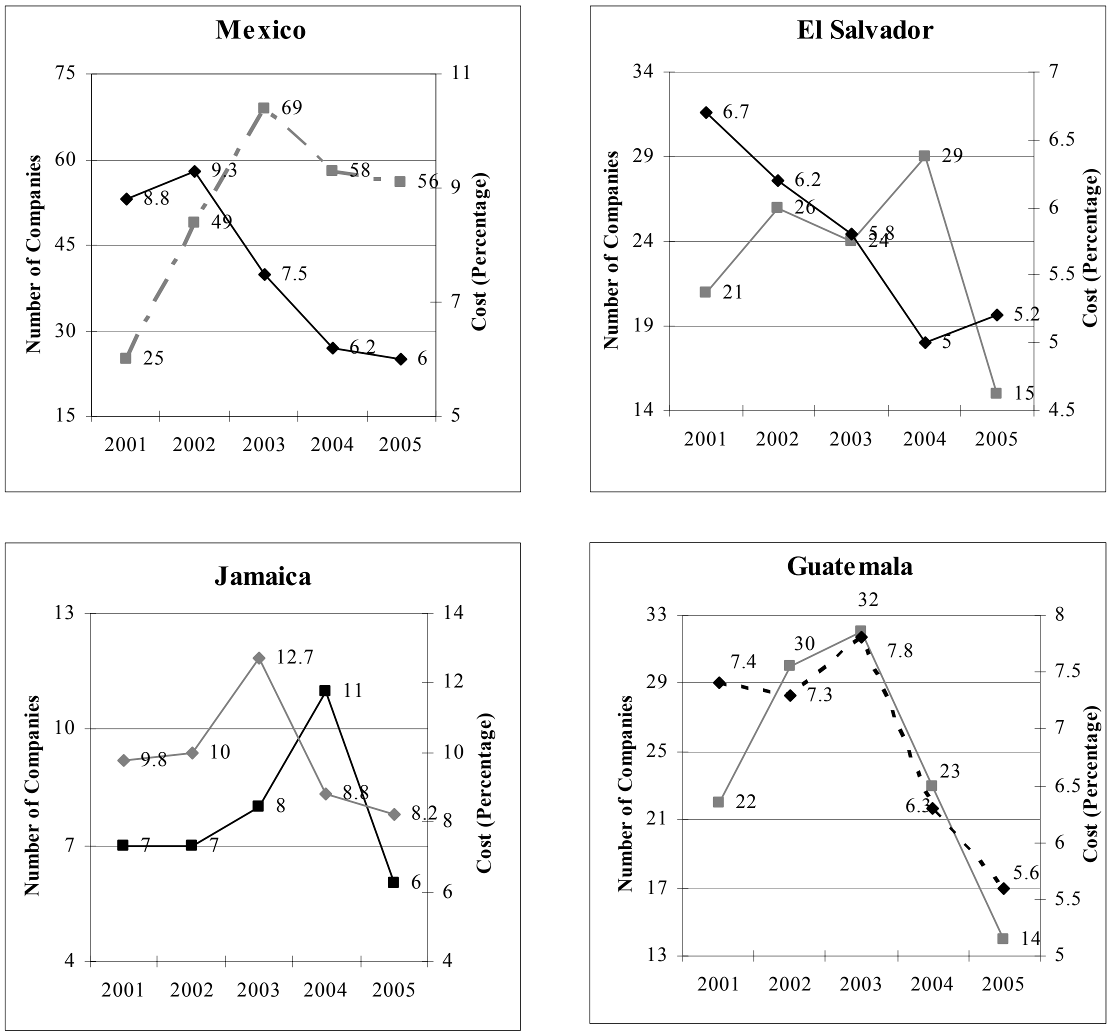
1. Jurisdictions should require licensing or registration of persons (natural or legal) that provide money or value transfer services, including through informal systems;
2. Jurisdictions should ensure that money or value transmission services, including informal systems, are subject to applicable FATF Forty Recommendations (2003) (in particular, Recommendations 4-16 and 21-25) and the Nine Special Recommendations (in particular SR VII); and
3. Jurisdictions should be able to impose sanctions on money or value transfer services, including informal systems, that operate without a license or registration and that fail to comply with relevant FATF Recommendations.[63]

This effectively means that customer due diligence (CDD), record keeping, suspicious transactions reporting (STR) and internal policies and controls requirements should apply to all operators in the formal and informal funds remittance area. Furthermore, countries must be able to devote enough resources to monitor and supervise such operators.

[62] See www.fatf-gafi-org, in October 2004 a ninth recommendation on cash couriers was adopted.
[63] FATF Interpretative Note to SR VI, paragraph #2.

Annex D

Cost of sending US$200 from the U.S. to and Number of Companies Operating Mexico, El Salvador, Jamaica and Gautemala (2001-2005)



Source: Data compiled by Manuel Orozco. IaDB. 2006

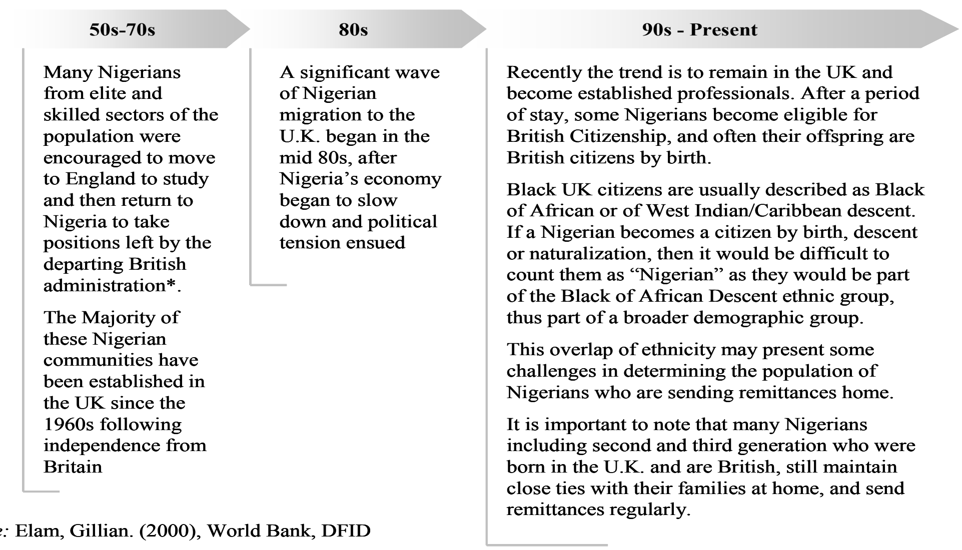
Annex E / Excerpts from BRCA Case Studies

1. The evolution of each remittance corridor is unique.

The evolution of each remittance corridor is unique, reflecting different historical factors and levels of institutional development at a bilateral level. Each corridor is shaped by the incentives which influence remittance senders' decisions regarding how to transfer remittances

<u>The U.K. – Nigeria Remittance Corridor</u>

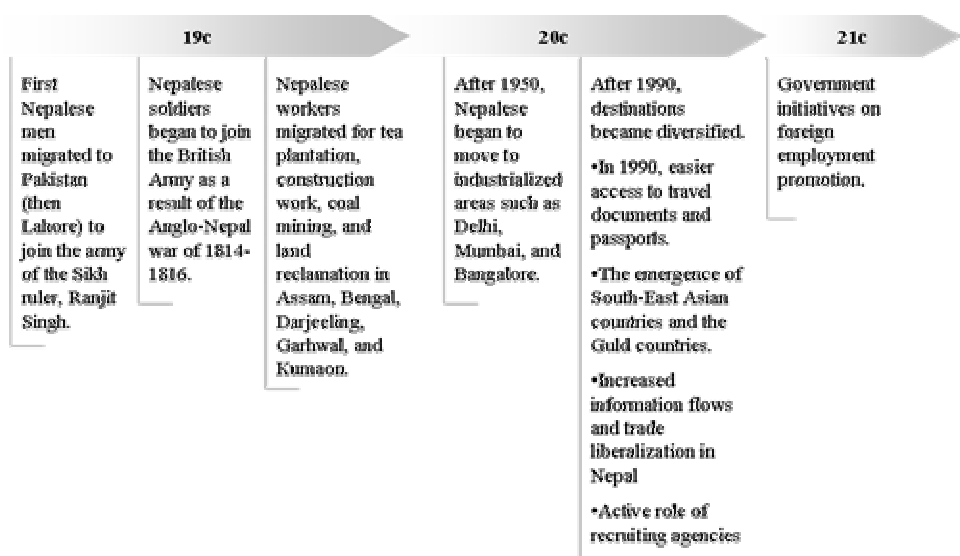
Figure E.1. Nigerian Migration History



Source: Elam, Gillian. (2000), World Bank, DFID

<u>The Qatar - Nepal Remittance Corridor</u>

Figure E. 2. Nepalese Migration History



Source: Thieme and Wyss (2005)

2. In some countries, consumer loans, mortgages or other kinds of retail banking activities are viewed as more profitable than remittances

<u>The Italy –Albania Remittance Corridor</u>

Table E. 1. Banks in Italy Promoting Remittances and Financial Services for Migrant Workers (2006)	
Banca Popolare di Puglia e Basilicata	It is offering services to migrants since the 1980s, and to Albanians since the 1990s. Services specifically tailored to Albanians' needs are "Risparmio amico" ("Friendly saving"), and "Deposito Amico" ("Friendly Deposit"). Albanian customers are given a check book and the fees are 50 percent, with no operation fees and a maintenance fee of 10 euros per year. For sending remittances, there is a 3 euros commission fee, and a 3euros fee for using SWIFT.
Banca San Paolo IMI	It is present in Albania through the acquisition of an Albanian bank. It operates 5 branches *(multi-ethnic points)* devoted to attend migrants in Rome, Turin, Padua, Naples and Pescara. Its product on remittance transfers is called *"get money to your family"*, which is based on a settlement agreement with correspondent banks. This service is not profitable for the bank and it is aimed to attract migrants for cross-selling financial products.
Banca Popolare Pugliese	It is present in Albania trough the acquisition of an Albanian bank. On remittances, it offers a 0,1% commission fee with a minimum transfer of 5 euros. Banca Popolare Pugliese is creating an helpdesk for Albanian citizens and other products/services such as opening of account without resident permission. The Bank is shareholder of the Albania-based *Banca Italiana di Sviluppo*, the first fully owned Italian bank in Albania. It offers products such as investment plans in activities of remittances and training courses for potential Albanian business men.
Banca Popolare de Milano (BPM)	This cooperative bank is the 12th banking group in Italy. With 727 branches, BPM has strong local branches network. The bank offers a variety of services specifically tailored to migrants. In particular, "Conto Extra" gives the migrant the possibility of having his salary accredited directly on his account, automatically paying bills, sending money home with low fees and an international pre-paid card. Moreover, the bank provides immigrants with an additional service "Polizza Extra", a toll-free number which help them with trip planning, school choosing and urgent messages to their families. Small loans are also granted to the account holders.
Unicredit	Unicredit is a retail bank with 2,500 branches. It is planning to launch new migrant banking products in the coming months. Bank's strategy does not include remittances as an entry point for cross-selling of financial products given the low revenue and the need of having a large number of entry points.
Banca Popolare Emilia Romagna	It offers remittance services to Albanian migrants in Milan and Bologna. One of the products is "Conto World". Fees for remittances are flat at 7 euros.
Cassa di Risparmio di Genova (Carige)	It was the first bank to open a dedicated teller service to migrants more than 10 years ago in Genoa. It focuses particularly on assistance to access banking services and mortgages for real estate.
Cassa di Risparmio	The project "Risorsa Immigrazione" –Immigration Resource- has been created in

di Treviglio e Geradadda	1995 as a low-fee bank account specific directed to immigrants. In 2001, it was upgraded to encompass a whole packet of services, which includes loans, insurance and remittances services. In 2004, 9 credit banks operating in the Bergamo area have jointly signed an agreement with the association "Casa Amica" to establish a solidarity fund which may be used to cover eventual insolvencies occurred to immigrants.
Banco Ambrosiano Veneto (belonging to the Banca Intesa Group)	"Conto People" by Banca Intesa is a no-cost maintenance account, which allows the account holder having two credit cards: one is for the immigrant living and working in Italy; the second one can be sent back home to families to withdraw money from the same account held and filled up by the immigrant in Italy
Banca Popolare Friuladria (belonging to the Intesa Group)	This bank offers "Sistema Welcome", which includes long-term saving programs and insurances. Information on housing, job market, social security, education is available on the bank web site. Moreover, an agreement with local associations has been signed, within the framework of "Casa Welcome", to help migrants in housing matters.
Banche di credito cooperativo dell'Emilia Romagna	The program "Radici" is directed to immigrants holding legal permit of residence. The bank has also a joint project with the University of Bologna to train 250 bank employees in migration related issues.
Banca Sella	At the time the money is sent, the sender pays a commission that starts from 7.75 euros for each transfer and varies from country to country. In some cases, the beneficiary will pay a small commission but the sender has the option to pay it entirely or not.
Monte dei Paschi di Siena	The Monte dei Paschi di Siena offers the product "Paschi senza Frontiere" ("Paschi without borders") to customers with a non-EU citizenship, officially resident in Italy. It provides privileged conditions to a number of services, particularly related to transfer of funds towards the home country, such as the opening of a mortgage at special conditions (called "Mortgage without borders"), to transfer money at a low price with the possibility to send it as a cumulative transfer of funds of migrants.

Source: World Banks interviews with Italian banks

3. Proximity, convenience, and user-friendly service are important features for the success of the remittance distribution industry.

A tentative SWOT analysis of each type of distribution channel in Guatemala is presented in table below:

Remittance Distribution Market Players in Guatemala

Strengths, Weaknesses, Opportunities and Threats

Market Player	Strengths	Weaknesses	Opportunities	Threats
MTO agents	• Ample distribution points, especially where no alternatives • Consumer loyalty to MTO brand • Information systems Instant delivery	• Mono-product (no Financial Services to cross-sell)		• Cost Trend
Local Banks	• Relatively significant branch network • Broad range of financial services • Ample liquidity	• Low focus on lower income and rural households or mypimes • High operational costs • Often limited rural presence • Limited usage of "plastic payments"	• Entry point for *bancarizacion* and cross-Sale of financial products • Alliance with US banks which enter the remittances in the First Mile	• Real ID could stall growth of bank-to-bank transfers
Local Stores	• Relationship with community • Geographical location	• Limited expertise • Liquidity constraints	• Cross-Selling of consumer products	
OPDFs	• Relationship with community • Geographical location	• Restrictions on Savings products • Lack of access to Payment Systems	• Cross-Selling of microcredit	• Regulatory void on their capacity to distribute remittances
CACs	• Relationship with community • membership orientation • Geographical location • Broad financial services	• Lack of access to Payment Systems • Unregulated entities	• Entry point for *bancarizacion* and cross sale of financial products	• More AML/CFT requirements than banks on remittances • Regulatory void on their capacity to distribute remittances
Cash Couriers (*Viajeros*)	• Convenience • Trust • Low Cost	• Time of Delivery • Security Risk	• If formal channels become too stringent in accessibility to undocumented migrants	• Regulations • Border controls

Source: World Bank staff based on interviews