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Outlook for Remittance Flows 2011-12

Recovery after the crisis, but risks lie ahead

By Sanket Mohapatra, Dilip Ratha and Ani Silwal¹

- Officially recorded remittance flows to developing countries are estimated to increase by 6 percent to \$325 billion in 2010. This marks a healthy recovery from a 5.5 percent decline registered in 2009. Remittance flows are expected to increase by 6.2 percent in 2011 and 8.1 percent in 2012, to reach \$374 billion by 2012. (Note that the World Bank's definition of developing countries has changed: Poland, which is estimated to have received \$9.1 billion in 2010, is no longer classified as a developing country.)
- This outlook for remittance flows, however, is subject to the risks of a fragile global economic recovery, volatile currency and commodity price movements, and rising anti-immigration sentiment in many destination countries.
- From a medium-term view, three major trends are apparent: (a) a high level of unemployment in the migrant-receiving countries has prompted restrictions on new immigration; (b) the application of mobile phone technology for domestic remittances has failed to spread to cross-border remittances; and (c) developing countries are becoming more aware of the potential for leveraging remittances and diaspora wealth for raising development finance.

Recent trends and outlook for 2011-12

Newly available data show that officially recorded remittance flows to developing countries fell to \$307 billion in 2009, registering a 5.5 percent decline (table 1).² The decline in remittances during the global financial crisis was modest compared to a 40 percent decline in foreign direct investment (FDI) between 2008 and 2009 and a 80 percent decline in private debt and portfolio equity flows from their peak in 2007 (figure 1). Thus, remittance flows became more important as a source of external financing in many developing countries. Recorded remittance flows to developing countries are estimated to have fully recovered to the pre-crisis level of \$325 billion in 2010. In line with the World Bank's outlook for the global economy, remittance flows to developing countries are expected to increase by 6.2 percent in 2011 and 8.1 percent in 2012, to reach \$346 billion in 2011 and \$374 billion in 2012 respectively.³

The resilience of remittances during the global economic crisis of 2008-09, as we have highlighted in previous Briefs, is due to many factors (box 1). Two important points are worth reiterating. While new migration flows fell significantly in many corridors due to the crisis, the net flow of migration remained positive and the stock of existing migrants did not fall,⁴ lending persistence to remittance

¹ We would like to thank Hans Timmer for extensive discussions, Sonia Plaza, Elina Scheja and Emiko Todoroki for useful comments on an earlier draft, and Uranbileg Batjargal for assistance with updating remittances data.

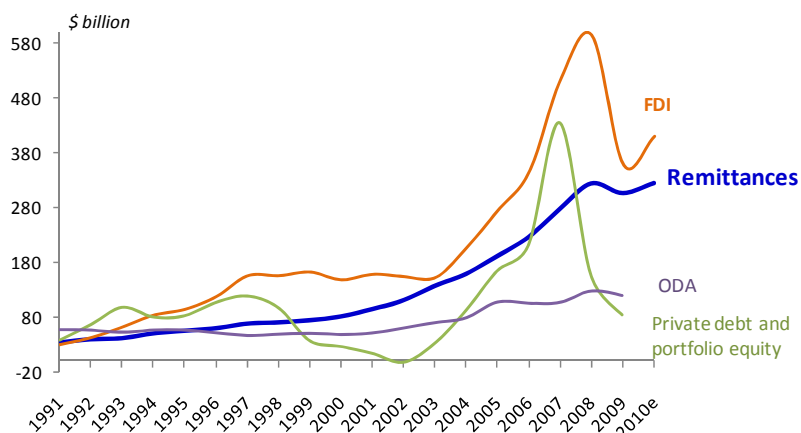
² For comparison with aggregate data published in earlier Briefs, it should be noted that Poland, which is estimated to have received \$9.1 billion in 2010, has been reclassified by the World Bank as a high-income country.

³ The forecasting methodology is based on estimates of bilateral remittances and the World Bank's outlook for the global economy. This is described in "Forecasting migrant remittances during the global financial crisis" by Mohapatra and Ratha, *Migration Letters*, October 2010.

⁴ Migrant stocks in the US have plateaued since 2008 while illegal border crossings along the Mexico-US border are significantly below pre-crisis levels, according to a BBC-MPI report "Migration and Immigrants Two Years after the Financial Collapse"

flows. Existing migrants did not return to extent desired by many countries (e.g., Spain and Japan) despite incentives offered to induce return migration.⁵ Also countries that had migrants in the GCC countries or in other countries less impacted by the crisis did not experience much of a slowdown in remittance flows.

Figure 1: Remittances remained resilient compared to private capital flows during the global economic crisis and have begun to recover in 2010



Source: World Development Indicators (September 2010), Global Economic Monitor, and staff estimates.

Box 1: Resilience of remittance flows relative to other types of flows during the current crisis

There are several reasons for the resilience of remittances in the face of economic downturns in host countries:

- (a) Remittances are sent by the cumulated flows of migrants over the years, not only by the new migrants of the last year or two. This makes remittances persistent over time.
- (b) Tightening of border controls and fear of unemployment back home may encourage the migrant to stay abroad longer (i.e., increase the duration of migration). Those staying back continue to send remittances.
- (c) Since remittances are a small part of a migrant’s income; the migrant can cushion a fall in income by cutting costs (especially housing) and continue to send remittances.
- (d) A returning migrant is likely to take back accumulated savings, which are counted as remittances.
- (e) Fiscal stimulus packages in response to the financial crisis may also provide a cushion to migrant employment and outward remittances.
- (f) At the macroeconomic level, countries with diversified migration destinations are likely to have more resilient remittances.

Source: Migration and Development Brief 9, March 23, 2009.

Papademetriou *et al.* Oct. 2010. As discussed later in the text and in earlier Briefs, migrant deployments from Bangladesh, Nepal, the Philippines and Kerala state in India fell during the crisis, but net emigration appears to have remained positive as there were few returns.

⁵ Anecdotal evidence also suggests that migrant workers moved to different sectors (for example, from construction to restaurants or farms), often in collusion with the employers. The number of colluded to are reported to have gone underground became undocumented workers, but did not return home fearing that they would not be able to travel back when the job markets recover. These undocumented migrants continued to send remittances, often through informal channels.

In the latest estimates for 2010, India, China, Mexico and Philippines retain their position as the top recipients of migrant remittances in US\$ terms. Other large recipients among developing countries include Bangladesh and Nigeria (figure 2).⁶ The top recipients in terms of the share of remittances in GDP in 2009 include smaller economies such as Tajikistan, Tonga, Lesotho, Moldova, and Samoa (figure 3). In these countries remittances exceeded a fifth of the GDP, providing a lifeline to the poor.

Figure 2: Top 10 recipients of migrant remittances

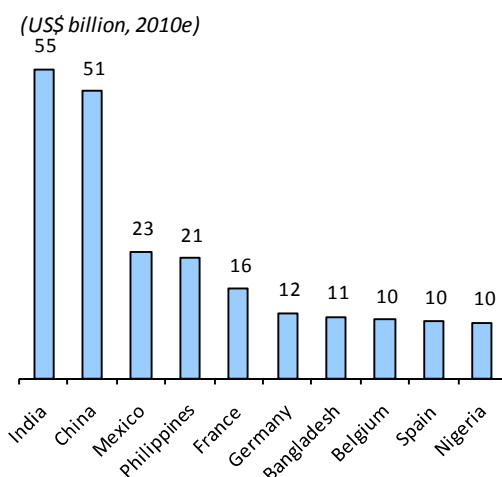
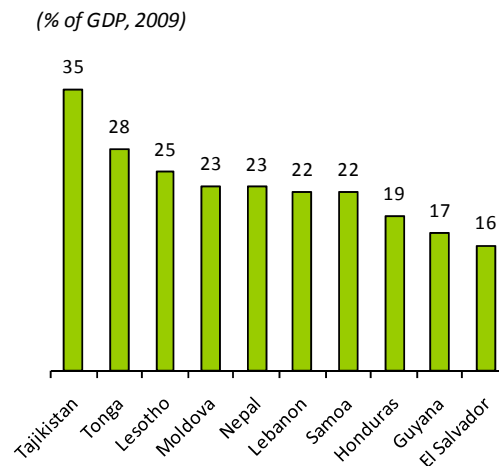


Figure 3: Top 10 recipients of migrant remittances as a share of GDP



Source: Migration and Remittances Factbook 2011.

Regional trends and outlook

Remittance flows to **Latin America and the Caribbean** declined by 12 percent in 2009 due to the financial crisis in the US, but have started recovering, registering a modest 2 percent growth in 2010 (figure 2). Monthly data show that remittance flows to several Latin American countries registered positive growth in the first half of 2010, but the rate of growth appears to be slowing in recent months (figure 4). The recovery in the housing sector in the US, a large employer of Mexican immigrants, in the first half of 2010 was accompanied by growth in remittances to Mexico (figure 5). The national and sector level employment data for the US tell a similar story of a recovery in migrant employment in the first half of 2010, particularly in construction and wholesale and retail trade and construction (figure 6).⁷

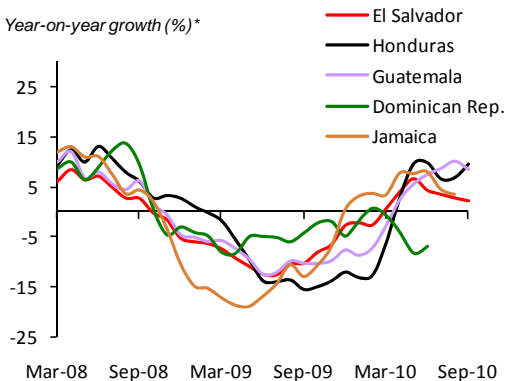
Remittance flows to Latin America and the Caribbean are expected to increase steadily by 7.6 percent in 2011 and 10 percent in 2012 to reach \$69 billion in 2012. However, a recent slowdown in the pace of increase in construction activity in the US suggests some downside risks to the outlook for remittance flows to Mexico. Also a high unemployment rate in Spain will affect remittance flows to Ecuador, Colombia and Bolivia.⁸

⁶ This top recipient list also includes high-income countries such as France, Germany, Belgium, and Spain; however, remittances are a relatively minuscule share of GDP in these countries.

⁷ A recent Pew Hispanic Center study based on analysis of the US Current Population Survey finds that foreign-born workers in the US gained 650,000 jobs in the 12 months since June 2009 ("After the Great Recession: Foreign Born Gain Jobs; Native Born Lose Jobs." Kocchar et al., Pew Hispanic Center, Oct. 2010). Since the start of the crisis in mid-2008, migrants in the US lost more than 700,000 jobs, or over 3 percent of migrant employment, a slightly lower rate than the 5 percent decline in employment of native US workers in the same period.

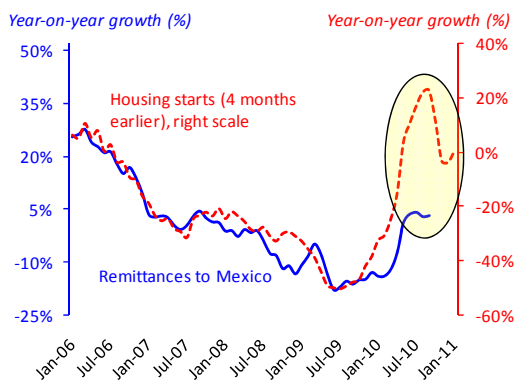
⁸ The unemployment rate in Spain increased to nearly 20 percent in 2010, and is expected to remain above 18 percent during 2011-12, according to the IMF.

Figure 4: Remittance flows to Latin America and Caribbean started recovering in 2010, but growth appears to be slowing



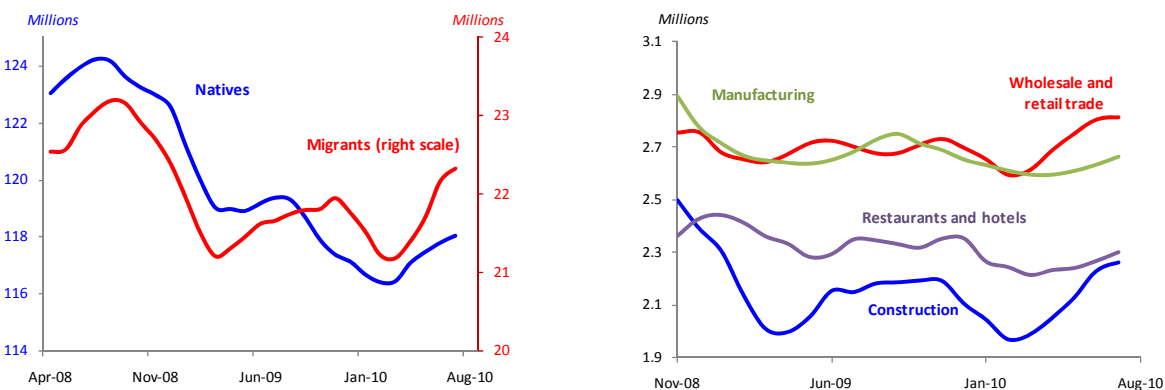
*Year-on-year growth of 3-month moving-averages.
Source: Central banks of the respective countries.

Figure 5: Remittance to Mexico have recovered with new housing construction in the US, but there are risks of a deceleration



Note: New home construction started in the US.⁹
Source: US Census Bureau and Banxico.

Figure 6: Migrant employment in the US is on a recovery path in many sectors



* 3-month moving average
Source: World Bank analysis based on US Current Population Survey

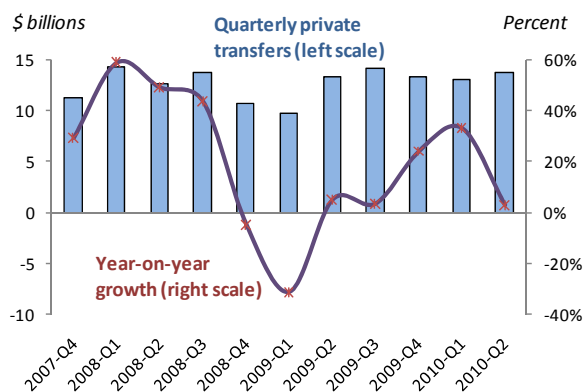
Remittance flows to South Asia, and to some extent East Asia, held up and grew robustly in 2010 because of the sectoral and geographical diversification of their migrants and in part because migrant-destinations in the Gulf were relatively less affected by the global economic crisis. Remittance flows to **South Asia** are estimated to have grown by 10.3 percent in 2010, and are expected to grow at relatively slower rates of 5.1 percent and 6.3 percent in 2011 and 2012 respectively. Flows to South Asia are facing the risk of a lagged effect of the slowdown in construction in the GCC countries. More recently in 2010, the appreciation of local currencies of remittance-receiving countries against the US dollar (and GCC currencies tied to the US dollar) may have reduced the incentive to send remittances for investment motives.

Remittance flows to India, the largest recipient in the South Asia region, grew robustly in the last quarter of 2009 and the first quarter of 2010, but flows appear to have leveled off in the second quarter of 2010 (figure 7). Migrant worker deployment from Bangladesh has been falling steadily since the onset

⁹ The remittance series for Mexico has been adjusted to smooth out a sharp 36% decline in October 2009 caused by a large increase in remittances in the same month the previous year because of the depreciation of the Mexican Peso (see <http://blogs.worldbank.org/peoplemove/fall-in-remittances-to-mexico-in-october-a-data-quirk>).

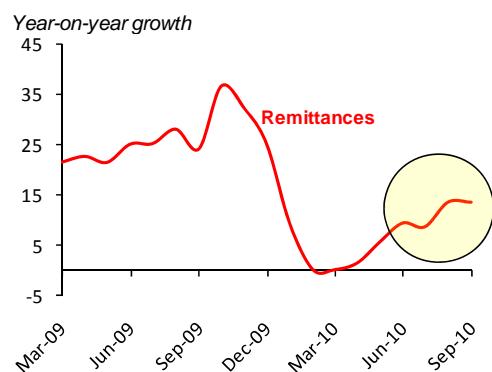
of the global crisis in September 2008 and has leveled off in recent months (figure 8). The growth of remittances to Bangladesh has also slowed considerably. By contrast, remittance flows to Pakistan surged following the floods in June-July 2010 as migrants responded to calls for help from their families and friends (figure 9).

Figure 7: Remittances to India recover to pre-crisis levels but slow down in second quarter



Source: Reserve Bank of India.

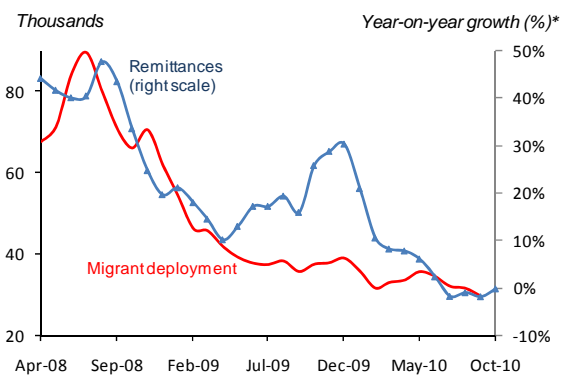
Figure 9: Remittances to Pakistan increase after June-July floods



*Growth of 3-month moving average

Source: State Bank of Pakistan

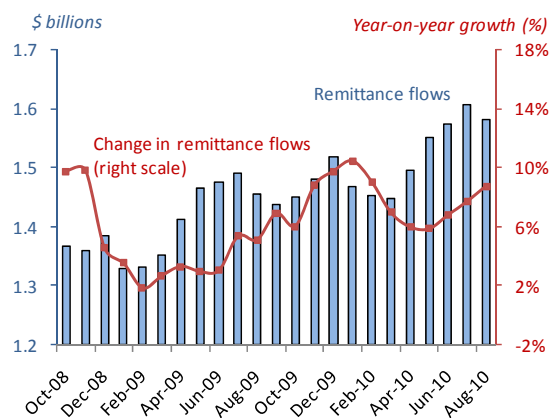
Figure 8: Migrant deployments from Bangladesh are falling and the growth of remittances slowing



*Growth of 3-month moving average

Source: Bangladesh Bank and Bangladesh Bureau of Manpower, Employment and Training.

Figure 10: Steady growth of remittances in the Philippines during the crisis



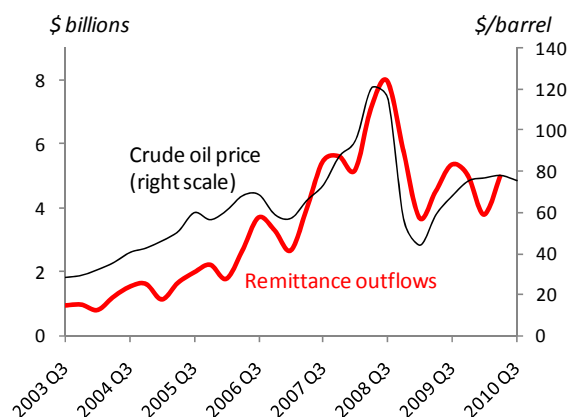
*Growth of 3-month moving average

Source: Bangko Sentral Ng Pilipinas

Remittance flows to **East Asia and the Pacific**, are estimated to have grown by 6.4 percent in 2010 to reach \$91 billion in 2010. Remittance flows to China, the largest recipient in the region, are estimated to have grown by 4.7 percent to reach \$51 billion in 2010, and flows to Philippines, the second largest recipient, by 7.8 percent to reach \$21.3 billion in 2010. As discussed above, the diversified destinations of Filipino (and Chinese) migrants contributed to steady growth in remittances in 2010 despite the crisis (figure 10). Similarly, flows to Vietnam are estimated to have grown by 9 percent in 2010 to return to the pre-crisis level of \$7.2 billion in 2010. With a recovery in global demand, remittance flows to the East Asia and Pacific region are expected to grow at 7.2 percent and 8.5 percent in 2011 and 2012 respectively, to reach \$106 billion in 2012.

Remittance flows to the **Europe and Central Asia** region registered a sharp 23 percent decline in 2009, but have since recovered to positive growth of 3.7 percent in 2010 to reach \$37 billion in 2010. Remittance flows to Central Asian countries such as Tajikistan, Kyrgyz Republic and Moldova declined by almost a third in US dollar terms in 2009 because of the collapse of oil prices and deep recession in the Russian Federation. (Also a sharp depreciation of the Ruble relative to the US dollar produced a valuation effect that reduced remittances in dollar terms, see Migration and Development Briefs 11 and 12). While some Central Asian migrants returned back to their countries of origin during the crisis, the recovery in oil prices and resumption of economic growth in Russia (figure 11) has encouraged new inflows of migrants.¹⁰

Figure 11: Remittance outflows from Russia have started growing with oil prices and economic recovery



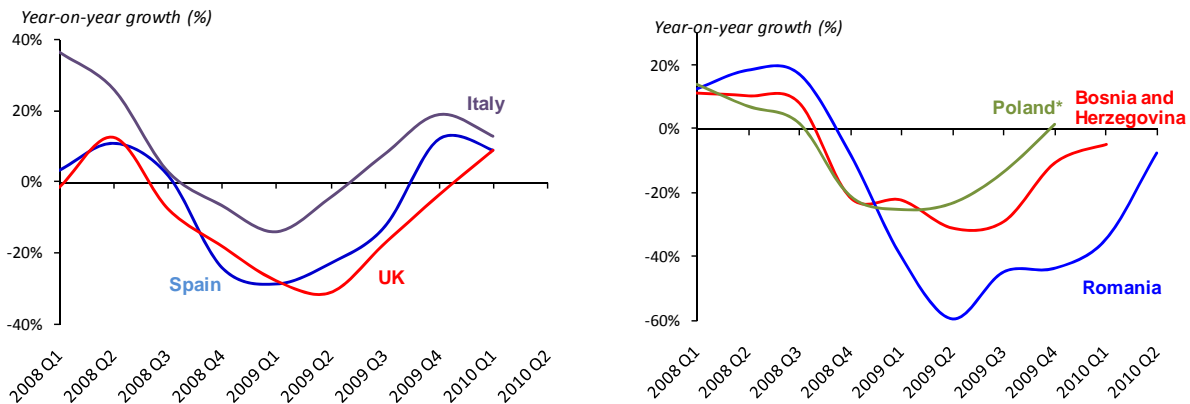
Source: IMF Quarterly Balance of Payments statistics, IMF World Economic Outlook October 2010.

The Eurostat reports that intra-EU remittances fell by 13 percent in 2008-09, while flows to outside the EU fell by 4 percent.¹¹ Remittance flows to Romania declined by more than 50 percent in 2009 (figure 12). Romanian migrants in Spain and Italy (numbering more 800,000 immigrants in each country) have been affected by the crisis in these countries. (Flows to Poland, now a high-income country, fell by a third.) As discussed in our previous Brief, freer labor mobility within the EU has made intra-EU remittance flows more pro-cyclical to the crisis in the destination countries, an interesting contrast to the flows within the Americas. Despite relatively high overall unemployment rates, the UK has seen some incipient signs of recovery in migrant employment, particularly those from Eastern European countries that joined the European Union in 2004 in the first half of 2010 (figure 13). Remittance flows to the Europe and Central Asia region are expected to recover by 6.5 percent in 2011 and by 10.4 percent in 2012, to reach \$43 billion in 2012.

¹⁰ Surveys by Gallup suggest that the number of temporary workers abroad from Tajikistan (mainly to Russia) declined from over 600,000 in 2008 to about 350,000 in 2009, but have gone back up to pre-crisis levels in 2010.

¹¹ "Remittances from the EU down for the first time in 2009, flows to non-EU countries more resilient." Eurostat report, July 2010.

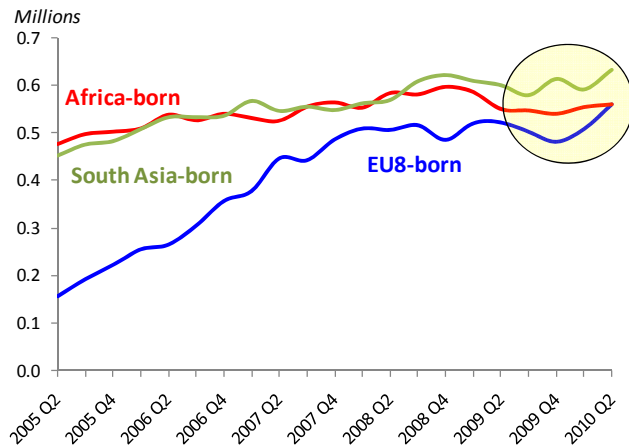
Figure 12: Remittance outflows from UK, Spain, and Italy have started recovering – and pace of decline in inflows to Poland, Romania and Bosnia-Herzegovina slowed – in 2010



* Poland is now a high-income country and not included in estimates of remittances received by developing countries. It is shown in the chart for illustrative purposes since it was a developing country until 2009.

Source: IMF Quarterly Balance of Payments statistics and World Bank staff estimates

Figure 13: Migrant employment in the UK slowed during the crisis but appears to have picked up



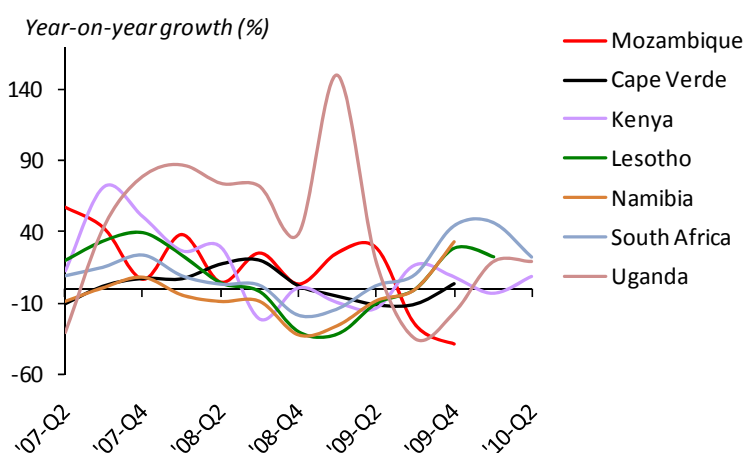
Note: EU8 in the chart above includes the EU “accession” countries Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovak Republic, and Slovenia. South Asia includes only Bangladesh, India, and Pakistan.

Source: UK Office of National Statistics.

Remittance flows to the **Middle East and North Africa** region are estimated to have grown by 5.3 percent to \$35 billion in 2010. While remittance flows to the region were affected by the continuing crisis in Europe, anecdotal evidence suggests that the destinations of migrants (especially high skilled migrants) from the region appears to be shifting towards the GCC countries that have remained resilient during the global crisis. Egypt has seen a surge in remittance flows in recent months, with inflows increasing from \$3.6 billion in the second half of 2009 to \$6.2 billion in the first half of 2010. After positive growth for a consecutive eight months, remittance flows to Morocco registered negative growth in July and August on a year on year basis. Despite this slowdown, remittance inflows to Morocco were 8 percent higher during the first 8 months of 2010 compared to the same period in 2009. Remittance flows to the Middle East and North Africa region are expected to grow by 4.5 percent in 2011 and by 6.7 percent in 2012, to reach \$40 billion in 2012.

According to available data, remittance flows to **Sub-Saharan Africa** are estimated to have remained nearly flat during the crisis and registered a modest 4 percent gain in 2010 to reach \$21.5 billion. Flows to Sub-Saharan Africa are expected to grow by 4.5 percent and 6.7 percent in 2011 and 2012 respectively, to reach \$24 billion in 2012. Unfortunately, however, the lack of reliable and timely data for most African countries makes it difficult to judge the actual extent of the flows, let alone the recovery. The remittance inflows data reported by the country authorities themselves are often higher than that reported in the IMF Balance of Payments statistics – for example, Ghana’s central bank reported \$1.6 billion in remittance inflows in 2008 compared to \$126 million in the IMF balance of payments statistics, and Ethiopia’s central bank reported more than \$700 million instead of \$387 million.¹² These discrepancies are partly related to the confusion of migrant remittances with other types of current transfers, such as small-value trade transactions, and also because a large part of remittances in Sub-Saharan Africa flows through informal channels.¹³ Only about half of Sub-Saharan African countries report annual remittance data with any regularity¹⁴, and some large countries, such as Central African Republic, Democratic Republic of Congo, Somalia and Zimbabwe, all of which are believed to receive significant amount of remittance flows, report no remittance data at all. Even fewer Sub-Saharan African countries report high-frequency monthly or quarterly data on remittances, and whatever high-frequency data is reported is subject to wide variation, raising questions about their reliability (figure 14).

Figure 14: High frequency data reported by Sub-Saharan African countries tend be highly volatile, reflecting issues with data collection



Source: IMF Quarterly Balance of Payments statistics and World Bank staff estimates

Risks to the outlook

There are three key sources of risks to the outlook outlined above for remittance flows to developing countries:

First, the economic recovery in the major destination countries in North America and Europe is not very firm yet. There is a risk that the fiscal retrenchment being planned or implemented in some of

¹² A recent survey by the World Bank’s Future of African Remittances (FARS) program suggests that annual remittance flows to Ethiopia could be as high as \$3 billion.

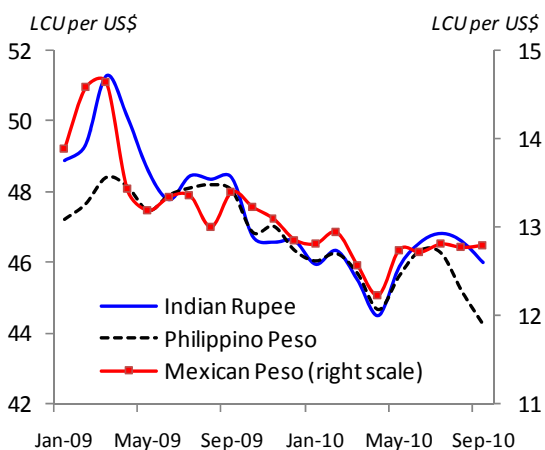
¹³ “Sending Money Home to Africa” IFAD report, October 2009.

¹⁴ “Migrant remittance flows: Findings from a Global Survey of Central Banks” By Irving, Ratha and Mohapatra, World Bank Working Paper 194, April 2010.

the major destination countries might restrain aggregate demand and economic growth, and contribute to high unemployment rates, which in turn could reduce the migrants' incomes and remittances.

Second, movements in currency exchange rates and commodity prices can pose unpredictable risks for remittance flows. While a weaker US dollar can imply larger dollar-denominated remittances from Europe, it can also increase dollar prices of assets and goods in remittance-receiving countries (such as India, Mexico and the Philippines, figure 15). Volatile oil prices also imply risks for outward remittance flows from the Russian Federation (and to a lesser extent, the GCC countries).

Figure 15: Exchange rate of major remittance-recipient currencies against the US Dollar



Source: Development Prospects Group, World Bank

Finally, there is a risk that immigration controls imposed in response to high domestic unemployment rates will deepen and adversely affect migration and remittance flows. Anti-immigration sentiment is on the rise across the world (box 2). In general, protectionist policies that slow the movement of goods and people across borders are likely to delay an adjustment to the crisis and prolong the process of recovery. In the near term, anti-immigration policies favoring native workers over migrant workers are neither helpful for businesses facing declining revenues and cost-cutting pressures, nor for the economies in need of labor market flexibility. Such policies are also inconsistent with the sharp increase in demand for migrants projected in the rapidly aging societies of the North.

Box 2: Rising anti-immigration sentiment

Despite a return to positive global economic growth in 2010, persistently high overall unemployment rates, large fiscal adjustments, and public and private sector job losses in migrant destination countries are contributing to rising anti-immigration sentiment and more restrictive immigration policies. The UK has implemented measures to sharply restrict the number of immigrants from non-EU countries to 24,100 annually immediately following elections in which immigration was a major issue. The US has also seen an increase in anti-immigration sentiment and shifts in policies. Arizona state in the US has implemented a law that allows police to demand proof of legal status during routine checks. Some migrants have responded to this crackdown by moving to neighboring states or back to Mexico. South Carolina, Pennsylvania, Minnesota and Rhode Island have also introduced similar bills seeking to reduce illegal immigration. Australia has also introduced changes to its migration regulations in July 2010 aimed at reducing intake of migrants by shortening the list of occupations under its skill migration program from 398 to 181.

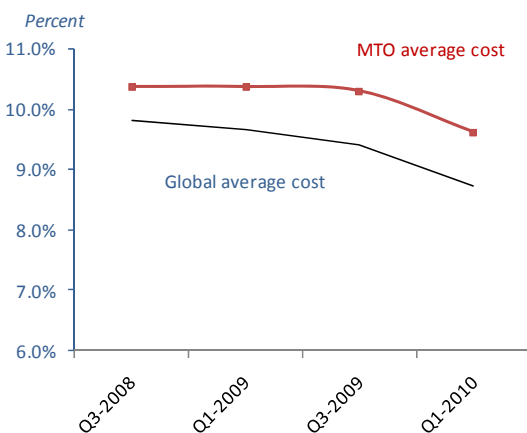
Many destinations of migrants have seen increasingly hostile and anti-immigration sentiments that are coinciding with high unemployment rates and sluggish economic recovery. Parties calling for stricter restrictions on immigration or ethnic groups have either received higher votes or are getting a bigger following in countries such as Netherlands, Austria, Bulgaria, Denmark, France, Germany, Hungary, Italy, Norway, Sweden, and Switzerland. Increasing negative attitudes towards immigrants are being observed in many European countries. One survey on Germany found that a third of Germans want foreigners to be repatriated. Nearly 60 percent of Finns now feel that Finland should not increase the number of migrants; only 35 percent felt so three years ago.

Structural and regulatory trends in remittance markets

The global remittance market is undergoing a major structural change with the increasing popularity of mobile phone-based (and internet-based) remittances. There have also been significant changes in the regulatory environment for remittances in the United States and Europe that are aimed at increased competition, transparency, and consumer protection in remittance markets.

Increasing competition and structural and regulatory changes have gradually put downward pressure on remittance costs. According to the World Bank Remittance Prices Worldwide database, the average remittance cost for sending \$200 fell from 9.8 percent in the last quarter of 2008 to 8.7 percent in the first quarter of 2010 (figure 16). Remittance cost in the US-Mexico remittance corridor fell between 1999 and 2005, from nearly 10 percent of the transaction amount in 1999 to less than 5 percent in 2005 because of greater competition (World Bank 2006). However, average costs in other corridors – particularly in Sub-Saharan Africa and the Pacific Islands, and in almost all South-South remittance corridors – have continued to remain high.

Figure 16: Global average remittance costs have been falling since third quarter of 2008



Note: Average cost for sending \$200. MTO average indicates average cost for sending remittances through money transfer operators (MTOs)

Source: Remittance Prices Worldwide database; “An Analysis of Trends in the Average Total Cost of Migrant Remittance Services” Policy Note, Payments Systems Development Group, Financial and Private Sector Development Vice-Presidency, World Bank, April 23, 2010.

US Wall Street reforms and EU Payment Services Directive will help increase transparency and competition in remittance markets

The Wall Street Reform and Consumer Protection Act signed into law by President Obama on July 21, 2010 also aims to increase transparency in the pricing of remittance services. Providers of remittance

services (RSPs) in the United States will be required to disclose to remitters the equivalent amount that will be received in local currency by the beneficiary, the fees for the transaction, access to error-resolution mechanisms, and contact details of the relevant regulatory authority. Remittance issues are going to be integrated into the strategy for financial literacy for low-income communities, as part of the US government's Strategy for Assuring Financial Empowerment (SAFE). Finally, the Federal Reserve and Treasury will work to extend automatic clearing house (ACH) systems and other payment systems for remittances to foreign countries, with a focus on countries that receive significant remittance transfers from the United States. Studies will be conducted on the feasibility of using remittance history to improve credit scores and the legal and business model barriers to such credit scoring.

However, the United States subsequently announced plans to implement regulations that will severely reduce or eliminate threshold requirements for reporting cross-border money transfers. Under the proposed requirements, banks will have to report all cross-border money transfers, and money transfer operators will have to report only transactions greater than \$1,000. There is lack of clarity about whether these thresholds are consistent with those recommended by the inter-governmental Financial Action Task Force (FATF) for customer due diligence (CDD). The FATF thresholds are themselves subject to interpretation. In practice, many countries require remittance service providers to undertake CDD for transaction below 1,000 US dollars or euros. In some cases, the CDD requirement applies to all remittance transactions. This could be for example if regulators believe that remittance transfers are highly vulnerable to money laundering or terrorist financing. While the majority of migrant remittance transactions are below \$1,000, a lack of clarity on these regulations has increased the cost of compliance for community banks and smaller money transfer operators.

Concurrently, the European Payments Services Directive (PSD) implemented in the European Union will have implications for transparency and improved consumer protection for remittance services. For example, a new type of institution called a Payment Institution (PI) has been created that is subject to less stringent licensing, capital, and reporting requirement compared to conventional banks and financial institutions (Previously money transfer operators had to register as financial institutions in some EU countries). In addition, in the UK remittance transactions will come under the independent Financial Ombudsman service for the first time.¹⁵ Although the PSD applies only for transactions from one EU country to another, some remittance-sending countries such as Italy have extended these rules for transfer to third-countries outside the EU.

Mobile money transfer services are slow to cross borders

Mobile money transfers have the potential to revolutionize access to remittance services and broader financial services for the poor. There is a compelling reason for applying mobile technology to cross-border remittance services: the bulk of poor cross-border migrants tend to travel short distances, mostly to neighboring countries just across the border,¹⁶ and a large number of them stay within the calling range of domestic mobile phones. Such migrants typically cannot have bank accounts in the host country, and in any case banks do not want to serve them. These migrants rely on friends (or strangers) going home or hawaladars to send money home.

M-Pesa in Kenya has done well by capitalizing on the technique of transferring mobile phone minutes and now has more than 10 million clients, each transacting small amounts. Similar mobile money transfer services are fast expanding to other countries and regions. In India, Bharti Airtel (which recently acquired the Kuwait-based mobile phone operator Zain which offers Zain-Zap mobile money

¹⁵ Report prepared for the World Bank by Leon Isaacs in "Remittance Markets in Africa" (forthcoming).

¹⁶ 80 percent of South-South migration is between countries with contiguous borders (Ratha and Shaw 2007)

transfer service in several West African and East African countries) has received approval for mobile money transfers. Several Indian banks have tied up to facilitate mobile money transfers.

There are some small pilots for cross-border remittances (e.g. from the UK and US to Safaricom's M-Pesa mobile money accounts in Kenya), but by and large the mobile phone remittances have stayed within national borders. Conversations with market players suggest that a lack of clarity on anti-money-laundering and combating the financing of terror (AML-CFT) regulations remains a major barrier to the entry of cross-border remittance service providers. Also it has become urgent now to address whether these new technologies should be regulated under Banking regulations or telecom regulations, and how the operational risks that might arise can be addressed. For example, while Kenya's M-Pesa owned by a telecom operator Safaricom was allowed to operate with very little regulatory oversight or reporting requirements in its initial years which allowed it to scale up rapidly, such regulatory "forbearance" can expose the financial system to systemic risk if the volume of transactions flowing through the mobile money transfer system is large and if the deposits are stored in one or two financial institutions.¹⁷

Innovative financing mechanisms leveraging on migration and remittances

With traditional financing sources drying up during the crisis, the resilience of remittances has highlighted the role of the diaspora as a potential source of external financing. Investors and credit rating agencies are paying attention to remittances in the analysis of sovereign creditworthiness in middle income countries and debt sustainability in low income countries. Also many countries are considering the issuance of diaspora bonds and securitization of future remittances.

Diaspora bonds¹⁸

On September 16 Greece announced that it plans to issue a diaspora bond. In the past the governments of India and Israel have raised over \$35 billion dollars, often in times of liquidity crisis. Preliminary estimates suggest that Sub-Saharan African countries can potentially raise \$5-10 billion per year by issuing diaspora bonds. Countries that can potentially consider diaspora bonds are Bangladesh, Colombia, El Salvador, Ghana, India, Jamaica, Kenya, Mexico, Morocco, Nepal, Nigeria, Pakistan, Philippines, Romania, Senegal, South Africa, Sri Lanka, Uganda, Zambia, and Zimbabwe (and also Greece, Ireland, Italy, South Korea and Spain).

Diaspora bonds have several advantages, both for the issuer and for the emigrant who buys the bond: Through retailing at small denominations, ranging from \$100-\$10,000, issuers can tap into the wealth of relatively poor migrants, although diaspora bonds are not necessarily limited to migrants. Diaspora bonds open new marketing channels such as churches, community groups, ethnic newspapers, stores, and home town associations in countries and cities where diaspora members reside in large numbers. A confident issuer could issue in local currency terms as migrants may have local currency liabilities in the issuing country and hence less aversion to devaluation risk. Migrants likely have better knowledge of their origin country's creditworthiness and likely have more legal recourse in the event of a default. Migrants are expected to be more loyal than the average investors in times of distress. And they might be especially interested in financing infrastructure, housing, health and education projects. A diaspora bond would offer a higher interest rate than the rate a diaspora saver earns from bank deposits in her country of residence, even as the diaspora investor demands a lower yield for these bonds compared to an international investor. Tax breaks and credit enhancement (first-loss guarantee, relatively senior creditor status) can enhance the attractiveness of these instruments for diaspora

¹⁷ "Regulating Transformational Branchless Banking: Mobile Phones and Other Technology to Increase Access to Finance." CGAP Focus Note 43, January 2008.

¹⁸ Dilip Ratha "Diaspora bonds for development financing during a crisis" October 26, 2010, Peoplemove blog.

members. Investment bankers may be needed to structure these bonds and ensure compliance with SEC regulations in the US and other jurisdictions. However, nothing can prevent an issuer from marketing these bonds under its national regulations and these bonds can be marketed (for a commission) through commercial banks with a global presence.

There are several factors that need to be fulfilled for the issuance of diaspora bonds which might explain why the actual issuance of diaspora bonds remains meager to date. First, there is limited awareness about this financing vehicle and governments and other entities are often deterred by the complexities of bond instruments, whether to register them with regulatory agencies such as the US SEC, and whether or not such instruments need to be rated by rating agencies. Market players and regulators in the developed destination countries are also unfamiliar with these bonds. Second, many countries still have little knowledge of where their diaspora are located or the resources of their respective diaspora, how much their diaspora earn, save and invest. Diaspora investors must have confidence in the government of their home country if they are to purchase bonds issued by their countries of origin. Also countries with political insecurity and weak institutional capacity would find it hard to market diaspora bonds unless credit enhancements are provided by more creditworthy institutions.

Securitization of future remittance flows

In June 2010, the International Finance Corporation provided up to \$30 million financing for Fedecredito, a credit cooperative in El Salvador, to raise funding via securitization of remittances of El Salvadorans working abroad (to increase lending to underserved micro entrepreneurs and low-income households in the country).¹⁹ In September, the United States signed Memorandums of Understanding with El Salvador and Honduras to assist them through the Building Remittance Investment for Development, Growth, and Entrepreneurship (BRIDGE) initiative in securitizing their future remittance receipts to raise lower-cost and longer-term financing for infrastructure, public works, and commercial development initiatives. The financing structure used for the Fedecredito remittance securitization and the BRIDGE initiative is similar to the future-flow securitization used by banks in several remittance-receiving countries such as Brazil, Jamaica, Kazakhstan, Mexico, Peru and Turkey to raise over \$15 billion in international financing during the last decade, with the average maturity of the loans ranging from 5 to 15 years (Ketkar and Ratha 2009).²⁰ Such a financing structure mitigates several elements of sovereign risk and thereby facilitates developing countries' access to international capital markets at substantially lower cost and for longer maturities. For example, the potential for raising additional financing for Sub-Saharan Africa through securitization of remittances and other future receivables is estimated at \$15 billion annually.²¹

¹⁹Fedecredito is a cooperative owned by 55 El Salvadoran credit unions and workers banks that mobilize savings deposits from 600,000 low-income member owners, who represent close to one-quarter of El Salvador's workforce (<http://www.ifc.org>)

²⁰See Dilip Ratha and Suhas Ketkar "New Paths to Funding" *Finance and Development*, June 2009

²¹Ratha, Mohapatra and Plaza (2009) in *Innovative Financing for Development*, Dilip Ratha and Suhas Ketka (eds.)

Table 1: Outlook for remittance flows to developing countries, 2011-12

| | 2007 | 2008 | 2009 | 2010e | 2011f | 2012f |
|-------------------------------|--------------|--------------|--------------|-------------|-------------|-------------|
| <i>\$ billion</i> | | | | | | |
| Developing countries | 278 | 325 | 307 | 325 | 346 | 374 |
| East Asia and Pacific | 71 | 85 | 86 | 91 | 98 | 106 |
| Europe and Central Asia | 39 | 46 | 35 | 37 | 39 | 43 |
| Latin America and Caribbean | 63 | 65 | 57 | 58 | 62 | 69 |
| Middle-East and North Africa | 32 | 36 | 34 | 35 | 37 | 40 |
| South Asia | 54 | 72 | 75 | 83 | 87 | 92 |
| Sub-Saharan Africa | 19 | 21 | 21 | 21 | 22 | 24 |
| Low-income countries | 17 | 22 | 22 | 24 | 26 | 29 |
| Middle-income countries | 262 | 303 | 285 | 301 | 319 | 345 |
| <i>World</i> | <i>385</i> | <i>443</i> | <i>416</i> | <i>440</i> | <i>464</i> | <i>499</i> |
| <i>Growth rate (%)</i> | | | | | | |
| Developing countries | 22.8% | 16.7% | -5.5% | 6.0% | 6.2% | 8.1% |
| East Asia and Pacific | 23.7% | 20.2% | 0.3% | 6.4% | 7.2% | 8.5% |
| Europe and Central Asia | 38.5% | 16.5% | -22.7% | 3.7% | 6.5% | 10.4% |
| Latin America and Caribbean | 6.9% | 2.2% | -12.0% | 2.0% | 7.6% | 10.0% |
| Middle-East and North Africa | 21.5% | 11.8% | -6.3% | 5.3% | 4.5% | 6.7% |
| South Asia | 27.1% | 32.5% | 4.5% | 10.3% | 5.1% | 6.3% |
| Sub-Saharan Africa | 46.7% | 14.9% | -3.7% | 4.4% | 4.5% | 6.7% |
| Low-income countries | 27.6% | 32.5% | 2.4% | 8.2% | 8.7% | 9.0% |
| Middle-income countries | 22.5% | 15.7% | -6.0% | 5.8% | 6.0% | 8.0% |
| <i>World</i> | <i>21.1%</i> | <i>15.1%</i> | <i>-6.1%</i> | <i>5.8%</i> | <i>5.4%</i> | <i>7.5%</i> |

e= estimate; f=forecast

Source: : Authors' calculation based on data from IMF Balance of Payments Statistics Yearbook 2009 and data releases from central banks, national statistical agencies, and World Bank country desks. See Annex 1 for the methodology for the forecasts. Remittances are defined as the sum of workers' remittances, compensation of employees, and migrant transfers – see www.worldbank.org/prospects/migrationandremittances for data definitions and the entire dataset.

Migration and Development Briefs are prepared by the Migration and Remittances Unit, Development Economics (DEC) and Poverty Reduction and Economic Management (PREM) network. These briefs are intended to be informal briefing notes on migration, remittances, and development. The views expressed are those of the authors and may not be attributed to the World Bank Group. The latest data on remittances and other useful resources are available at <http://www.worldbank.org/migration>. Our blog on migration titled "People Move" can be accessed at <http://blogs.worldbank.org/peoplemove>. Contributions, feedback, and requests to be added to or dropped from the distribution list, may be sent to Dilip Ratha at dratha@worldbank.org.