

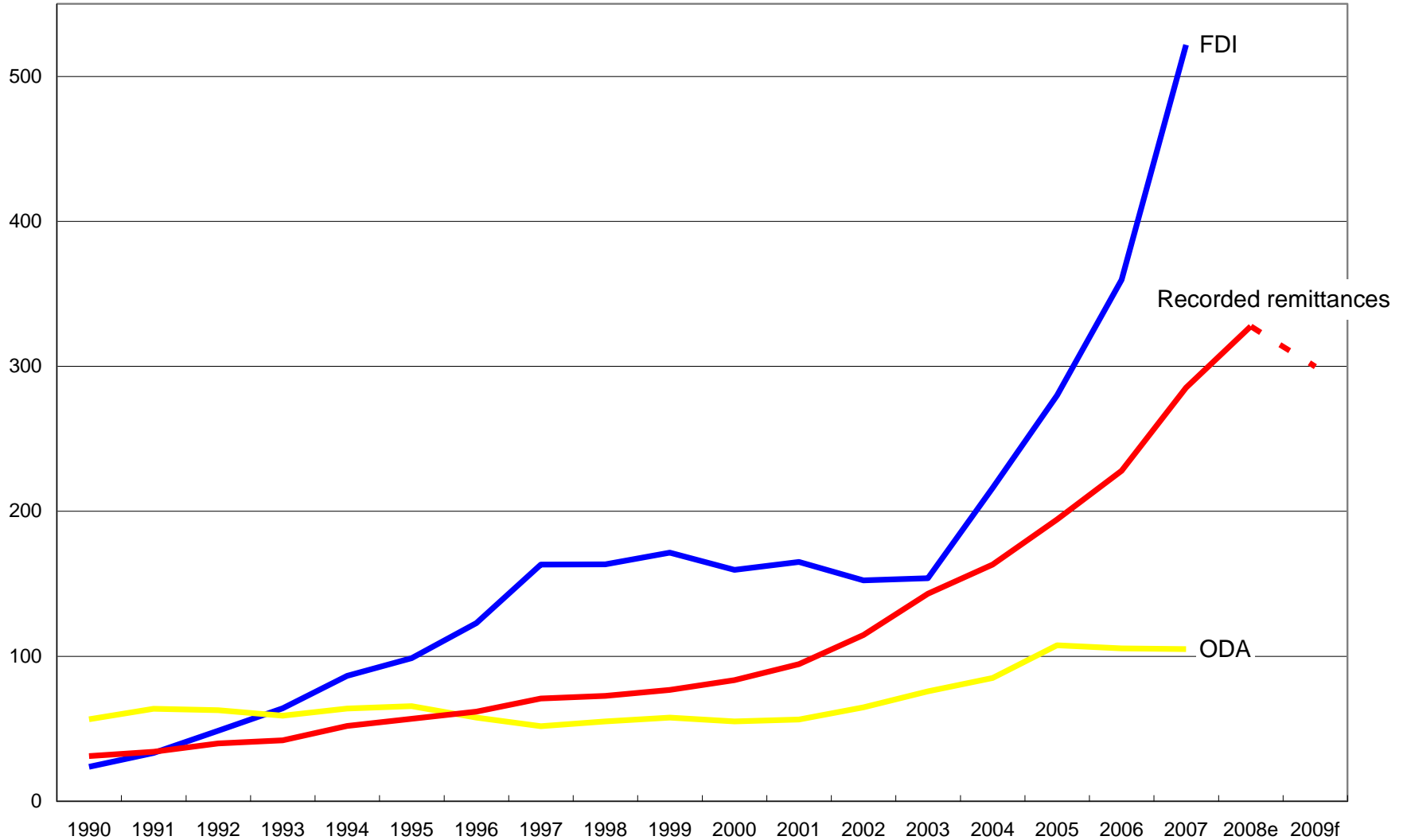
# **Remittances and Access to Financial Services as a Lever for Economic Development**

SUPPORTING SMEs IN A TIME OF CRISIS: HOW TO CHOOSE THE RIGHT ACTIONS

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# Remittance, FDI and ODA flows to developing countries (current USD billion): 1990-2008



## Rapid growth of officially recorded remittance flows due to:

- General increase in remittance transfers;
- Increased use of formal transfer channels because of:
  - Intensified international efforts to attract remittance transfers into formal channels to encourage their potential “development impact” and to support AML/CFT activities following 9/11;
  - Decreasing formal transfer costs; and
- Improved data collection and recording procedures.

# Formal and Informal Remittance Transfer Channels

**Formal** transfer channels – those included in the regulated financial system; such as banks, MTOs, postal offices, credit unions and MFIs (including pre-paid cards and transfers over the Internet or by mobile phone).

**Informal** transfer channels – those not regulated by financial authorities; such as direct physical transfer of cash and hand delivery or value transfers through stores, travel agencies and courier services.

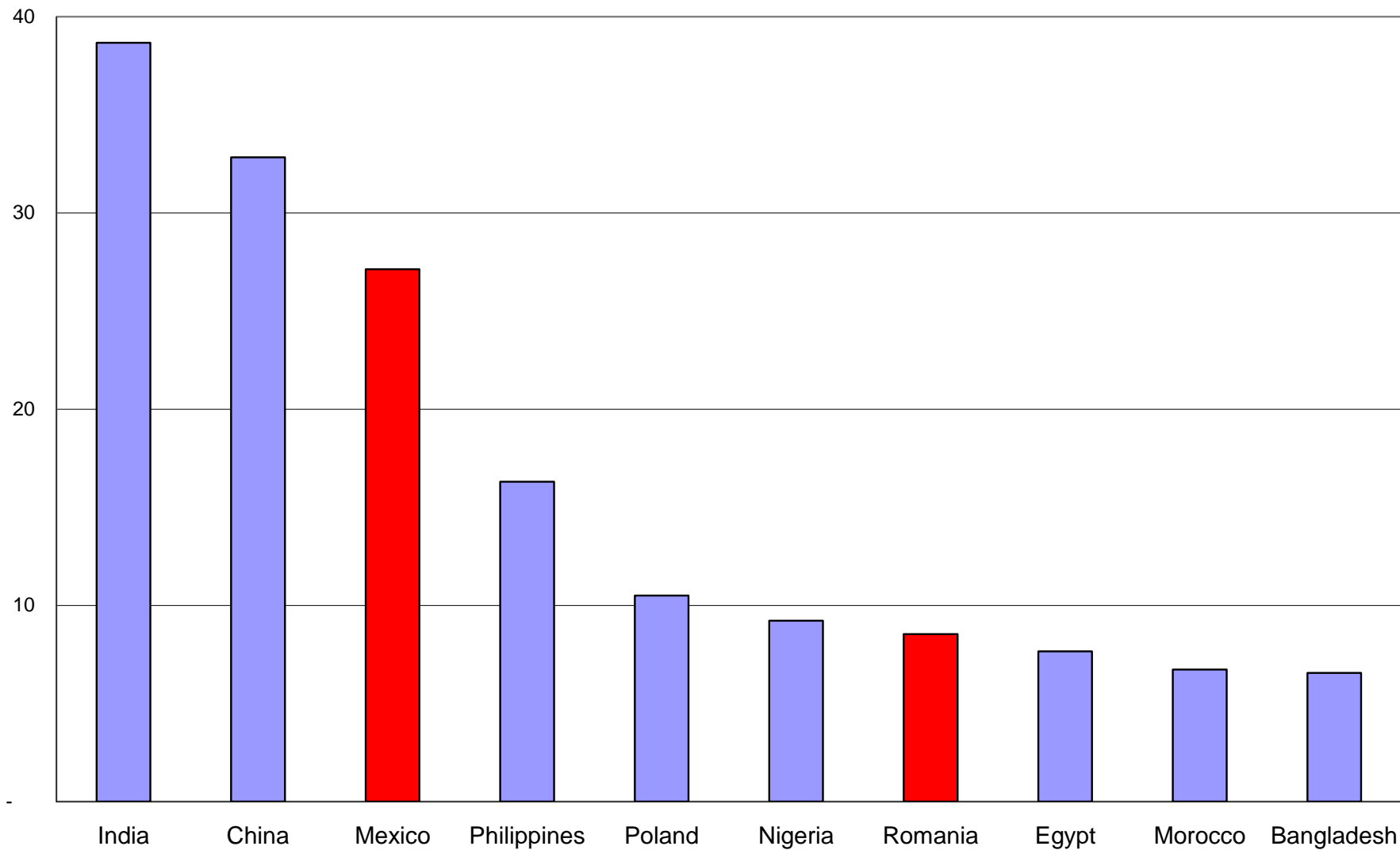
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Informal remittance transfers are guesstimated to add around 50% to officially recorded flows worldwide.

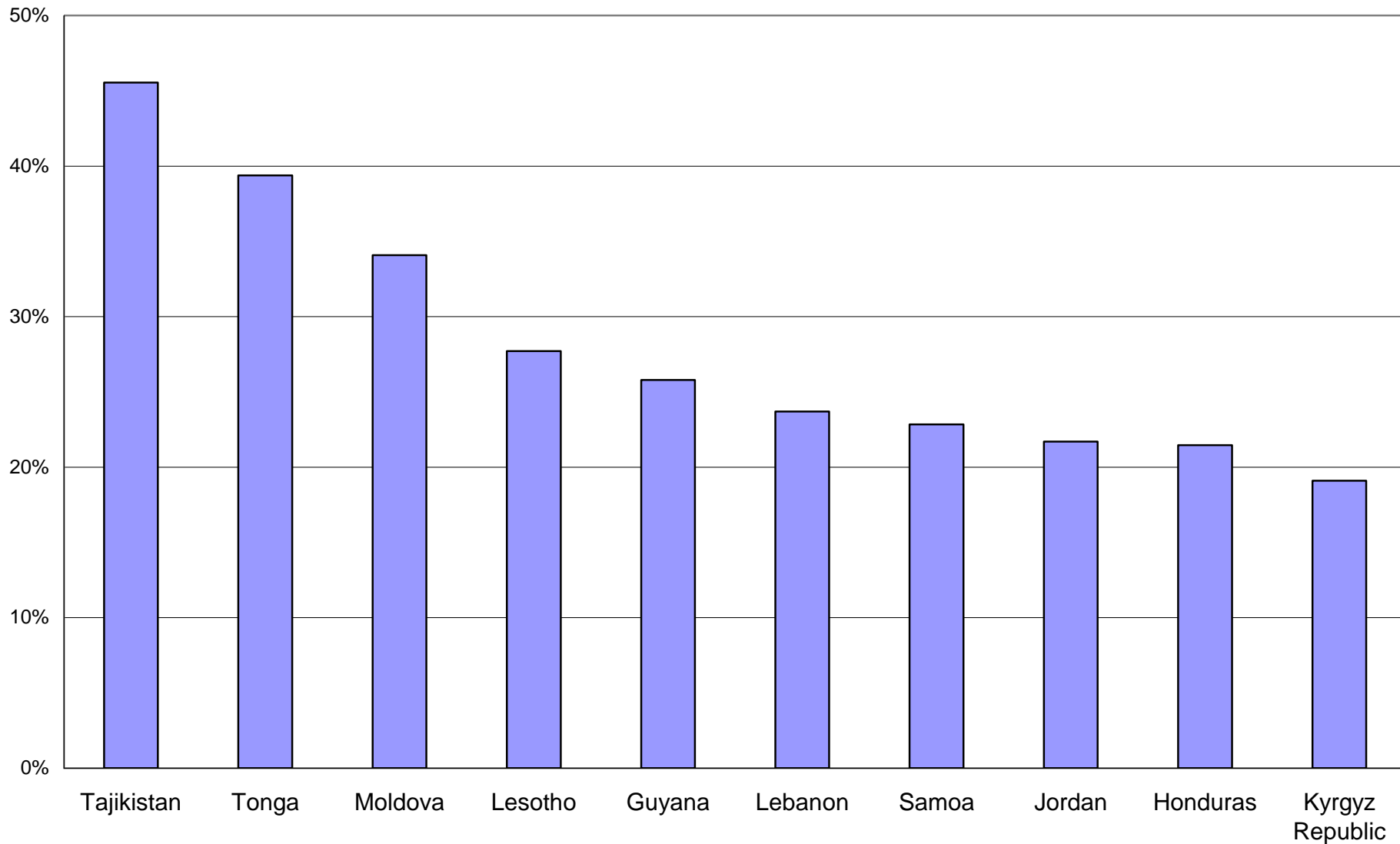
The choice of transfer mechanism is based on preferences for accessibility, confidentiality, cost & transparency, ease of use, safety & trust, speed, and transaction convenience & cost.

- Although increasing competition in formal markets has resulted in lower fees, wire transfers are still relatively expensive.
- Importance of south-south remittances, accounting for 30-45% of total flows to developing countries.
- Importance of domestic money transfers.
- Growing importance of remittance inflows as a source of funds and foreign exchange for many countries. Generally considered as more stable and less cyclical (even counter-cyclical) than other inflows... although the current global economic downturn is expected to cause a 7-10% drop in remittance flows to developing countries in 2009.

# Top 10 remittance-receiving developing countries in **absolute** terms (current USD billion): 2007



# Top 10 remittance-receiving developing countries in relative terms (% of GDP): 2007



# Remittances - the new development mantra?

Evidence suggests that remittances:

- Do have important and direct welfare-enhancing and consumption-smoothing effects for the remittance-receiving households; and
- Do contribute to the reduction of poverty on a country / macroeconomic level; but
- Do **not** *per se* lead to economic growth and development.

# Remittances and access to financial services

- The development impact of remittances is often thought to be linked to their impact on financial development.
- Remittances can be seen as a point of entry into the formal financial system for many remittance-receiving households, allowing them to access other financial services.
- Microfinance institutions (MFIs) can:
  - offer wider and deeper outreach (generally more present in rural areas and more accessible for poor and low-income households),
  - play an important role in guiding the use of remittance funds (through for example financial literacy programs and/or business development services), and
  - provide more competition in the remittance transfer market.

# MFIs and remittance transfers: Institutional advantages

- Client retention and attraction;
- Diversification of income;
- Cross-selling of products;
- More income (hopefully profit) to finance other MFI activities (such as business development services or financial education programs) or to lower the cost of lending; and
- Diversification of funding sources.

# MFIs and remittance transfers: Institutional challenges

- Proper market/customer analysis;
- Compliance with regulatory requirements (with regard to money transfers, foreign exchange and AML/CFT);
- Sufficient institutional and technical capacity;
- Sufficient financial strength; and
- Difficulty to reach sufficient scale.

## How can MFIs provide remittance services?

- Build up their own transfer service; or
- In partnership with MTOs, banks, postal offices and/or mobile phone companies as agents or part of platform/network.
- Using which technology? In addition to wire and bank/SWIFT transfers, branchless options to expand and improve access and reduce costs include:
  - Pre-paid cards
  - Internet
  - Mobile phone

- Potential role of financial literacy programs in expanding outreach and meeting clients' needs, especially with regard to branchless banking.
- Final considerations:
  - Remittances and microfinance are not the only routes to growth and development; and
  - Microfinance should be considered as a complement (not a substitute) to other types of financing to avoid crowding out more advanced financing for SME development and alike.