Making the Most of Family Remittances

Second Report of the Inter-American Dialogue Task Force on Remittances

May 2007

Inter-American Dialogue

The Inter-American Dialogue is the leading U.S. center for policy analysis, exchange, and communication on issues in Western Hemisphere affairs. The Dialogue brings together public and private leaders from across the Americas to address hemispheric problems and opportunities. Together they seek to build cooperation among Western Hemisphere nations and advance a regional agenda of democratic governance, social equity, and economic growth.

The Dialogue's select membership of 100 distinguished citizens from throughout the Americas includes political, business, academic, media, and other nongovernmental leaders. Twelve Dialogue members served as presidents of their countries and more than two dozen have served at the cabinet level.

Dialogue activities are directed to generating new policy ideas and practical proposals for action, and getting these ideas and proposals to government and private decision makers. The Dialogue also offers diverse Latin American and Caribbean voices access to U.S. policy debates and discussions. Based in Washington, the Dialogue conducts its work throughout the hemisphere. A majority of our Board of Directors are from Latin American and Caribbean nations, as are more than half of the Dialogue's members and participants in our other leadership networks and task forces.

Since 1982—through successive Republican and Democratic administrations and many changes of leadership elsewhere in the hemisphere—the Dialogue has helped shape the agenda of issues and choices in inter-American relations.

Making the Most of Family Remittances

May 2007

Second Report of the Inter-American Dialogue Task Force on Remittances

CONTENTS

MEMBERS OF THE TASK FORCE

Ernesto Armenteros, Chief Executive Officer, Grupo Quisqueyana

José Francisco Avila, President, New Horizon Investment Club

Daniel Ayala, Senior Vice President, Global Remittance Services, Wells Fargo

Carl Braun, Chairman and CEO, Unibank

María Eugenia Brizuela, President, Banco Salvadoreño; former Minister of Foreign Affairs, El Salvador

Teresa de Velilla, Vice President, El Comercio Financiera

Ernesto Fernández Hollman, Chief Executive Officer and President of the Board of Directors, Grupo Financiero Uno

Michael Frias, New Alliance Task Force National Coordinator, Federal Deposit Insurance Corporation

Javier Gavito, General Director, BANSEFI

David Grace, Financial Services and Regulatory Manager, World Council of Credit Unions, Inc.

Moises Jaimes, President, Bancomer Transfer Services

Earl Jarrett, Executive Director, Jamaica National Building Society

Efraín Jiménez, Executive Projects Director, Federación de Clubes Zacatecanos

Irene Lee, Senior Associate, Annie E. Casey Foundation

Doris Meissner, Senior Fellow, Migration Policy Institute; former Commissioner, U.S. Immigration and Naturalization Service

David Myhre, Program Officer, Development Finance and Economic Security, Ford Foundation Office for Mexico and Central America

Linda Singer, Executive Director, Appleseed Foundation

Elisabeth Rhyne, Senior Vice President, Research, Development, and Policy, ACCION International

Gert Rosenthal, Minister of Foreign Affairs, Guatemala

Donald Terry, Manager, Multilateral Investment Fund, Inter-American Development Bank

Task Force Coordinator

Manuel Orozco, Senior Associate, Inter-American Dialogue

MEMBERS OF THE TASK FORCE

Ernesto Armenteros, Chief Executive Officer, Grupo Quisqueyana

José Francisco Avila, President, New Horizon Investment Club

Daniel Ayala, Senior Vice President, Global Remittance Services, Wells Fargo

Carl Braun, Chairman and CEO, Unibank

María Eugenia Brizuela, President, Banco Salvadoreño; former Minister of Foreign Affairs, El Salvador

Teresa de Velilla, Vice President, El Comercio Financiera

Ernesto Fernández Hollman, Chief Executive Officer and President of the Board of Directors, Grupo Financiero Uno

Michael Frias, New Alliance Task Force National Coordinator, Federal Deposit Insurance Corporation

Javier Gavito, General Director, BANSEFI

David Grace, Financial Services and Regulatory Manager, World Council of Credit Unions, Inc.

Moises Jaimes, President, Bancomer Transfer Services

Earl Jarrett, Executive Director, Jamaica National Building Society

Efraín Jiménez, Executive Projects Director, Federación de Clubes Zacatecanos

Irene Lee, Senior Associate, Annie E. Casey Foundation

Doris Meissner, Senior Fellow, Migration Policy Institute; former Commissioner, U.S. Immigration and Naturalization Service

David Myhre, Program Officer, Development Finance and Economic Security, Ford Foundation Office for Mexico and Central America

Linda Singer, Executive Director, Appleseed Foundation

Elisabeth Rhyne, Senior Vice President, Research, Development, and Policy, ACCION International

Gert Rosenthal, Minister of Foreign Affairs, Guatemala

Donald Terry, Manager, Multilateral Investment Fund, Inter-American Development Bank

Task Force Coordinator

Manuel Orozco, Senior Associate, Inter-American Dialogue

PREFACE

At more than $50 billion a year, family remittances are central to economic growth, national expenditures, and balance of payments for many countries in Latin America and the Caribbean. Remittances now exceed portfolio investment, foreign aid, and government or private borrowing, and they have proven to be remarkably stable, often increasing when economies falter. Perhaps most importantly, remittances are reducing poverty and inequality in the region, with most transfers going to low-income families.

Subsequent to the publication of the 2004 report of the Inter-American Dialogue's Task Force on Remittances, *All in the Family*, the task force convened twice more to review developments in the field and explore a few mechanisms that would allow families to get more out of remittance transfers. Although the cost of sending remittances has decreased sharply over the last several years, further reductions can and should be achieved. Another challenge is to turn remittance senders and recipients into bank customers. Without changing the private and voluntary nature of remittance transfers, governments can create productive opportunities for their use. Finally, understanding the macroeconomic effects of remittances is essential in developing appropriate incentives to increase their contribution to national development.

The task force includes prominent political and business leaders; financial, technical, and legal experts; and representatives of sending and recipient communities. We deliberately set out to assemble a diverse group, but—more than anything else—we wanted participants who were knowledgeable about key aspects of migration and remittances, and who could speak with authority on these issues. We sought to craft recommendations for government and private efforts to bolster the value of remittances—for families, communities, and nations.

This report reflects the consensus of the task force members. Not every signer agrees fully with every phrase in the text, but each endorses the report's overall content and tone, and supports its principal recommendations. Signers subscribe to the report as individuals; institutional affiliations are noted here for purposes of identification only.

We want to acknowledge the critical contributions to this exercise of the task force coordinator, Manuel Orozco, including his extensive and highly regarded original research on remittances. The members of the task force played an invaluable role in shaping this report, bringing their considerable breadth of experience and knowledge to our deliberations. We are appreciative of the financial and intellectual support the Inter-American Development Bank and the Annie E. Casey Foundation provided to this initiative.

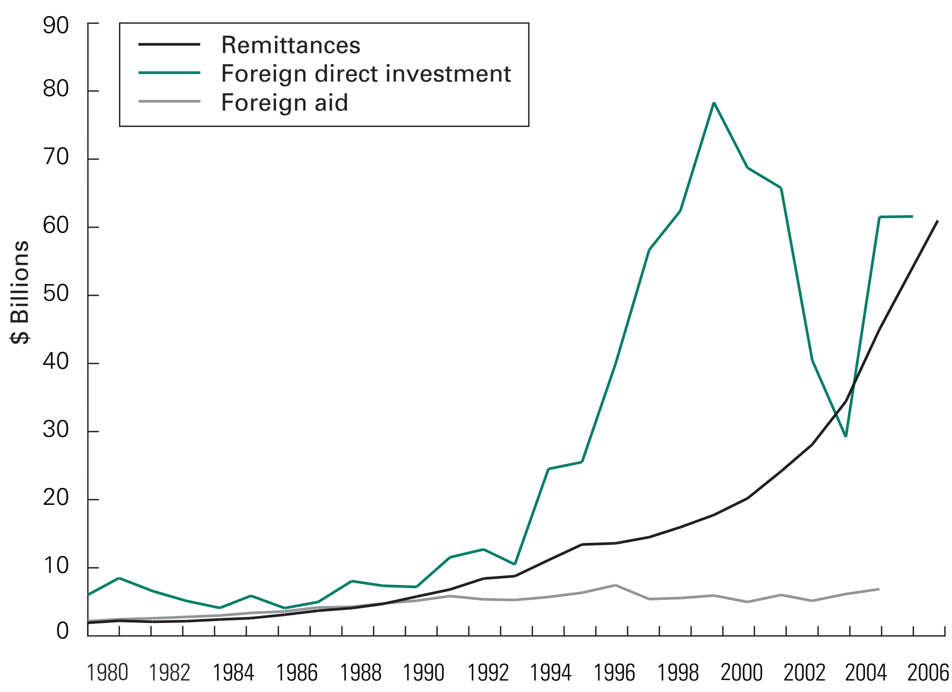
Peter Hakim, President
Inter-American Dialogue
May 2007

Context

Latin American migrants to the United States now send upwards of $50 billion a year to their families and communities in Latin America. Remittances are second only to foreign direct investment among international flows of capital to Latin America and the Caribbean (see figure 1). They exceed, by substantial margins, such other flows as portfolio investment, foreign aid, and government and private borrowing. For some countries, particularly in Central America and the Caribbean, they are larger than all of these other flows and foreign direct investment put together.

But it is not only the amount of money involved that makes remittances so significant for economic and social development in Latin America. For an economically volatile region known for its boom-and-bust cycles, remittance flows have been remarkably constant over many years—and may be responsible, in part, for the recent economic stability of so many Latin American countries. Remittances have grown markedly from year to year; moreover, when Latin American economies falter and growth diminishes, remittances to many countries tend to increase. Further, remittances, which are directed to low-income groups in most countries, are reducing poverty and improving social equity in Latin America, where income and wealth disparities are greater than in any other region of the world. And, unlike debt or imports, the largest share of remittances imposes no financial obligations on recipients. They are a family affair.

Figure 1: Latin America and the Caribbean: remittances, investment, and aid



Sources: *World Bank Development Indicators* (2006); Multilateral Investment Fund of the Inter-American Development Bank 2006, http://www.iadb.org/mif/.

These advantages notwithstanding, questions are regularly raised about whether remittances contribute to development, in Latin America and elsewhere. The argument is that remittances are inconsequential for development because they are mostly used to cover the cost of living. However, the opportunity for people to have a wider set of choices is precisely what development is all about. Remittances enable families to improve their diets, secure higher quality housing, dress better, and escape the drudgery of daily life. All of these activities have multiplier effects. More food has to be grown, processed, and sold. Houses have to be built or renovated. And even if the items purchased with remittances are imported, development still takes place. A television from Japan has to be delivered; a CD player from Korea must be repaired.

Furthermore, as discussed here, remittances are contributing substantially to national income in many countries. In Mexico, remittances are nearly 5 percent of national income; in several smaller countries, this proportion is even higher. For El Salvador, remittances are more than 15 percent of national income; for Jamaica, nearly 20 percent; and for Honduras, over 20 percent. A number of countries would fall into recession if remittances were curtailed, and growth rates would be lower in virtually every country north of Panama (see table 1).

In most countries, a large fraction of remittances are sent to rural areas, where incomes are generally far below national averages. And the majority of remittances in nearly all countries go to lower income families. Remittance recipients tend to have higher savings rates and spend more on education and health. Although research findings are not yet conclusive, there are good reasons to believe that remittances are making a substantial contribution to development, particularly to combating poverty and inequality.

> Sending remittances is unambiguously a private matter.

The question the Inter-American Dialogue Task Force on Remittances was asked to address was what, if anything, could be done to enhance the development outcomes of remittances. In seeking to answer this question, four key issues were explored:

- ▷ How the costs of sending remittances could be reduced further, thus adding to the amounts received by recipients
- ▷ What could be done to increase the number of migrants and their families in Latin America who have bank accounts
- ▷ How Latin American and Caribbean governments could create more productive opportunities for the use of remittances by expanding and improving such public services as health and education
- ▷ What would be needed to better understand the macroeconomic impacts of remittances

In addressing these issues, the task force started with a central premise—that the sending of remittances is unambiguously a private matter and that the basis of any constructive public policy or program is acknowledgment of the private nature of these flows. Every member of the task force agreed that remittances should not be taxed. They also agreed that remittances should not be directed to government programs and that official agencies monitoring remittance use should not infringe on individual privacy. Governments should enhance the opportunities for private citizens—through appropriate regulatory and policy incentives—to make productive use of remittances.

Reducing Transfer Costs: How Low Can You Go?

In the past several years, sending remittances from the United States to Latin America has become much less expensive (see figure 2). In the mid-1990s, the cost of sending $200 averaged about $30 (or 15 percent). By 2001, this cost had dropped to about $20 (10 percent), and to about $12 (6 percent) by 2005. The amount saved in transfer fees in 2005 alone was approximately $5 billion—far exceeding total foreign aid to the region that year.

Table 1: Remittances and key economic indicators

Country (Ordered by % GDP)	Remittances				
	As % GDP	Per capita ($)	Cost per transfer (%)	Average transfer ($)	Annual volume ($ millions)
Guyana	37	360	10	179	270
Haiti	35	116	7	123	1,100
Honduras	23	245	6	225	2,359
Nicaragua	19	155	5	133	950
Jamaica	18	623	8	209	1,770
El Salvador	18	411	5	339	3,316
Dominican Republic	13	271	6	176	2,700
Guatemala	11	238	6	363	3,610
Bolivia	10	94	6	235	989
Paraguay	9	89	9	263	650
Ecuador	6	136	4	293	2,900
Grenada*	5	220	—	220	23
Colombia	5	90	5	220	4,200
Barbados*	4	418	12	220	300
Suriname	4	122	10	220	102
Belize	4	149	9	220	93
Peru	4	89	5	169	2,869
Mexico	3	187	6	351	23,053
Costa Rica	2	92	9	301	520
Antigua and Barbuda*	2	140	—	220	11
Dominica*	2	56	—	220	4
Panama	1	62	11	196	292
St. Kitts and Nevis*	1	86	—	220	4
Brazil	1	31	8	541	7,373
St. Vincent and the Grenadines*	1	27	—	220	3
Trinidad and Tobago	1	71	11	200	110
St. Lucia*	1	25	—	220	4
Uruguay*	.3	71	11	198	115
Argentina*	.2	7	9	212	800
Venezuela	.1	5	17	138	124
Chile*	0	1	9	279	13

Sources: Central banks of each country, *World Bank Development Indicators* (2006), and data collected by Manuel Orozco.
Note: Excluding annual volume of remittances, all data are for 2005, except those indicated with an asterisk (*), which are for 2003. All data on annual volume of remittances are for 2006.

Table 2: Some characteristics of remittance recipients (percent)

Country	Live in rural areas	Female	Spend on health and education	Have a bank account	Non-remittance recipients with bank accounts	Have investments
Bolivia	—	52	—	44	35	—
Colombia	—	68	84	52	45	15
Dominican Republic	40	73	39	66	58	21
Ecuador	57	74	48	46	34	30
El Salvador	40	72	50	31	19	11
Guatemala	—	80	59	41	17	5
Guyana	40	71	23	62	—	12
Haiti	54	53	86	68	—	18
Honduras	—	—	—	34	16	4
Jamaica	—	—	—	65	60	—
Mexico	46	63	—	29	28	—
Nicaragua	45	72	54	10	10	27
Peru	—	46	—	37	35	—

Source: Data compiled by Manuel Orozco from multiple surveys (2005).

Table 3: Some characteristics of remittance senders (percent)

Country	Female	Have investments
Bolivia	71	4
Colombia	54	5
Dominican Republic	45	3
Ecuador	28	1
El Salvador	46	3
Guatemala	29	2
Guyana	48	8
Haiti	32	26
Honduras	37	4
Jamaica	49	2
Mexico	17	2
Nicaragua	44	3
Peru	—	—

Source: Data compiled by Manuel Orozco from multiple surveys (2005).

Table 4: Monthly cost of living, income, and remittances ($)

Expenses and Earnings of Remittance Recipients	Jerez, Mexico	Catamayo, Ecuador	Suchitoto, El Salvador	Salcaja, Guatemala	May Pen, Jamaica
Cost of living*	359	348	352	403	478
Wages	323	303	125	162	200
Remittances received	637	331	515	181	200
Total earnings, remittances included	960	634	640	343	400

Source: Orozco (2006a).

*Monthly cost of living includes food, utilities, education, health, and entertainment expenses. It excludes housing expenses.

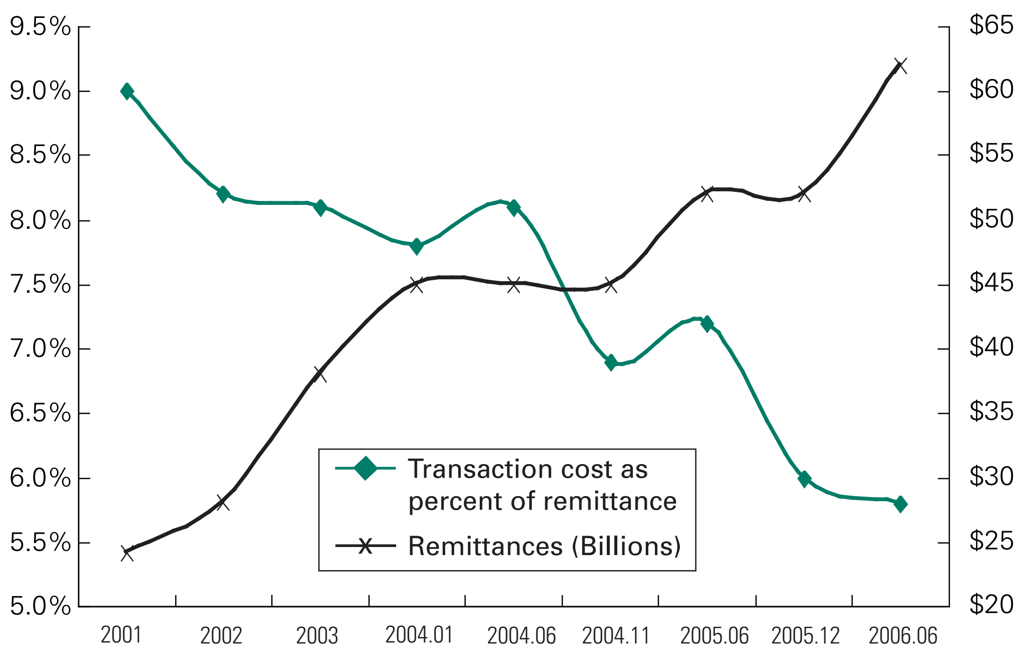
The decline in fees can be explained largely by growing competition among money transfer operators (MTOs), companies that send and receive money but do not offer banking services. Today, for example, more than 100 MTOs are serving Mexico; a dozen years ago, there were just five. The use of technology has also increased. Directo a México, an automated clearinghouse, charges U.S. banks only 67 cents per transaction to transfer money to Mexican banks (see box). Other companies are expanding their use of automated teller machines (ATMs), debit and credit cards, and prepaid cards. Some are experimenting with the use of cell phones to make remittance transfers.

MTOs are the principal means for transferring remittances to most countries. For some destinations, MTO operating costs make it difficult to bring prices down much further. The average cost of managing a remittance collection point (which includes rental or purchase of space, salaries, and equipment) is about $7 per transfer. In recipient countries, additional investments have to be made in delivery services, with expenses varying from place to place. For instance, a

The Experience of Directo a México

The Federal Reserve Bank of Atlanta, along with the Bank of Mexico, created an innovative bank-to-bank binational automated clearinghouse to facilitate affordable and secure remittance transfers to Mexico. This service, branded for consumers as Directo a México in 2005, is currently being used by at least 35 banks. The clearinghouse requires that senders and recipients have bank accounts in the Federal Reserve's network. The cost of a transfer is 67 cents.

Figure 2: Total value of remittances sent to Latin America and the Caribbean and transaction costs of remitting



Source: Orozco (2006b).
Note: The transaction cost is based on a remittance of $200.

money transfer to Mexico costs about 5 percent of the amount sent, and this charge cannot be reduced much more—even with the adoption of innovative business models and new technologies. Average costs are higher in the Dominican Republic and Haiti, where remittances are typically delivered to recipients' homes. However, substantial price reductions are possible in several particularly high-priced corridors, including the United States to Cuba and the United States to Venezuela, where competition and innovation are limited.

Beyond expenses related to the individual recipient countries, there is another set of factors affecting MTO operating costs. Specifically, the U.S. post-9/11 regulatory environment has added to the cost of sending remittances. Tighter regulations and compliance with new anti-money-laundering legislation have raised MTO costs of doing business. There has also been a significant increase in the regulatory scrutiny of banks that provide services to MTOs, and a growing number of banks are choosing not to do business with MTOs rather than absorb the higher management costs and increased risk. Many MTOs are struggling to find banks to serve their needs and are consequently paying higher banking costs. As a result, some MTOs have had to suspend part or all of their operations.

No one opposes efforts to combat money laundering to curtail the financing of criminal networks and terrorist groups. Illegal financial transactions must be aggressively policed. But no one gains when legitimate businesses unnecessarily get caught up in enforcement actions. The regulators waste resources, the cost of doing business goes up, and—in the case of remittances—low-wage immigrant workers and their low-income families pay a high cost. Surely, it should be possible for regulators to work with banks and MTOs to develop mechanisms that would facilitate (or at least not interfere with) the flow of remittances while combating money laundering. The predictability of MTO operations and the small sums involved in each transaction (the average transfer is about $200) should allow for an approach that is less burdensome.

Every effort should be made to get remittance senders and recipients to open and use bank accounts.

Other initiatives that could help reduce costs include the following:

- ▷ **Encouraging or requiring MTOs to provide accurate, up-to-date information on their costs and methods of operation**. Transparency is critical. MTOs should provide their customers with information on the fees they charge, the exchange rate they will use to convert the dollars into foreign currency, how they will transfer and deliver the money, and any additional financial services they might offer. An industry-wide agreement on what information to provide and how to present it would be an important aid to immigrant senders. In addition, the adoption of a common formula for determining exchange rates would eliminate a major source of confusion for senders about the pricing process. One or more independent groups, either official or nongovernmental, could monitor the accuracy and completeness of MTO disclosures and work with community organizations and financial institutions to educate senders on how to use the information.
- ▷ **Promoting cooperation between banks and MTOs**. While banks and MTOs are competitors in the remittance transfer business, they could both benefit from some measure of cooperation that would take advantage

of their relative strengths. For their part, banks offer a wider range of services than MTOs and greater geographical coverage in both the United States and abroad. MTOs tend to be seen as trustworthy by senders and recipients, and they offer experience with remittances and better knowledge of sender and recipient communities. Such collaboration could result in more remittance senders and recipients using banks and their products, including credit and debit cards—which would probably speed the transition to account-to-account transfers.

▷ **Accelerating the use of new technologies**. New technologies that enable transfers from bank account to bank account would result in far less costly transactions, but MTOs, financial institutions, and senders and recipients would have to learn how to use these new technologies and make substantial adjustments in their behavior. International debit cards are perhaps the most promising technology because they make possible remittance transfers to overseas banks that are linked to a network of retail stores. It is encouraging that nearly 30 percent of remittance recipients already use debit or credit cards; this proportion is as high as 50 percent in some countries (Orozco et al. 2005).

Banking the Unbanked

The most critical recommendation of *All in the Family*—the 2004 publication of the Dialogue's Task Force on Remittances—is that policy and advocacy efforts by all institutions should focus on encouraging remittance senders and recipients—indeed, all citizens and residents—to use bank accounts. That recommendation is still paramount. Banks and other financial institutions can help reduce the cost of money transfers because they are able to move money across international boundaries more cheaply than MTOs or couriers. Perhaps even more important, they offer a range of other relevant products: interest-bearing savings accounts; checking accounts for paying bills (replacing costly money orders); free and secure check-cashing services; the means to establish a credit history, such as credit and debit cards; loans for housing and education; small business credit; and insurance products. With accounts in banks or other financial institutions, migrants and their family members back home become economic citizens as well as promote economic development in their countries (Fajnzylber and Lopez 2007).

U.S. Banks

Over the past several years, U.S. banks have made progress in recruiting remittance senders. More than 100 U.S. banks now offer remittance transfer services, and a variety of innovative experiments are under way; worth noting are the following:

▷ Over 50 U.S. banks have partnered with MTOs to provide remittance services.

▷ More than 150 U.S. banks are taking advantage of an automated clearinghouse established by the Federal Reserve Bank of Atlanta and the Bank of Mexico. The clearinghouse processed about 350 transfers in August 2006, a threefold increase in monthly transactions since the beginning of the year.

▷ BANSEFI, a Mexican government development bank, is seeking to allow bank account holders in the United States to open a linked bank account for relatives in Mexico to whom they send remittances.

▷ The New Alliance Task Force—a joint initiative of the Federal Deposit Insurance Corporation and the Consulate General of Mexico—is a coalition of banks, community organizations, and government agencies working to facilitate immigrant access to the U.S. banking system. The coalition's efforts have resulted in more than 183,000 new accounts opened by immigrants over the past four years.

Their promise notwithstanding, these efforts are all experiments, and none has managed to recruit large numbers of immigrant customers, despite the enormous advantages that come with opening a bank account. Nor have many U.S. banks been eager to join these programs. In short, not much progress has been made in bringing Latin American immigrants into the U.S. banking system.

Adoption of the recommendations in *All in the Family* depends mostly on the willingness of banks to change their ways of doing business. When that report was written, the task force believed U.S. banks would, on their own, conclude that serving the immigrant community was good business. Some banks have responded, but the number is far too small. Moreover, the Patriot Act and other anti-money-laundering efforts discourage banks from offering remittance services, which could be an incentive for immigrants to open accounts. As the recommendations of the present report suggest, the task force is now convinced that it will take a heavier dose of government policy to make a difference, although much of the initiative still must come from private banks and community and immigrant organizations.

To encourage more immigrants to use banking services, the task force recommends the following:

- ▷ **The FDIC and Federal Reserve of Atlanta experimental programs discussed above must be vigorously pursued by other parts of the Federal Reserve System and other government agencies**. Although these programs are valuable, they have had only limited reach. The U.S. government should understand the importance of moving remittance flows from informal markets to the banking system, where they are more easily monitored—and where criminal activity can be confronted more effectively and individuals' rights better protected. The U.S. government should enforce the Patriot Act and other anti-money-laundering statutes in ways that do not keep remittance senders out of U.S. banks. Everyone gains when remittance senders become bank customers—banks and senders, recipients, their communities and countries—and U.S. security is enhanced.
- ▷ **Private banks should do more to make their services attractive to immigrants**. Besides remittance services, banks should consider providing additional products for immigrants. For example, they could offer low-cost money orders and direct electronic payments (without requiring checking accounts). These services make MTOs and check-cashing stores vital for newly arrived immigrants, but banks could perform these tasks—and others—better and cheaper. Hiring bilingual tellers and offering extended hours would also make banks more attractive to immigrants. As an alternative to check cashing, banks, prepaid card companies, and MTOs could offer debit or prepaid cards into which immigrants could deposit their paychecks and then use them for transactions in stores accepting such cards. The suggested initiatives are straightforward and should not be costly to test.
- ▷ **Community organizations—where possible in cooperation with banks, government agencies, foreign consulates, and financial institutions—should provide immigrants with information on managing their finances**. Better financial management can reduce economic burdens on immigrant families, and the advantages of a bank account—as well as the costs of not

having one—should be made clear. Furthermore, immigrants must be informed of how to acquire the identification needed to open a bank account.

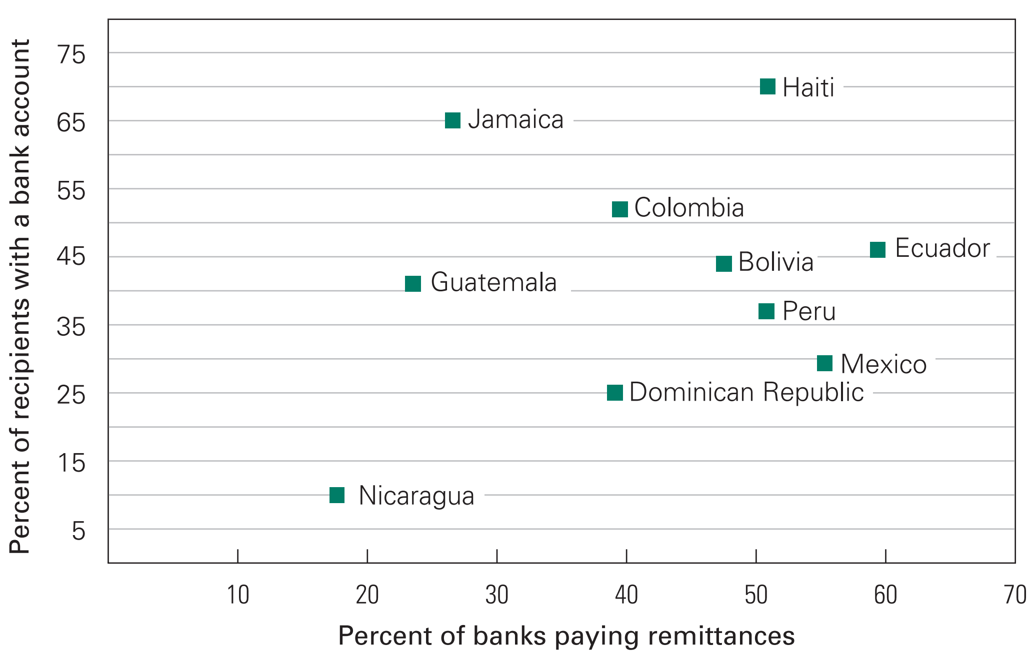
Latin American and Caribbean Banks

Progress in encouraging remittance recipients in Latin American and Caribbean countries to open bank accounts has also been slow. Ironically, across Latin America, banks distribute nearly 50 percent of all transfers—but so far, they have not taken advantage of this central role to turn recipients into bank customers (see figure 3).

Sustained and intelligent efforts to recruit low-income customers do produce results (see table 5). In Mexico, BANSEFI established L@ Red de la Gente, a network of some 1,200 banks, microfinance institutions (MFIs), and credit unions that serve as remittance distribution centers. By the end of 2006, L@ Red de la Gente was distributing 100,000 transfers a month. In 2003, Caja Popular Mexicana, the largest credit union in Mexico, began distributing remittances for several MTOs. With a network of 330 branches in 28 states, the credit union has distributed over $165 million in remittances to recipients in rural Mexico. Membership in the credit union has grown from 600,000 to over 1 million since 2003. Moreover, BBVA-Bancomer, a remittance payer that distributes over 40 percent of all flows to Mexico, transfers more than 12 percent of these flows from account to account. This means that more than a half-million Mexicans are now using bank accounts.

In Guatemala and El Salvador, the record is even better. The Guatemalan Banco Industrial entered the remittance business as a payer

Figure 3: Access of remittance recipients to banks and bank accounts



Source: Orozco (2006b).

for King Express, a major U.S. MTO. When Banco Industrial realized that some recipients were interested in opening accounts, it began offering a range of financial services; about 30 percent of its remittance clients now have a savings or checking account. Banco Salvadoreño adopted a different model (see box). It opened its own MTO in the United States, and most of its transactions go directly into bank accounts in El Salvador. The Salvadoran Federation of Credit Unions has enrolled about 25 percent of its remittance recipients as members (Orozco and Hamilton 2005).

Credit and savings cooperatives and MFIs are also providing financial services to a growing number of remittance recipients. In rural Guatemala, for example, the credit union Salcaja offers remittance recipients a wide range of products, including pensions, life and medical insurance, home equity, and small business credit. Although only 3 percent of remittance payers in Latin America are MFIs, they have been recruiting one-third of their remittance recipients as clients (Orozco and Hamilton 2005; Orozco 2006b).

The experiences of these institutions illustrate how remittance recipients can be transformed into bank customers—but their efforts are the exception in Latin America and the Caribbean. Most banking institutions in the region offer only cash withdrawals to remittance recipients, showing little interest in providing them other services. Low-income groups do not usually have access to bank services for a host of reasons (for example, banks may be geographically inaccessible, require minimum deposits that are too high for low-income people, or simply not be very accommodating to poorer people). This lack of access prevents countries from taking full advantage of remittance flows—either for national development or for bringing excluded groups into the economic mainstream. In Central America, for example, each bank receives an average of 30,000 remittance transfers a month, but each bank's client base averages fewer than 10,000 customers, the majority of whom are not remittance recipients. Remittance transfers are an important source of income for banks, comprising up to 8 percent of total revenue for some banks. Banks and financial institutions in Central America could reach out to remittance customers to increase their clientele and revenue base (Claros 2006).

Latin American governments need to do much more to promote wider access to financial

The Experience of Banco Salvadoreño

Banco Salvadoreño is an example of the link between MTOs, banks, and financial services in El Salvador. Currently, banks receive 70 percent of all remittances in El Salvador. Banco Salvadoreño has a presence in most U.S. states because of BancoSal, an MTO it established, and strategic alliances with some of the biggest MTOs, including Western Union and Bancomer Transfer Services. In 2005, Banco Salvadoreño made over 1 million remittance payments, totaling $256 million. Of these payments, $90 million were transfers from its own BancoSal, and 63 percent of BancoSal transfers were deposited directly into the accounts of at least 13,000 remittance recipients at Banco Salvadoreño. Banco Salvadoreño offers remittance recipients the opportunity to borrow up to 80 percent of the last six months' remittance flows. The bank has also opened more than 29,000 savings accounts for recipients and distributed nearly 9,000 debit cards to small business owners and more than $10 million in loans to Salvadorans living abroad. In addition, Banco Salvadoreño is the only bank in El Salvador that has an Internet-based remittance service that enables clients to use the bank's Web site to send money from any account in the United States.

The Experience of the Jamaica National Building Society

An important lesson from the Jamaican experience is that the "bancarization" of small businesses, such as convenience stores that install ATMs or accept debit cards, is not only feasible but also promotes economic development. In Jamaica, remittance receipts have been accompanied by the distribution of debit cards by banks and some MFIs. Meanwhile, banks and MFIs have also offered ATMs and electronic points of sale at a low cost to their small business clients, many of which offer goods and services demanded by typical remittance recipients.

The Jamaica National Building Society (JNBS), through its subsidiary JN Money Services Ltd., serves Jamaicans living abroad by offering remittance services in Canada, the United States, and the United Kingdom. In partnership with the U.S. Agency for International Development, JNBS has automated the process of sending and receiving money transfers through swipe card technology. As a result, JNBS now has over 70,000 money transfer card users. JNBS's Computers in Schools project applied one-third of the cost savings accrued from the money transfer card to education, donating approximately 250 computers to schools across the island. In turn, 50 percent of remittance recipients in Jamaica have been brought into the formal banking system, with 25 percent of those receiving remittances through a card product that can be used for purchases at small businesses that accept debit cards. These small businesses, clients of JNBS, are benefiting from their relationship with remittance-receiving customers. Savings ratios have increased considerably, not only through direct deposits to savings accounts, but also through a reduction in the amount of cash in circulation and the increased use of electronic transactions.

institutions. Governments can and should encourage banks to actively recruit low-income customers. In many cases, governments in the region must revise regulations that discourage banks and other financial institutions from offering services to the poor—which hurts both banks and national development prospects. For their part, banks should learn about the needs of low-income groups and what it would take for them to open accounts. Remittances give people the resources to participate in the formal financial system, and they should provide banks with substantial incentives to seek out recipients and turn them into customers. Conversely, banks, governments, and nongovernmental organizations in Latin America should together be doing more to educate remittance recipients about the value of bank accounts.

Table 5: Number of accounts opened by remittance recipient households at credit unions and MFIs (2005)

Institution	Number of accounts opened	Number of monthly transfers	New accounts as % of monthly transfers
L@ Red de la Gente (Mexico)*	10,000	100,000	10
Guayacan (Guatemala)	533	5,426	10
El Comercio (Paraguay)*	2,000	20,000	10
Coosadeco (Guatemala)	529	4,780	11
Fedecaces (El Salvador)	4,375	22,000	20
Acocomet (El Salvador)	800	2,383	34
Salcaja (Guatemala)	500	1,000	50
Banco Solidario (Ecuador)	4,000	5,000	80
Acacu (El Salvador)	2,703	2,703	100

Source: Orozco and Hamilton (2005).

*December 2006.

Remittances and Development: Macroeconomic Impacts and the Role of Governments

The amount and continuing growth of remittance flows to Latin America and the Caribbean present the region's governments and international organizations with an array of policy issues. The central question is what governments can and should do to account for remittances in broader economic and social policies. One of the challenges to developing coherent policies on remittances is that the transfers are private (mostly within families), each transaction is relatively small (averaging about $200), and the transfers are decentralized and mostly outside the formal banking system. Although there are increasingly reliable data on the volume of remittances reaching almost all recipient countries, the statistics have been collected for only a short time, and variations among countries are great. The models that have so far been used to analyze and interpret these data were developed for other financial flows and are not yet well adapted to remittances. Accordingly, any research linking remittances to macroeconomic or development phenomena have to be considered tentative at this point.

Some preliminary conclusions are worth noting, however:

1. Remittances are central to economic growth, national expenditures, and balance of payments for many countries in Latin America—particularly Mexico, almost all of Central America and the Caribbean, Bolivia, Colombia, Ecuador, and Peru. Remittances represent more than 15 percent of the national income of Honduras, Jamaica, and El Salvador. In many other countries, including Mexico, remittances make up nearly 5 percent of national income. Haiti, where remittances account for some 35 percent of national income, is clearly an outlier. Remittances bolster economic growth, particularly in countries recovering from financial crises (Fajnzylber and Lopez 2007).
2. Despite their economic significance, remittances must be treated as voluntary transfers between individuals and their families. Governments seeking to tax remittances or intervene in their use will provoke remitters to stop sending money or turn to transfer channels outside official control. Regardless of their volume and importance, these decentralized flows are inappropriate for direct government intervention.
3. As remittances increase in importance in the economy, some variant of the "Dutch disease" emerges, leading to higher exchange rates and a deterioration in the balance of payments. Export growth tends to decline while imports increase. However, these effects are partially counterbalanced in some places by the regular travel of expatriates to their countries of origin and the external market for home country goods created by emigrants.
4. Although the numbers are inexact, savings from remittances appear (even under conservative assumptions) to have become an increasingly important source of investment financing. These savings have not eliminated Latin America's debt, but remittances have surely reduced its magnitude—thus setting the stage for more sustainable economic growth. Because remittance flows tend to be countercyclical (that is, they increase when recipient economies turn downward), they should help dampen Latin America's economic volatility.

5. The value of remittance flows to national development could be enhanced by sound economic policies in recipient countries. Good policies and predictable economic environments will provide greater opportunities for remittance recipients and encourage reinforcing flows of investment capital.
6. Research and statistics are scarce on how remittances are used by recipients, their effects on family and community well-being, and their contribution to reducing poverty and inequality. Remittances obviously are improving the lives of poor families and communities in most recipient countries—particularly those in which migrant senders come from the poorest groups. Low-income rural areas receive a large share of remittances in a majority of countries. And remittances mostly go to poor families; over half of all recipient households in Latin America earn less than $200 per month. In Guatemala, 60 percent of household income for the poorest 10 percent of the population is from remittances. In short, remittances are—in most places—helping improve Latin America's skewed income distribution. This is particularly important in countries with low per capita incomes and large inequalities between rich and poor.

Although these preliminary findings do not yet provide much guidance for remittance policy, two points are clear:

▷ **Governments and international organizations should invest much more in research on remittances and their impact**. The quality and extent of research and data collection should reflect the size of remittance flows and their importance to national, local, and family economies. When finally recognized—perhaps in the past half-dozen years—the sheer amount of remittances surprised almost everyone. Now it is time to generate the information and analysis necessary to understand these flows, how much they contribute to development, and what policies can make them more valuable both to senders and receivers and their communities and families.

▷ **Governments should not intervene in remittance flows by imposing taxes or burdensome regulations**. Instead, banks should be encouraged to make their services more accessible to remittance recipients. There is still too little information to suggest the extent to which governments should seek to offset the impact of remittances on trade and exchange rates or which instruments governments should use. Governments should not count on remittances to be the main driver of national development—nor to solve problems of poverty and inequality. Positive government initiatives are needed to deal with these challenges.

REFERENCES

Claros, Jose Ignacio. 2006. "Grupos Financieros." *Estrategia y Negocios* 77 (May).

Fajnzylber, Pablo, and J. Humberto Lopez. 2007. *Close to Home: The Development Impact of Remittances in Latin America*. Washington, DC: World Bank.

Inter-American Dialogue Task Force on Remittances. 2004. *All in the Family: Latin America's Most Important Financial Flow*. Washington, DC: Inter-American Dialogue.

Orozco, Manuel. 2006a. "Between Hardship and Hope: Remittances and the Local Economy in Latin America." Washington, DC: Inter-American Dialogue. http://www.thedialogue.org/programs/policy/trade/remittances/default.asp.

———. 2006b. "International Flows of Remittances: Cost, Competition and Financial Access in Latin America and the Caribbean—Toward an Industry Scorecard." Washington, DC: Inter-American Dialogue. http://www.thedialogue.org/programs/policy/trade/remittances/default.asp.

Orozco, Manuel, B. Lindsay Lowell, Micah Bump, and Rachel Fedewa. 2005. *Transnational Engagement, Remittances and Their Relationship to Development in Latin America and the Caribbean*. Washington, DC: Institute for the Study of International Migration, Georgetown University.

Orozco, Manuel, and Eve Hamilton. 2005. "Remittances and MFI Intermediation: Issues and Lessons." In Judith Shaw, ed., *Remittances, Microfinance and Development: Building the Links, Volume 1: A Global View*. Brisbane, Australia: Foundation for Development Cooperation.

World Bank. 2006. *World Bank Development Indicators*. Washington, DC.

INTER-AMERICAN DIALOGUE

1211 Connecticut Avenue, NW
Suite 510
Washington, DC 20036

PHONE: 202-822-9002
FAX: 202-822-9553
EMAIL: iad@thedialogue.org
WEB: www.thedialogue.org