Worker Migration and Remittances in South Asia

Every year South Asian countries send out a significant number of migrant workers, resulting in remittances becoming an important source of funds for economic development. However, despite its huge potential to contribute to economic growth, South Asian countries have not yet fully maximized benefits from remittances because of their limited financial sector development and financial inclusion, and because a substantial portion of remittances to the region are channeled informally. Concerted efforts by the governments, regulators, and financial sectors are required in addressing legal and policy constraints, improving formal financial systems, and enhancing customer education to expand formal remittance markets and achieve financial inclusion.

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Worker Migration and Remittances in South Asia

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No. 12 May 2012

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ABSTRACT

South Asia is a remittance economy. Every year, South Asian countries send out a significant number of migrant workers and remittances sent by migrant workers become an important source of funds for economic development of the countries. Over the last decade, migrant workers going abroad from South Asia has been continuously on the rise and reached nearly 1.5 million in 2010. The global financial crisis in 2008 affected, but only moderately, worker migration from South Asia, and the number of outgoing migrant workers still greatly surpasses the number of returning migrant workers. Corresponding to the growth of the number of migrant workers, remittance inflow to South Asia show a significant growth and reached a record high $72 billion in 2010. This shows, however, only officially recorded figures and the total remittance including informal remittances is substantially greater than the officially recorded amount. The prevalence of informal remittance systems is a key characteristic of remittances in South Asia and is attributed to the limited financial development and inclusion in the region. The high dependence on informal remittances by South Asian migrant workers is a concern for the governments and regulators because informal remittances are not only ineffective to promote productive financial intermediations, but also can be sources for smuggling, money laundering, and other illegal activities. Efforts to restrict informal remittances by the regulators so far have had limited impacts. Rather, it is observed that informal remittance systems have a strong appeal to unbanked populations especially in rural areas due to their relatively low cost, speed, accessibility, and customer friendliness. Concerted efforts by the governments, regulators and financial sectors are required in addressing legal and policy constraints, improving formal financial systems, and enhancing customer education to significantly expand formal remittance markets and achieve financial inclusion.
ABBREVIATIONS

MFI microfinance institutions
MTO money transfer organizations
NCCBL National Credit and Commerce Bank Limited
NFCD Non-Resident Foreign Currency Deposit
NRB Nepal Rastra Bank
NRI Non-Resident Indian
POS point-of-sales
TMSS Thengamara Mohila Sabuj Sangha
UAE United Arab Emirates
I. Worker Migration from South Asia

A. History and Trends

1. South Asia is a remittance economy. South Asian countries send out a significant number of migrant workers annually and remittances sent by migrant workers become a significant source of funds for economic development of the countries. Most governments in South Asia view worker migration as helping to curtail unemployment, reduce poverty, and earn foreign exchange through remittances, and make worker migration as one of the key economic policy priorities.

2. Historically, South Asian migrant workers are categorized into two types. The first group includes the immigrants and permanent residents to industrialized countries in the 1950s and 1960s, mostly professionally qualified persons such as medical doctors, academicians and engineers, migrated to the more developed countries, especially western countries. The second type of group includes short-term semi-skilled or unskilled migrant workers. The number of the second group workers has increased especially in the 1970s when the surge in oil prices led to the oil-producing Middle East countries heavily investing in infrastructure development. The second group of migrant workers is found predominantly in Saudi Arabia, the United Arab Emirates (UAE), Kuwait, Qatar, Oman, Iraq, and Libya. Since the mid-1980s, such migration expanded to the newly industrialized countries in East and South East Asia, such as the Republic of Korea, Malaysia, and Singapore.

![Figure 1.1: Annual Migration Outflow from South Asia, 2000–2010](image)

Sources: Ministry of Overseas Indian Affairs, the Government of India; Bureau of Manpower Employment and Training, Ministry of Expatriate Welfare and Overseas Employment, the Government of Bangladesh; Ministry of Finance, the Government of Nepal; Sri Lanka Bureau of Foreign Employment, the Government of Sri Lanka.

3. Overall, worker migration from South Asia has been continuously on the rise until 2008, when the number of total worker migration from the four countries (Bangladesh, India, Nepal, and Sri Lanka) reached over 2 million (Figure 1.1). The global financial crisis in 2008 has affected worker migration in South Asia and the number of outgoing migrant workers decreased by 30% from 2008 to 2009. However, the crisis did not fundamentally alter the migration trends.
in South Asia and the number of outgoing migrant workers significantly surpasses the number of returning migrant workers. The oil exporting Middle East countries, i.e., Dubai, Qatar, UAE, and Saudi Arabia have been less affected by the crisis due to the reserves accumulated during the time of high oil prices which enable them to finance the infrastructure projects even after the crisis. In 2009, nearly 80% of migrant workers from South Asia work in the four Middle East countries: UAE, Saudi Arabia, Qatar, and Oman (Figure 1.2). This high concentration of South Asian migrant workers in the Middle East countries is expected to continue at least foreseeable future, especially because the industrialized South-East and East Asia were more severely affected by the global financial crisis. Malaysia, for example, took direct measures to curb migrant workers from abroad by deciding not to recruit foreign migrant workers in the manufacturing and service sectors from January 2009 and doubled the levy for hiring them in order to increase the salaries of local workers.

**Figure 1.2: South Asia Migration Outflow by Destination, 2009**

![Pie chart showing migration outflow by destination, 2009](image)

UAE = United Arab Emirates.

Sources: Ministry of Overseas Indian Affairs, the Government of India; Bureau of Manpower Employment and Training, Ministry of Expatriate Welfare and Overseas Employment, the Government of Bangladesh; Ministry of Finance, the Government of Nepal; Sri Lanka Bureau of Foreign Employment, the Government of Sri Lanka.

i. **Bangladesh**

4. According to the government estimates, the stock of migrant workers from Bangladesh will exceed 5 million, or about 3% of the total population in 2011. The annual average outflow of migrant workers between 2000 and 2010 is around 435,000 persons. Around 80% of all migrants are located in oil exporting countries, and a large component, or about 40% are based in UAE. Other major destinations among the Middle East countries are Oman and Kuwait which host 12% of the migrant workers, respectively. Other major destinations outside of the Middle East include Singapore, which account another 11% (Figure 1.3).
ii. **India**

5. A total of 6 million migrant workers went abroad from India from 2000 to 2010, growing on average at the rate of 16% annually. UAE, Oman, Qatar, and Kuwait are the top four destination countries and absorb approximately 85% of the total migrant workers in 2010. At the same time, migration from India to other industrialized countries such as Singapore, in particular to the information technology related sector, grew significantly (Figure 1.4).

iii. **Nepal**

6. It is estimated that 1.5 million Nepali nationals are working in India. However, they are not officially accounted as migrant workers by the Indian authorities due to the no visa policy between the two countries. The official figure of Nepal migrant workers registered with the Ministry of Labour as of July 2009 was 219,956 persons. During 2000 to 2010, a total of 1.6 million migrant workers left the country. The number of outgoing migrant workers grew steadily at the rate of 26% on average. Qatar, Saudi Arabia, Malaysia, and UAE are the top four destinations and account 87% of labor migration from Nepal (Figure 1.5). As compared to other South Asia countries, Nepal especially has a high dependence on Malaysia as a migration destination and 16% of the outgoing migrant workers from Nepal went to Malaysia in 2010. As a consequence of the financial crisis, the number of migrant workers departing from Nepal to Malaysia decreased by 90% from 2008 to 2009.
Figure 1.4: India Migration Outflow by Destination, 2010

UAE = United Arab Emirates.
Source: Ministry of Overseas Indian Affairs, the Government of India.

Figure 1.5: Nepal Migration Outflow by Destination, 2009

UAE = United Arab Emirates.
Source: Ministry of Finance, the Government of Nepal.
iv. Sri Lanka

7. It is estimated that over 1 million Sri Lankans are currently working abroad. From 2000 to 2010, in total, 2.4 million migrant workers left Sri Lanka. The average growing rate of the number of migrant workers was 3% during the same period. However, the growth rate of the number of migrant workers decreased by 4% in 2009 largely due to the effect of the financial crisis. Qatar, Saudi Arabia, Malaysia, and UAE are the top destination countries and absorb 82% of the total migrant workers from Sri Lanka in 2009 (Figure 1.6).

Figure 1.6: Sri Lanka Migration Outflow by Destination, 2009

[Diagram showing migration outflow to various destinations]

UAE = United Arab Emirates.
Source: Sri Lanka Bureau of Foreign Employment, the Government of Sri Lanka.

B. Government Policies and Regulations

8. Among the countries in South Asia, Bangladesh has the most comprehensive overseas employment policy, which was adopted in 2006. There are three government agencies to manage the welfare of migrants: the Ministry of Expatriates’ Welfare and Overseas Employment; its Bureau of Manpower, Employment and Training; and the Bangladesh Employment Services Limited. The Ministry of Expatriate Welfare and Overseas Employment has the mandate of increasing overseas employment for Bangladeshi nationals and ensuring the welfare of migrant workers. The Ministry is primarily responsible for implementing the legal and regulatory framework for international migration, registering recruitment agencies, managing the labor wind in diplomatic missions abroad, and administrating the Wage Earners’ Welfare Fund. Bureau of Manpower, Employment and Training is responsible for providing regulatory oversight on recruiting agencies, developing and implementing training programs for national and international labor markets, and organizing pre-departure briefings for migrant workers. Bureau of Manpower, Employment and Training; and Bangladesh Employment
Services Limited functions as a consultant and recruitment agency for Bangladeshis looking for foreign employment. The government has also set up the Wage Earners' Welfare Fund to expand the scope of coverage for migrant workers (Table 1.1).

Table 1.1: Legal and Institutional Frameworks for Worker Migration in South Asia

<table>
<thead>
<tr>
<th>Legal and Regulatory Framework</th>
<th>Bangladesh</th>
<th>India</th>
<th>Nepal</th>
<th>Sri Lanka</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ministry in Charge</td>
<td>Ministry of Expatriate Welfare and Overseas Employment</td>
<td>Ministry of Overseas Indian Affairs</td>
<td>Ministry of Labour and Transport Management</td>
<td>Ministry of Employment and Labor</td>
</tr>
<tr>
<td>Executing Agency</td>
<td>Bureau of Manpower, Employment and Training</td>
<td>Office of Proctor of Emigrants</td>
<td>Department of Labour and Employment Promotion</td>
<td>Sri Lanka Bureau of Foreign Employment</td>
</tr>
<tr>
<td>Pre-migration Services</td>
<td>Provision of market information; training and pre-departure briefings</td>
<td>State governments have set up manpower corporations to promote labor exports</td>
<td>Provision of market information; skills training and pre-departure briefings</td>
<td>Foreign market information; skills training; pre-departure briefings, and pre-departure loans and life insurance</td>
</tr>
<tr>
<td>Post-migration Services</td>
<td>Labor attaché to promote overseas employment and assistance to migrants, including assistance in settling disputes</td>
<td>Labor attaché to provide welfare assistance to migrants, including assistance in settling disputes</td>
<td>Embassies of Nepal to solve the problems of migrants, but they are not present in all labor recipient countries</td>
<td>Labor attaché to promote overseas employment and welfare; officer to ensure the welfare of migrants including settling of disputes</td>
</tr>
<tr>
<td>Welfare Fund for Migrants</td>
<td>Wage Earners' welfare Fund; a publically administered fund based on the contributions of migrants and spent for their welfare including death and disability</td>
<td>Individuals are required to take private insurance for death and disability before departure; setup of a non-resident Indian welfare fund being considered</td>
<td>Individuals are required to take private insurance up to NRs100,000</td>
<td>Overseas Workers Welfare Fund, based on fees by migrants prior to departure</td>
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<td>Recruiting Agencies</td>
<td>Registered; well-laid procedures for registration; mildly regulated</td>
<td>Registered; well-laid procedures for registration; mildly regulated</td>
<td>Registered; well-laid procedures for registration; mildly regulated</td>
<td>Registered; well-laid procedures; mildly regulated</td>
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SRO = Statutory Rules and Regulatory Orders.

9. Traditionally, the Government of India has had limited involvement in worker migration. However, the growing number of short-term worker migration to the Middle East and Malaysia prompted the Government of India to institute policies on migration. The key focuses of the migration policies are preparing migrants, controlling and monitoring the licensing and brokers, and safeguarding migrants’ rights in host countries. Maximizing their remittance potential, and facilitating reintegration upon their return. To support the policy, the Indian Emigration Act
was enacted in 1983 focusing on the welfare of the migrants and promotion of overseas employment. The Protector-General of Emigrants at the Ministry of Overseas Indian Affairs is responsible for monitoring migrant workers’ welfare. Since 2003, there is a compulsory insurance system for Indian migrant workers and the government established a welfare fund for migrant workers and negotiated bilateral agreements on the transferability of their social security contributions.

10. Recently, the Government of Nepal has recognized overseas employment opportunities as one way to alleviate poverty and unemployment of the country, and reflected its policies on overseas employment in its Three Year Interim Plan (2007–2010). Nepal’s Foreign Employment Act 1985 aims to regulate provision of recruiting agencies licensed to procedure of selecting workers. The Department of Labor and Employment Promotion of the Ministry of Labor and Transport Management is the principal agency that supports migrant workers. The Department of Labor and Employment Promotion has the responsibility for registering foreign employment recruiting agencies, issuing recruitment licenses to recruiting agencies, and promoting programs of foreign employment and collecting overseas employment information and initiating training and welfare activities for migrant workers.

11. Like any other South Asian countries, Sri Lanka also has a proactive policy on worker migration, and is the only country that promotes female migration. Migration and remittances are looked after by the Ministry of Employment and Labour, along with its implementing machinery, the Sri Lanka Bureau of Foreign Employment. While the Ministry has responsibility for formulating policies and monitoring the administration of foreign employment, the Sri Lanka Bureau of Foreign Employment implements a wide range of workers’ welfare programs, both at home and in host countries. Those include mandatory pre-departure skill and awareness training, compulsory registration of workers, free insurance coverage, pension scheme, low interest pre-departure loans, low interest housing loan, scholarship for migrant children, and health camp for migrant workers’ families.

C. Worker Migration System

12. Over 90% of the worker recruitment in South Asia is organized by private recruitment agencies. Agencies will inform or advertise job opportunities abroad, collects and interviews potential employees, and assist workers to obtain passport, visa, insurance, and air tickets in exchange for fees paid both by employers and workers. Sometimes, there are middlemen between an employer in a host country and a private recruitment agency in a sending country. In all countries in South Asia, private migration agencies are required to register and be licensed by relevant government authorities. Fees to be provided to the agencies vary depending on destinations of workers. In case of Middle East countries, an average fee to be paid from a worker to a recruitment agency is estimated around $1,400. But in some industrial countries such as Japan, the fee will be higher at around $12,000.

D. Profile of Migrant Workers

13. Most migrant workers from South Asia are unskilled or semi-skilled and come from a poor background. According to a household survey of Bangladeshi migrant workers and their families, one third of the migrant workers have had only a few years of education (up to

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class 5), and 12% are illiterate. About half of them worked as laborers before migration. The majority of the workers (about 70%) are below 30 years old. Migrant worker families remaining in home countries are mostly female household members, and 46% of them are illiterate and have no sources of income other than marginal farming. This high concentration of unskilled or semi-skilled workers among migrant workers from South Asia is seen as a reflection of scarce domestic job opportunities or excess supply for those types of workers.

E. Gender in Worker Migration

14. Worker migration is a male-dominated phenomenon in most of the South Asian countries. In Bangladesh, India, and Nepal, male migrant workers outnumber by a large extent female migrant workers. While in Sri Lanka, women migrant workers were in a majority except in 2008 when male migrant workers outnumbered female workers. Migration of women was prohibited until 2003 in Bangladesh, and migration of women to the Middle East countries was banned until 2007 in Nepal. Overall, women constitute approximately 15% of the total migrant workers from South Asia: 6.5% in Bangladesh; and approximately 10% in India and Nepal. In Sri Lanka, women constituted 52% of the total migration outflow in 2009. The majority of women migrant workers from South Asia are involved in domestic work followed by manufacturing. A small portion of them also work as nurses. Most of them are illiterate or only with the elementary level of education.

15. While the officially recorded number of women migrant workers is far less than that of male migrant workers, the actual number of women migrant workers is estimated to be substantially higher. Although the government of South Asian countries started having policies to proactively support women’s migration, their implementations are lagging behind. Women are still disadvantaged as compared to men in terms of access to resources, information, and legal support for migration. For the majority of women, the cost required for migration is prohibitive and they have limited sources to borrow money. In Nepal, under the Foreign Employment Act 2007, women need to have a written permission of male guardian or husband to migrate. Due to those social or legal restrictions, many women opt to migrate through informal channels and remain undocumented.

16. In 2006, the Government of Bangladesh adopted the overseas employment policy and in Nepal, the government enacted the Foreign Employment Act in 2007. Those policy and legislation are the first policy change that recognizes women’s right to migrate and commit states to facilitate their migration. Based on the policy, the Government of Bangladesh initiated some measures to promote women migration such as training program for women migrant workers.

F. Issues in Worker Migration in South Asia

i. Recruiting Agencies

17. Although the South Asian countries regulate recruitment agencies, their supervision and regulatory enforcement remain weak and many migrant workers have become victims of fraud by recruitment agencies. Especially due to the exponential growth of recruitment agencies during the last two decades, the number of exploitative practices also increased and some recruitment agencies send workers without proper documentations, charging extraordinary high fees, or collecting fees based on false employment advertisements. In other cases, workers were taken to a transit country and requested to wait until the visa from the host country is issued, then the agent disappeared with the money collected from the workers. Workers are also often cheated on the job contracts. After arriving in the host country, workers found that the
jobs given to them are different from what was specified in the contract, or they are paid less than what was promised. Workers seeking employment opportunities abroad are seldom aware of the details of the fee of recruitment agencies and there is little transparent information on how much is the actual costs for sending workers and margin for the agents.

ii. Women Migrant Workers

18. Except for Sri Lanka, the South Asian countries have generally more restrictive policies on women’s migration than that for men. However, due to the limited economic opportunities domestically and high poverty incidence among women, increasing number of women are going abroad to find jobs. This means many women have to apply jobs abroad informally and they face greater vulnerabilities at the time of application as well as during the employment. It is estimated among the undocumented informal migration, the number of women workers are far greater than male workers. Many women are employed as domestic helpers, and due to the closed nature of the work place, those women are more susceptible to sexual harassment or other forms of abuse. Although some South Asian countries signed bilateral agreement protecting domestic workers, these conventions are not effectively implemented. Many women migrants do not have insurance, have limited access to health facilities, and have no guarantees of wages or leave.

iii. Informal Migration

19. In South Asia, proportionally to the growth of registered migrant workers, there was a significant growth of informal undocumented migrant workers. Many workers from South Asia find ways to go abroad through informal (unlicensed) agents, middlemen, friends, or family connections. The exact numbers of such informal migrants are unknown, but the estimates indicate that they are equal to the number of documented migrants (Bangladesh and India) to five times (Nepal). The irregular movement of people is often the result of inadequate or too complex regulatory requirements of migration and restrictions on particular segments of society, particularly women. Those informal migrants face greater vulnerabilities than those migrated through formal channels. Most of the informal migrants are not covered by insurances, have no other protections in case of illness, accidents, or early termination of work contracts. Also without a formal agent that can negotiate with the employer, they tend to be susceptible to underpayment, illegal working environments, or excessive long working hours.

II. REMITTANCE IN SOUTH ASIA

A. Trends

20. Among the regions, South Asia is the second largest remittance recipient in 2009 following the East Asia and Pacific. The formal remittance inflows to South Asia have been increasing from $16.13 billion in 2000 to $72.51 billion in 2010 (Figure 2.1). Among the South Asian countries, India and Bangladesh ranks first and seventh in the world, respectively in terms of volume of remittances they received in 2010. As a share of gross domestic product, Nepal receives the largest formal remittance inflows (23%) among the South Asian countries and ranks fifth in the world, followed by Bangladesh (12%), and Sri Lanka (8.7%). Remittances are also the most important external funding source for the countries in South Asia. In 2009, remittances in South Asia were three times larger than foreign direct investments and more than ten times larger than official development assistance (Table 2.1).
21. In terms of origins of remittances to South Asia, the Middle East countries are the largest recipient of South Asian migrant workers and correspondingly, the amount of remittances originated from the three countries, UAE, Saudi Arabia, and Qatar are estimated to account over 60% of the total remittance inflow to South Asia. India is a significant country both as a remittance sending and receiving country. The total remittances inflow to India amounted $49.5 billion in 2009, while the remittance outflow was $2.8 billion.

22. Due to the global financial crisis in 2008 many migrant worker host countries tightened their labor market to ease domestic unemployment situation. As a result, annual migrant worker outflow from South Asia decreased by 30% in 2009. On remittances, in 2009, South Asian countries, except for India experienced growth, and South Asia overall had the remittance growth of 3% with the total remittance inflow of $66 billion. However, this growth rate is significantly slower than the average growth rate of remittances of 39% from 2000 to 2008. In 2010, remittances to South Asia experienced a 10% growth, and in terms of remittance, it is considered the worst phase of the global crisis is over for South Asia. Migrant worker outflows from South Asia in 2010–2011 shows stronger growth trend as compared to 2008–2009.
Subsequently, remittance inflow to South Asian countries shows growing trends. For example, remittance inflow to Bangladesh in 2010 amounted $11 billion, a 6% growth from the previous financial year and highest remittance inflow in its history. This coincided with the upward economic growth trend of migrant worker host countries such as Saudi Arabia, UAE, and Qatar.

B. Remittance Policies

23. For South Asian countries, remittances play a vital role for their economies. The steady flow of remittances has helped the countries easing the foreign exchange constraints, balance of payments, and increase the supply of national savings. Remittances also contributed to the countries’ development budget. Given the importance of remittances in the country’s economic stability and development, many countries have taken policy measures to maximize benefits of remittances. The key priority for most of the governments is to maximize remittance inflows to contribute to the enhanced government budget and capital availability to finance development projects or to stimulate domestic investments. For this, it requires remittances to be transferred through formal channels. Formal channels include bank drafts, telegraphic and electronic transfers through banks, foreign exchange centers, money transfer companies, or other legal entities that are registered at and supervised by the regulatory authorities, as opposed to informal channels such as hawala brokers, traders, friends, or relatives that do not have legal status or licenses for foreign exchange transactions and are unregulated.

24. One of the characteristics of the remittance economy in South Asia is a high volume of remittances that are transferred through informal channels. As remittance depending economies, the governments of South Asian countries took various measures to improve and smooth formal remittance inflows. Typical measures include exchange rate liberalization, creating a special remittance unit at the central banks, improving licensing to money transfer agencies, and encouraging domestic banks to have partnership with foreign banks in the countries where there are high concentrations of migrant workers. The government also became increasingly proactive to support migrant workers and their families’ investments in small businesses and income generating activities for employment generation.

i. Bangladesh

25. The government recognizes migration and remittances are the important sources for the development and aimed to promote increased flow of remittances through formal channel as one of the poverty reduction strategies in its national strategy.2 The Bangladesh Bank, the central bank, liberalized foreign exchange rates and promoted establishment of branches abroad by Bangladeshi state banks. The Bangladesh Bank further encouraged domestic banks to develop arrangements with exchanges houses and foreign banks.

26. The government developed several instruments to encourage remittances. Bangladesh nationals working abroad can open Non-Resident Foreign Currency (NFCD). NFCD can be opened at any bank operating in Bangladesh and opened for one month, three months, six months or one year term in major foreign currencies. Interest on deposits in these accounts is exempted from taxes under the Income Tax Act. The account holder can freely repatriate the balances and the interest and may convert the balance into taka at the prevailing exchange rate.

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27. The government also issued the US Dollar Premium Bond. The Bond was issued for three years in the name of a holder of a non-resident account against remittances from abroad to the account. The bondholder was entitled to draw interest on half-yearly basis at 7.5% fixed rate per annum. The Bond was issued in the denominations of $500, $1,000, $5,000, and $50,000.

28. Bangladesh nationals working abroad are also entitled to purchase the Wage Earners Development Bond. The maturity of the bond is five years with the annual interest rate of 12%. The premature encashment interest rate varies from 9%–12% depending on the holding period of time. The Bond is issued in denominations of Tk25,000, 50,000 and 100,000.

ii. India

29. Compared with other South Asian countries, the Government of India has had a less proactive approach to promote active remittance market. However, the dramatic rise of the remittance inflows during the last decade induced a series of reforms. The foreign exchange control act was replaced with the more relaxed Foreign Exchange Management Act of 2000. The liberalized foreign exchange controls provided incentives to switch from informal channels such as hawala brokers to the formal remittance channels. Also, the government has promoted the Non-Resident Indian (NRI) deposit accounts, which were established primarily to attract foreign capital to India. NRI depositors are given the choice of holding deposits in foreign currency denominations or in Indian Rupees, and are also exempted from wealth and gift taxes. The reforms on the exchange rate controls during the 1990s reduced the barrier to use NRI deposit accounts as a remittance channel. Combined with the increase in other options for money transfers, the financial liberalization helped promoting the increased remittance inflow through formal channels to India.

iii. Nepal

30. Given the potential huge positive impact of remittances, the Government of Nepal gives high priority in promoting overseas employment and mobilizing remittances as capital for the country’s economic development. Nepal Rastra Bank (NRB), the central bank, started issuing licenses to private sector organizations for remittance-transfer businesses (money transfer companies). NRB has arranged to provide NRs0.15 per US dollar as commission to licensed money transfer companies in addition to the prevailing buying rate. Non-resident Nepalese can also open accounts denominated in Nepalese rupee or foreign currencies, and deposits in non-resident Nepalese accounts can be repatriated to overseas accounts.

31. In addition to those policy measures, the government floated “foreign employment bond” to raise funds for infrastructure development. The original goal was to issue NRs7 billion, but the initial issue in July 2009 was NRs1 billion. Nepali workers in Qatar, Saudi Arabia, UAE, and Malaysia could buy the bond from one of the seven licensed money transfer companies in denominations of NRs5,000. For the initial issue of NRs1 billion, the total NRs4 million was subscribed. The government continued the second issue of the bond in 2010, but the final subscription was amounted only NRs3.38 million. The limited responses were attributed to the insufficient marketing. Not enough publicity was carried out before the issue of the bond. In addition, the bond was marketed to migrant workers to the Middle East and Malaysia, but migrant workers in India were not allowed to buy the bonds. Also, the money transfer companies that sold the bonds received a 0.25% commission on the sale but had to forgo money transfer fees, and this was a disincentive for the companies to sell the bond. Also, the exchange rate was fixed at the time of subscription of the bond.
iv. Sri Lanka

32. The Sri Lankan government introduced incentives to facilitate foreign employment including pre-migration facilities and services, identification of employment opportunities, training, and pre-departure loan schemes and introduced various financial instruments targeted for Sri Lankan migrant workers abroad. Under the Exchange Control Act (2001), foreign exchange transactions are permitted only through licensed commercial banks appointed as full-fledged authorized dealers, but any other person can be appointed by the Central Bank of Sri Lanka as a restricted dealer.

33. The Central Bank of Sri Lanka has permitted non-resident workers to open and maintain non-resident accounts both in rupees and major foreign currencies with authorized dealers. Also, Sri Lankan nationals who are employed abroad can obtain foreign currency loans which are released in rupees but repayable out of their foreign currency earnings for the purpose of construction or purchase of residential houses in Sri Lanka. Loans are made against the pledge of their non-resident foreign currency deposits. Migrant workers abroad are entitled to open Share Investment External Rupee Accounts for the purchase of shares with the authorized dealers, and to purchase dollar denominated Sri Lanka Development Bonds or rupee denominated Treasury Bonds and Treasury Bills. However it is not permitted to utilize funds available in non-resident foreign currency or resident foreign currency accounts or any other foreign currency accounts in Sri Lanka to purchase T-bonds or T-bills.

C. Issues in South Asia Remittances

34. It is widely believed that total remittance inflow to South Asia is far greater than the officially recorded amount due to the high use of informal remittance channels. Because of the anonymous nature of informal remittance transactions, it is difficult to estimate the amount of informal remittances. However, for South Asia overall, an estimated informal remittance inflow could reach to around 42% of the total remittances, with a range of 16% in India and 55% in Nepal.

35. The high degree of informal remittances inflows is one of the key characteristics of the remittance system in South Asia. High dependence of informal remittance channels by South Asian migrant workers is problematic because informal remittances do not create effective linkage to capital enhancement in the formal financial system. For individual households, informal remittances are not effectively linked to financial investment products such as savings. Empirical studies suggest that with increased incomes with remittances but without linkages to formal financial systems, households spend on houses, land, and other consumption items such as household appliances, food and clothes, but have little financial assets such as savings and investments.

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4 In Bangladesh, according to a household survey conducted in 2001, 54% of the total remittances have been channeled through informal means including hundi (40%), friends and relatives (5%), and hand-carry by migrant workers themselves (9%). (T. Siddiqui, and C. R. Abrar. 2003. Social Finance Program Working Paper No. 38. Migrant Worker Remittances and Micro-Finance in Bangladesh. Prepared for the Social Finance Program. International Labour Office.) For Sri Lanka, the estimated informal remittance inflow ranges from 30%–70%. (The estimate by Katarina Harrod, UNDP Regional Centre Colombo [K. Harrod. 2007. Remittance of Sri Lankan Female Migrant Workers–Macro- and Household Level Impacts. Colombo)].

36. The prevalence of informal remittances is closely related to the limited financial system development in South Asia. In general, a repressive and underdeveloped financial system tends to promote informal remittance systems. Specific financial sector policies such as exchange rate control or restrictions on repatriation of foreign currencies particularly induce the higher share of informal remittances. Underdevelopment of financial service networks such as limited bank branch networks in rural areas is also contributing to a greater use of informal channels. It is important for South Asian countries to improve the utilization of remittances by enhancing formal channels of financial transfer of remittances by developing the financial sector, reducing the transaction costs of this process, and improving knowledge and information among migrant worker households. Greater utilization of formal transfers ensures greater receipts of foreign exchange and also inclusion of poor and low income households into the formal financial systems.

III. FORMAL REMITTANCE INFRASTRUCTURE IN SOUTH ASIA

A. General Mechanism of Remittances

37. Remittances can be domestic or international. However, in this report, remittances refer to “cross-border person-to-person payments of relatively low value.” In practice, remittances are fund transfers by migrant workers to family members or other individuals in the country of their origin. There are various ways that remittances are made including mail or telegraphic transfers between banks, electric transfers made by money transfer organizations (MTOs), international money orders through post offices, and informal network of transfers such hawala. This chapter focuses on formal remittances which are made by authorized remittance service providers. Informal remittances are discussed in the next chapter (Chapter IV).

38. For remittances, at least three participants are required to complete a transaction: a sender (a migrant worker), a receiver (a family member or other individual in the country of migrant worker’s origin), and a remittance service provider. Remittance transfer typically involves four phases: capturing, messaging, settlement, and disbursing. The capturing phase is the sender (a migrant worker) pays the capturing agent (a bank, MTO, postal office, etc.) with an instruction to remit fund to the designated receiver. The payments from the sender to the capturing agents can be made not only in cash but also in other forms including debiting the sender’s bank account, use of pre-paid funds like electronic money. In addition to fund, the sender also must provide the information on the receiver to enable the capturing agent to send the money to the receiver (Figure 3.1).

39. In between the capturing and disbursing phases, there are essential steps of messaging and settlement. Messages including the sender and receiver information need to be transmitted from the capturing agent to the disbursing agent to complete the transaction. The settlement phase is the fund transfer arrangements between the capturing and disbursing agents. In cross-border remittance transfer, the settlement process is more complex than domestic money transfer, often involving more than one financial institution. Sometimes, there may also be liquidity arrangements between the capturing agents and disbursing agents to enable the disbursing agent to pay the receiver before the funds from the sender have arrived.

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40. Upon the completion of the messaging and settlement phases, the receiver receives the fund at outlets of remittance service providers such as a bank branch or kiosk of MTO. It is also possible for the receiver to receive the funds in electric money stored in mobile phone or internet. However, the majority of remittances are still cash based.

41. For settlements between the capturing and disbursing agents, there are various instruments depending on the country’s legal and regulatory framework, financial sector infrastructure, and capacity and network of the financial institution. Typical settlement instruments include:

(i) Demand draft or bank draft drawn on a bank.
(ii) Mail transfers sent directly by the remitting bank.
(iii) Travelers’ checks to be encashed in the receiver’s country.
(iv) International money orders issued by banks or post offices.
(v) Telegraphic transfers, transmitted over SWIFT, fax, or email from the remitting bank to the bank in the receiver’s country.
(vi) Electronic transfer made by MTOs for delivery as cash to various destinations, or as credit to the bank accounts of the receiver.
(vii) ATM withdrawal from the sender’s account abroad in the receiver’s country.
(viii) Electric money transfer to the receiver’s account in mobile phone or internet.

42. Bank drafts, telegraphic transfers, and electronic transfer are the most commonly used settlement instruments. Other instruments, in particular, electric money transfers through mobile phone or internet have an advantage in terms of providing accessibility to formal remittance to the people who do not have bank accounts. However, the use of such technology based remittance instruments is still limited and confined mostly in urban areas.
B. Formal Financial Sector Infrastructure for Remittance

i. India

43. In India, the formal remittance infrastructure has significantly developed since the 1990s. Apart from commercial banks, a number of non-bank institutions entered in remittance operations based on the correspondent relationship with international banks and MTOs. In India, entities that are authorized to undertake cross-border remittance transfers are commercial banks, public-owned financial institutions, post offices, and exchange bureaus. The overseas network of the Indian bank branches or offices has also facilitated remittances from the host countries to distant locations in India as the banks have a wide domestic network.

44. MTOs in India are regulated by the Reserve Bank of India under the money transfer service scheme. The scheme requires MTOs to enter into commission-based agent agreements with authorized commercial banks, non-bank finance company, or money exchangers. Remittances through MTOs normally do not require beneficiaries to have accounts at banks or other financial institutions or credit cards. Among MTOs, Western Union, an international MTO, is the most dominant. MTOs are reaching out lower segment of households especially those who do not have access to banks. Despite the extensive network, the postal system in contribution to remittance transfer is limited as compared to banks and MTOs. However, increasingly the postal offices in India are having agent agreements with MTOs and delivering remittances. The Indian Post Office established a partnership with Western Union to enable the post office’s network of 150,000 offices as remittance disbursing agents.

ii. Bangladesh

45. In Bangladesh, commercial banks, MTOs and post offices are the formal remittance channels. Among them, commercial banks are the most preferred options in receiving remittances. State-owned commercial banks have the largest share in terms of branch networks and four state-owned commercial banks have nearly 3,000 branches accounting over 50% branch network of the banking sector. However, despite such extensive network, state-owned banks’ remittance outreach is relatively low as compared to private commercial banks and account 36% of the total remittance inflow. State-owned banks are generally recognized with inefficiency, lack of technology infrastructure, and poor client orientations.

46. On the other hand, local private commercial banks, which account 25% of the whole branch networks, handle 61% of the total remittances coming to Bangladesh. Private banks are actively expanding remittance operations by extending branch networks, establishing correspondent relationship with foreign banks and MTOs, and upgrading technology infrastructure. Such technology infrastructure includes instituting electronic fund transfer mechanisms such as ATMs for domestic branches and internet banking.

47. MTOs, both international and local, are increasingly becoming important channels of remittance transfers in Bangladesh. MTOs can operate alone or under the agent relationship with the authorized dealers—banks and non-bank institutions that are authorized to undertake remittance operations by the Bangladesh Bank. For example, Western Union has an agent agreement with 11 commercial banks in Bangladesh. MTOs usually provide speedier services mainly because of their electronic based messaging and settlement system, but their cost tends to be higher than bank-to-bank remittance services.
48. The post offices in Bangladesh have a long history in remittance mainly by issuing money orders. The Bangladesh Post Office has 1,600 branches all over the country. However, the participation of the post offices for the country’s remittance business is negligible due to their inefficiencies, security concerns, and low technology infrastructure. Recently, the Bangladesh Post Office has signed agreements with several MTOs including Western Union.

iii. Nepal

49. In Nepal, the formal remittance inflow more than tripled during the last decade largely due to the development of MTO networks. Commercial banks, microfinance development banks, finance companies, and MTOs are agents that are allowed to undertake money transfer businesses by the Nepal Rastra Bank (NRB), the central bank. In 2009, there are two state-owned banks, 24 commercial banks, two finance companies, and 45 MTOs that are licensed to conduct money transfer businesses. Among them, state-owned banks have wide branch networks covering all the 75 districts of the country. MTOs can engage sub-agents to receive and disburse funds without permission from NRB. Not only financial institutions, but also other retail outlets such as shops and petrol station can also be sub-agents. As a result, MTOs have expanded rapidly their outreach and are present in all 75 districts.

50. MTOs are the most preferred option in receiving remittances in Nepal. This is attributed not only to the extensive presence of MTOs but also their speedy transaction, reliability, and less documentation requirements as compared to banks. MTOs normally do not require remittance recipients to hold accounts. This no-account requirement is particularly important in terms of facilitating accessibility to formal remittance channel because in Nepal only 30% of the total households have accounts with banks and other financial institutions.

51. Banks undertake basic electronic or bank draft transfers between banks, but also serve as sub-agents of money transfer agents. Banks have also developed partnerships with banks in major migrant worker host countries. For example, Nabil Bank, Himalayan Bank, Nepal Bangladesh Bank, and Nepal Investment Bank have partnered with Doha Bank to offer remittance services to Nepalese workers in Qatar. Still, banks are not large players in the remittance market. And the role of the post office in remittances, despite its large network, is insignificant.

52. It is estimated that the majority of remittances to Nepal is still channeled through informal means. Especially, the bulk of remittances (90%) from India to Nepal are either hand-carried by migrant workers themselves, friends or relatives, or through hawala and hundi. Due to the proximity and visa waiver policies between the two countries make migrant workers more prone to use informal channels. Also, the formal remittances from India to Nepal are restricted and regulated under the Indo-Nepal Remittance Facility Scheme of the Reserve Bank of India, in which remittances are disbursed only through the branches of the State Bank of India and agents of Prabhu Money Transfer in Nepal with the maximum remittance ceiling of Rs50,000.

iv. Sri Lanka

53. Both inward and outward remittances from and to Sri Lanka are presently effected through 22 licensed commercial banks. In addition to the commercial banks, Sri Lanka Post, the National Savings Bank, a specialized bank, and MMBL Money Transfer Ltd. are authorized as restricted dealers. Of these, the National Savings Bank and MMBL are permitted only to engage in inward money transfers.
State-owned commercial banks are the dominant players for remittances in Sri Lanka. Especially, the Bank of Ceylon deals approximately 50% of the total formal remittance inflows largely because of its extensive 618 branch networks spreading over the country. Together with another state-owned bank, People’s Bank, the state-owned banks handle nearly 60% of the total remittance inflows. Banks typically use (i) telegraphic transfers based on SWIFT messages, (ii) drafts/checks drawn on banks, and (iii) international money orders issued by banks and post offices. Recently, a growing number of banks are eyeing on internet and mobile money transfer businesses. Increasingly, private commercial banks also entered the remittances market and started aggressive marketing programs. Some banks offer a variety of products to migrants including insurance and pre-departure loans at concessional rates to be repaid from remittance proceeds.

Like other countries in South Asia, MTOs are increasingly playing the bigger role in remittances in Sri Lanka. In Sri Lanka, MTOs can operate only through banks and other authorized dealers, i.e., Sri Lanka Post, the National Savings Bank, and MMBL Money Transfer Ltd. Unlike in Nepal, exchange bureaus, credit unions, or microfinance institutions are not permitted to be sub-agents of MTOs. The most predominant MTOs in Sri Lanka is Western Union, which has 3,000 sub-agent networks. Although the postal service has a long tradition in providing cross-border remittance instruments, its market share is minimal due to inefficiency and slow service.

C. Issues in Formal Remittance Infrastructure

In South Asia, formal remittance inflows more than tripled during the last decade. This growth can be attributed not only to the growth of the number of migrant workers but also the development of the formal remittance infrastructure including a rapid expansion of MTO networks. However, informal channels still capture a substantial portion of remittances.

Technology innovations in remittance financial products are on the rise in South Asia. However, technology-based remittances products have not yet made substantial penetration in rural markets. Such technology innovations, if appropriately marketed to currently unbanked populations, will greatly enhance the potential of the remittance outreach. Appropriate public and private support may be needed to induce such technology innovations. For bank-to-bank remittances, banks normally use bank drafts or electronic transfer, but increasingly, banks are investing in other payment system technology such as for credit cards, debit cards, and ATMs. Further payment system infrastructure development especially at state-owned banks will reduce costs and improve efficiency in delivering remittances.

Currently, the governments of the South Asian countries do not allow unlicensed semi-formal financial institutions such as microfinance institutions (MFIs) and cooperatives to become agents of the authorized remittance dealers. The use of MFIs and cooperatives as remittance intermediaries is effective especially reaching out the poor and low income populations. In Bangladesh, MFIs serve more than 17% of the total population, or about 35% of the poor population. If this legal constraint is effectively addressed, it could facilitate a significant expansion of formal remittance service outreach.
IV. INFORMAL REMITTANCES IN SOUTH ASIA

A. General Mechanisms

59. Informal remittance systems can trace their origin to the traditional bills of exchange or other payment practices between traders before the modern banking system developed. In the present context, informal remittance systems are used not only among the traders but also various other settlements both for legal and illegal purposes. There are three main ways in informal remittance systems: courier (or hand-carry), in-kind remittances, and hawala.\(^7\) Courier services are the simplest and oldest ways to transfer money. Migrant workers carry cash with them or ask their friends or relative to carry on their behalf. Migrant workers also remit in goods or services (in kind). Migrant workers can buy durable goods such as refrigerators or televisions to carry to their families or sell off to convert into local currencies. Migrant workers can also have deals with local construction companies and build houses in their home countries and pay the contractors’ accounts overseas.

60. Among the informal money transfer systems, hawala is the most sophisticated system. In the hawala system, money is transferred from migrant workers to recipients in migrant workers’ home countries without physical transfer of currencies. Figure 4.1 (upper part) illustrates the basic mechanism of hawala:

   (i) A migrant worker who wants to send money approaches a hawala broker (hawala broker A) and agrees on the amount and types of currency to be sent, the charge for the service, and the amount to be received by the recipient at the other end;

   (ii) A hawala broker (hawala broker A) records this agreement and proceeds to arrange for transfer to take place. The hawala broker (hawala broker A) provides an identification or code to the migrant worker to be passed onto the recipient for the identification with the hawala broker (hawala broker B) in the recipient’s country;

   (iii) The hawala broker (hawala broker A) sends an instruction to the other hawala broker (hawala broker B) in the recipient’s country by fax, e-mail, telephones; and

   (iv) Based on the instruction, the hawala broker (hawala broker B) in the recipient’s country make payments to the designated recipient.

61. At this point, the hawala dealer in the remitting country (hawala broker A) is indebted to the hawala dealer in the recipient’s country (hawala broker B). The settlement between the two hawala dealers can be made in various ways including cash deliveries, checks, and wire transfer to the dealer’s accounts. However, in real practices, the direct settlement between the accounts of hawala dealers are rarely used, rather they use more indirect reverse remittance transactions to settle the balance. Reverse remittance can be a simple remittance order from the recipient’s country (hawala broker B) to the remitting country (hawala broker A). The reverse remittance, however, is rarely symmetrical in terms of volume to the initial remittance, and in real situations, settlement between hawala dealers have great varieties and are more complex, often involving third parties. Unlike remittances from migrant worker receiving countries to migrant worker home countries, reverse remittances are made for various purposes, both legal and illegal. Those include: funds to cover students tuition overseas, fund to cover medical expenses overseas, fund to cover medical expenses overseas,

\(^7\) Many terms are used to refer to informal money transfer in different countries. It is called ‘fei-ch’ien in the People’s Republic of China; hundi in Pakistan and Bangladesh; hawala in India and the Middle East; padala in the Philippines; hui kwan in Hong Kong, China; and phei kwan in Thailand. In this document, hawala is used as it is most commonly used in South Asia.
tourist’s money beyond amounts allowed under currency controls, payment for imports, tax evasion, mis-invoicing of trade, etc.

62. A hypothetical example of a reverse remittance transaction is shown in Figure 4.1 (lower part). In Figure 4.1, a person B approaches hawala broker B to remit money to pay medical expenses of his family member in the country of hawala broker A. Hawala broker B receives cash from person B and in exchange provides a remittance code to person B. Person B informs the remittance code to his family member (Person A) in the country of hawala broker A. Hawala broker B sends a remittance instruction to hawala broker A by fax or e-mail. Based on the remittance instruction, hawala broker A makes payments to person A.

**Figure 4.1: General Informal Remittance Transaction Mechanism**

B. Key Features of Informal Remittances

63. In South Asia, informal remittances are widely used due their distinct features that formal financial institutions cannot offer. In a sense, the hawala system is filling a gap of the formal financial system in particular to meet the poorer segment of the society.
64. **Speed.** In general, *hawala* transfer is speedier than remittance through banks. The development of telecommunication technologies contributed to faster services in the *hawala* system. It is estimated that effecting *hawala* transfers between major international cities takes, on average, 6 to 12 hours. Commonly, 24 hours is required for transfers between countries where the recipient is in a location with a different time zone or where communications are less reliable. Slightly more time may be required for payments in more rural regions or villages where *hawala* broker does not have a local office or representative. A study\(^8\) in Bangladesh found that, on average, a remittance transfer through a bank draft took 13 days, while the one through *hawala* took 3 days.

65. **Cost.** *Hawala* transfer is also cheaper than bank transfer. The direct cost of making funds transfers between major international centers through *hawala* is said to be on average 2\% to 5\%. The final quotation depends on the volume of the transaction, the financial relationship between the remitter and the *hawala* dealer, the currency of exchange, the destination of funds, and the negotiation skills of both parties and their understanding of how the market operates. While the formal remittance market is becoming increasingly competitive and prices are falling, informal remittances are still cheaper alternatives for the majority of migrant workers. *Hawala* brokers have cost advantages due to their low fixed and overhead costs as well as their virtual exemptions from regulatory compliance and taxation.

66. **Accessibility.** Due to language barriers or illiteracy, many migrant workers feel uncomfortable to deal with banks and filling out forms to send money or even opening an account. Many migrant workers migrate informally and do not have documents that are required to open a bank account. Informal remittance systems have an advantage by offering easier access to migrant workers who are unwilling or unable to use formal bank transfer. Cultural considerations, networks, and solidarity among migrant workers’ community also contribute to the development of informal remittance networks. Cultural considerations in the *hawala* system that respect social rules and behaviors including confidentiality and privacy are also an important determinant for family members in the recipient countries to use *hawala*.

67. *Hawala* brokers also operate in the environment where the formal financial system can hardly be functional such as war, civil unrest, and economic crisis. Due to their virtual lack of regulatory oversight, *hawala* brokers can operate almost any regulatory regime or legal environment. In such environment, *hawala* often acts as a parallel financial system to fill the gap of the formal financial system.

68. **Anonymity.** *Hawala* transactions are made almost anonymously. *Hawala* dealers do not request any identification from the remitters and, except for the remittance code, records of the transaction, if any, can be destroyed after the transaction or cannot be accessible by third parties. This lack of transaction records makes virtually impossible any audit or accounting trace of the transactions. This anonymous nature of *hawala* transactions is especially attractive to the migrant workers who migrated informally.

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C. Regulating Informal Remittances

69. While informal remittances provide migrant workers means for innocent needs of remitting money to their family members, largely undocumented anonymous nature of informal remittance makes it susceptible to illegal activities including smuggling, capital control, tax evaluation, money laundering, and other forms of financial abuse. Recently, there has been a growing concern that hawala-type of informal remittance systems can be a financing source for terrorism.

70. Governments of both migrant worker sending and receiving countries initiated various measures to curb informal remittances and promote formal remittances ranging from outright ban on informal remittances to mandatory minimum remittance requirements through banks. Among the migrant worker sending countries, the Government of India under the Foreign Exchange Management Act (FEMA, 2000) explicitly prohibit hawala-type of transactions. The number of authorized institutions that are permitted to deal in foreign exchange has been closely defined and the kinds of transactions (travel, medical treatment, acquisition of foreign assets, etc.) permitted for customers are also set forth in the regulations. The Indian government also promoted formal remittances by increasing the efficiency and cost effectiveness of banking services. The Reserve Bank of India, the central bank, directed massive expansion of bank branches during 1970s and 1980s and allowed non-bank financial companies to undertake Money Transfer Service Schemes to facilitate swift and easy transfer of personal remittances from abroad to India.

71. In most of the migrant worker receiving countries, especially in the Middle East, hawala-type of informal remittances are prohibited. In Saudi Arabia, hawala transactions are illegal under the Banking Control Law. In the UAE, hawala brokers are permitted but have to be registered with the central bank. Also, hawala broker are requested to provide the information on remitters and beneficiaries to the central bank.

72. Those government initiatives to reduce informal remittances have mixed results. While, overall informal remittances are on a downward trend due to improved services and price competitiveness by formal financial institutions, restriction of informal remittances by regulatory measures so far had little to moderate effects. There has also been an argument that prohibiting informal remittances can be counterproductive from an economic development point of view by depriving a convenient access to remittance services from unbanked populations.

73. Undisclosed and implicit nature of informal remittance operations make it extremely difficult for the regulatory authorities to enforce the law. It is easy for hawala dealers, even if one operation was banned and closed, to resume another operation from a different location because most of hawala dealers require only handful equipment, i.e., telephone, fax machine, to start businesses. Further, there is often a complex web of transactions in the settlement of hawala transactions between the originating and recipient countries unlike official bank to bank transactions and such settlements may not be amenable to regulations in all the countries concerned. The legal approach may not even be practical as informal transfers involve cross-border transactions between two jurisdictions and while it may not be illegal in one country, it may be so in another country.

D. Opportunities in Informal Remittances

74. Informal remittance operations are highly elusive, and restricting informal remittances by regulatory enforcement has limitations. There is a fact that informal remittances cater to the
segment of the populations who are unable to or difficult to access to formal banking services. The best approach of facilitating a shift from informal to formal remittances will be a combination of regulatory measures and incentives to use formal remittance services. On regulatory measures, a complete ban of informal remittances is neither feasible nor effective. Rather, for purposes of long-term financial sector development, it is recommended that informal remittance dealers are registered and licensed. Those registration and licensing requirements shall also include requirements for information disclosure of remittance operations to improve the level of transparency of informal remittances.

75. To provide better incentives to migrant workers to use formal remittance services, the formal financial sector first needs to address weaknesses in their services. Formal remittance services, whether it is bank draft or telegraphic transfer, tends to take more time and cost than informal remittances. Also, despite the majority of remittance recipients in South Asia live in rural areas, remittance outlets are limited in rural areas. The best approaches to address those issues are largely classified into three areas: develop payment systems, investment in technologies, and improve financial literacy.

76. **Payment Platform.** To maximize the remittance potential of the formal financial sector, there needs to be a harmonization of the payments infrastructure across banks within a country. Many banks in South Asia do not share a common platform with other banks. As a result, only limited number of ATMs can provide cross-institutions clearing. This is a significant missed opportunities in terms of remittance transactions because in most of the countries in South Asia, state-owned banks have extensive branch networks even in the most remote areas. Electronic instruments offers a superior service, but in order to provide the best value to the use, such remittance instruments require that payments be processed electronically to the disbursing branches and that interbranch and interbank networks be connected electronically.

77. **Technology Investment and Linkage to Non-Bank Financial Institutions.** Many formal remittance service providers, especially MTOs, have been providing faster and cheaper services. Technologies enabled formal remittance services providers to link to their services to various types of agents including, postal offices, exchange houses, shops, gas stations, and MFIs. Investment in technologies such as ATMs, point-of-sales (POS), mobile phone and internet will have a great potential. Such institutions may be able to leverage remittance deliveries, if connected to payment networks. Linkages to MFIs especially have a significant potential as in most of the South Asian countries have dense networks of MFIs including cooperatives.

78. **Financial Literacy and Consumer Protection.** Formal financial institutions in South Asia offer varieties of remittance and investment products for migrant workers and their families. However, those are largely targeting at middle or upper class populations. The finance sector, as a whole, lacks comprehensive efforts to tap into the lower segment of the market. Financial literacy education and remittance information disseminations, for example at pre-departure orientation of migrant workers, are important to expand the formal financial service outreach. It can help migrants to overcome some of the misperceptions and social conditions regarding formal financing institutions. Information about various providers of remittance services and disclosing all costs and benefits associated with their services will encourage migrants to direct remittances to the most efficient providers and as such create incentives for the remittance providers to enhance their services. For migrant workers’ households, information about benefits of holding accounts and using financial products such as loans, deposits, and cashless bill payments could be a first step to access to formal financial systems.
V. REMITTANCE INNOVATIONS

A. Innovations in Technology

79. In South Asia, the majority of households reside in rural areas. For rural people, the use of formal remittance channels is often costlier than for urban populations owning to weak presence of formal financial institutions in rural areas. One of the key constraints in expanding formal remittances services in recipient countries is limited accessibility to formal remittance channels such as bank branches and money transfer agent offices—so called “last mile” issue.

80. In many countries, the last mile issue is tackled with the use of technologies combined with partnerships with non-formal financial institutions (credit unions, MFIs, retail shops, etc.). For example, a bank could receive remittance payments through inter-account transfers, and provide access to rural clients through an arrangement with a post office that has rural branches. Alternatively, an international MTO could link to a national credit union network. The use of technology such as POS and internet is an integral part of these banks and non-bank institution partnership.

81. Under UK Department for International Development funded the Remittances and Payments Challenge Fund, National Credit and Commerce Bank Limited (NCCBL) in Bangladesh teamed up with Thengamara Mohila Sabuj Sangha (TMSS), a microfinance nongovernment organization to extend its remittance service networks to rural areas in 2008. NCCBL is a private bank and has agency networks with a number of foreign banks and exchange companies. This arrangement makes people, who do not have bank accounts, access to formal bank-based remittance services. Under the partnership agreement, NCCBL installed POS in all NCCBL branches and 250 branches of TMSS in mainly rural areas. They provided clients with pre-paid debit cards that will allow card transactions up to the amount of remittances. The debit cards enable clients to withdraw remittances in cash at NCCBL and TMSS branches, and ATMs as and when they require, or use the cards to buy goods and services from merchants that have POS machines.

82. M-PESA in Kenya is one of the pioneers of mobile-phone based financial services. M-PESA is a mobile-phone based service for sending and storing money by Safaricom, Kenya’s largest mobile service provider. Clients can store money in, or send money by their mobile phone by visiting one of more than 10,000 merchants who act as “agents” for account opening, handling of deposits and withdrawals in clients’ virtual “wallet” in mobile phones, and client support. Then, clients can use the application on their mobile phones to check their balance, send money to other people, pay bills, and purchase mobile phone airtime. Since its launch in March 2007, M-PESA has achieved substantial scale along several key metrics. Nearly 7 million clients have registered with the service. An average of 150 million Ksh (approximately $1.96 million) is transferred through M-PESA per day, mostly in small amounts averaging just over 1,500 Ksh (approximately $20) per transaction. So far, the system has handled over 130 million Ksh (approximately $1.7 billion). Initially, M-PESA’s service was limited to domestic remittances; however, since 2011, M-PESA offers international remittances services through agreements with Safaricom and Western Union. M-PESA clients can send money through any of 80,000 Western Union agent locations worldwide to Kenya using M-PESA’s mobile wallet.
B. Innovations in Products

83. The majority of households who depend on informal means of remittances are unable to make use of remittances for productive purposes due to the lack of linkages to formal financial systems. Remittances that are effectively linked to other financial products such as savings, loans, and insurance can help households to stabilize their income streams, reduce their vulnerabilities, and ultimately improve their social and economic welfare. Thus, it is important for formal financial institutions to develop and offer attractive remittance linked financial products that effectively meet the needs of poor and low income households.

84. ACCION International, a microfinance nongovernment organization based in the United States, has seen a potential for offering home-improvement loans to families of migrant workers. ACCION found that many remittance receiving households already use a portion of their remittance incomes to buy construction materials to improve their houses. The existing home-improvement loans were catered for microentrepreneurs and salaried workers and migrant workers' households whose incomes are only remittances were not qualified for such loans. ACCION has worked with Financiera FAMA, an MFI in Nicaragua to offer a home-improvement loan for its remittance recipient clients.

85. In Mexico, CEMEX’s Construmex program enables immigrants to channel remittances to construct houses in their home countries. CEMEX has opened 7 stores in the United States, and families in Mexico can pick up the construction supplies paid by their migrant worker family members in the United States at any of their 4,000 affiliated distributors. The program also offers consulting advice from CEMEX architects who help clients design home plans and calculate how much material to deliver at what time intervals. From 2004–2006, the company offered its services to 4,500 migrant workers in the United States with this product and also with their mortgage financing products. Surveys carried out by CEMEX estimate that $3 billion out of the $16 billion in remittance that were sent in 2006 to Mexico were intended for house construction.

86. In 2006, Dubai-Citibank U.A.E and Citibank India developed the Citibank NRI accounts or Dirham/Rupee checking account (RCA) consisting of two different accounts at Citibank U.A.E and Citibank India, respectively. The Twin UAE-RCA accounts enable clients in Dubai to remit money to their twin account in India. Clients in India can withdraw remittances from the account and at the same time, can apply for personal loans or auto loans and will be able to use the funds remitted as a repayment source.

C. Innovations in Policy, Regulation, and Consumer Protection

87. The recent use of technologies is proven to be effective in expanding outreach of formal financial services and widening the frontier of remittance services. Regulatory policies that will facilitate development of innovative branchless banking solutions while ensuring the safety and security of the financial sector are indispensable for the development of remittance sector. Along with the development of technology based branchless banking services, policy makers and regulators have a common challenge: how to formulate proportionate regulatory policy for innovation and permits branchless banking to scale up safely.

88. Unlike branch-based banking services where a transaction can be concluded only between a financial institution and a client, branchless banking services involve multiple entities with a technology. Typically, branchless banking solutions involve a client, a retail agent, a financial institution, and a technology service provider. The technology devices typically used
are mobile phones, and networks of POS devices that capture client details from plastic cards. Regulatory challenges in branchless banking services are particularly concerned with regulating agents, who are outsourced by regulated financial institutions to directly interact with clients for cash-in, cash-out functions. Another critical consideration in regulating branchless banking is adopting a risk-based approach for combating money laundering and terrorist financing. Protecting consumers in branchless banking is also a concern.

89. In Brazil, the central bank permits a wide range of entities to serve as agents. The central bank of Brazil established the notion of banking correspondents in 1973, permitting banks to engage third parties to collect and process payments. In 1999, the National Monetary Council substantially broadened the scope of activities that could be outsourced to correspondents, including receiving documents for account opening and handling deposits and withdrawals. The Philippines developed a regulatory arrangement that permits agents to conduct CDD (continuous due diligence)/KYC (know-your-customer) norms for clients for branchless banking. It also allows multiplicity of formal identity documents to be presented for verification purposes. Countries took various measures to mitigate the new or enhanced consumer protection challenges of branchless banking. India requires banks working through agents to set up complaint-filing procedures for customers, designate a Grievance Redressal Officer within the bank, and publicize these mechanisms widely through electronic and print media.

VI. THE WAY FORWARD

90. Studies suggest that, in general, remittances positively affect annual GDP per capita of remittance receiving countries.\(^9\) It is also found that remittances decrease the poverty gap and ameliorate the depth of poverty. Remittances also contribute to improvements of welfare of remittance receiving households by smoothing consumptions and increasing spending on food and housing-relating expenditures.\(^10\) Remittances’ contribution to poverty reduction especially at households has an important policy implication especially the most of migrant workers from South Asia are from poor backgrounds. Policy makers, regulators, and private sector in South Asia shall have a concerted effort to promote formal remittances and productive use of remittances. This, for the short-term, will improve financial intermediation and product investments of the economy as well as ease depth of poverty of the country, and for the medium to long term, could develop viable domestic industries that can correct the current situation of high worker out-migration from South Asia.

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\(^9\) C. Vargas-Silva et al. 2009. Remittances in Asia: Implications for the Fight against Poverty and the Pursuit of Economic Growth. *ADB Economics Working Paper Series* No. 182. Manila: Asian Development Bank. The study examined the potential of remittances for promoting economic growth and reducing poverty in Asian countries using data for more than 20 countries in the region for 1988–2007. The study concluded that remittances affect home country real annual GDP per capita growth positively and a 10% increase in remittances as a portion of GDP lead to about a 0.9%–1.2% increase in output growth. The study also stated that “It seems to be safe to conclude that remittances decrease the poverty gap and ameliorate the depth of poverty. In this regard, the estimation suggests that a 10% increase in remittance can decrease the poverty gap in Asian countries by about 0.7%–1.4%.”

91. Governments could maximize the benefits of labor flows by ensuring that the migration channel is kept open, by enhancing the safety and security of transferring funds back to home countries, by strengthening formal transfer systems, and by providing an environment that encourages households to create assets by investing more of the funds that they receive from family members working abroad. Encouraging the use of remittances for investment such as in health and education will create human capital, enhance domestic demand, and boost economic growth in the short and long terms. Policies that encourage remittances for productive use such as small businesses require an improved investment climate that allow markets to work efficiently. Improving legal aspects to lessen the financial cost of international migration and to provide access to potential migrants from the lower income groups can also increase the equity-enhancing effect of remittances. A well-organized financial system would also allow remittance-receiving families to leverage remittances so as to access small loans for investment. On specific measures to improve remittance financial systems, the following can be points for consideration:

92. **Bringing Informal Remittances to “Formal.”** All the South Asian countries ban *hawala*. However, the effectiveness of restricting *hawala* is questionable. Also some financial experts argue that *hawala* type of information remittance system is filling a vacuum of financial services to the unbanked segment of the population and outright ban of informal remittances system is counterproductive from a development point of view. Therefore it is recommended that informal remittance brokers be registered. In these systems, additional efforts should be made to improve the level of transparency by bringing the informal remittance systems closer to the formal financial sector. In this way, the formal and informal financial systems benefit from their mutual deficiencies and each tends to expand when the condition of the other is impaired.

93. **Improving Formal Financial Systems.** Informal remittance systems will prevail as far as formal financial sector does not address its fundamental deficiencies. Those are (i) reaching out to the unbanked populations, and (ii) improving their services competitiveness vis-à-vis informal remittances in terms of price, speed, and customer friendliness. Empirical studies suggest that providing incentives to people to use formal remittance systems is more effective than imposing restrictions on informal remittances. A better incentive for formal remittance system is synonymous to developing formal financial system of the countries and requires various efforts both at macro and micro level.

94. First, the best way to significantly reduce the volume of informal remittance transactions is to liberalize the financial sector. Positive interest rates, a stable and realistic exchange rate, and reliable financial institutions are the fundamentals for the people to remit through formal remittance channels.

95. Second, improving the ability of formal financial institutions to compete with the informal market is a requisite. Efficiency, costs, reliability, outreach, products offered, and convenience are critical factors that migrant workers consider in determining a preferred remittance channels. Strengthening and improving of banks, particularly state-owned banks have a strong implication in formalizing remittances in South Asia. Reforms of state-owned banks to improve their efficiency, client orientation, and product development will improve the formal remittance infrastructure in South Asia.

96. Third, the recent innovations in remittance transactions (origination, system operation and distribution) have found the new market of remittances and expansion of remittance frontier. A common settlement platform such as in the US-Mexico remittance corridor significantly improved seed of transactions by providing a single common platform for settlement and
clearance. Also, mobile, ATM technologies expanded distribution networks in urban as well as rural areas and reach to people who have had limited access to traditional branch-based banking services, streamlining remittance delivery and contributing to lower prices for remitters, and more importantly, reliable delivery of funds to the recipient. Policy makers and regulators should encourage financial institutions’ effort in investing in technology solutions and develop a regulatory environment that will facilitate innovations in the financial sector. Currently, the regulators in South Asia do not allow non-bank based remittance services, which virtually makes M-Pesa type of services impossible to take off. Each country has different regulatory policies and regulators should not compromise safety of the sector and security of customers. However, some regulatory innovations for example in simplified KYC norm for low value transactions, etc., will facilitate technology innovations in remittances.

97. Fourth, MFIs are important links in the chain for formal remittance system to rural areas and the unbanked. Regulators should foster linkages between banks and non-bank institutions including MFIs. MFIs are considered particularly suitable delivery channels to those unbanked in rural areas because MFIs often have extensive member network of poor and low income people. They act as a rural remittance distribution network that brings financial services to communities that have been disconnected from mainstream banking services. A further effort in regulatory innovations in fostering banks and MFIs linkages are recommended.

98. **Consumer Education and Protection.** One of the key factors constraining the expansion of formal financial services to poor and low income populations is their limited financial literacy. Without financial education and outreach, customers of technology-based remittance services are unlikely to take full advantage of benefits that the products offer. Not only for educations on new technology based products, but policy makers and regulators should also pay attention to information disclosure and transparency of remittance services offered by financial institutions including costs and pricing, legal rights of consumers, and complaint mechanism. Regulators should create robust but simple mechanism for consumer protection. Grievance redress across great distances, particularly for less sophisticated customers is a challenge, but it can be mitigated by requiring service providers to offer a simple complaint mechanism.
REFERENCES


Worker Migration and Remittances in South Asia

Every year South Asian countries send out a significant number of migrant workers, resulting in remittances becoming an important source of funds for economic development. However, despite its huge potential to contribute to economic growth, South Asian countries have not yet fully maximized benefits from remittances because of their limited financial sector development and financial inclusion, and because a substantial portion of remittances to the region are channeled informally. Concerted efforts by the governments, regulators, and financial sectors are required in addressing legal and policy constraints, improving formal financial systems, and enhancing customer education to expand formal remittance markets and achieve financial inclusion.

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