Developing a Road Map for Engaging Diasporas in Development

A HANDBOOK FOR POLICYMAKERS AND PRACTITIONERS IN HOME AND HOST COUNTRIES

Dovelyn Rannveig Agunias and Kathleen Newland

International Organization for Migration (IOM)

MIGRATION POLICY INSTITUTE

Chapter 6: Remittances: Making Private Money Work for the Common Good

Remittances are among the most tangible links between migration and development. According to World Bank estimates, officially recorded remittances flows in 2010 totaled over $440 billion worldwide.[206] As in the past, developing countries received the lion's share of global remittances ($325 billion). In 24 countries, remittances were equal to more than 10 percent of the gross domestic product (GDP) in 2009; in nine countries they were equal to more than 20 percent of GDP.[207]

Remittances have also been critical sources of foreign exchange for national balance of payments accounts and have been found to promote macroeconomic stability. Various studies have also shown that remittances facilitate human capital formation, mainly by improving access to education and health. They also lead to an increase in investments and the reduction of poverty, particularly within recipient households.

Previously confined to the everyday conversations of migrants and their families, remittances are now on the minds and agendas of many governments, members of civil society, the international community at large, and the private sector.

Remittances: A Menu of Viable Options

1. Strengthen remittance infrastructure
    - Inform the diaspora about existing remittance transfer mechanisms
    - Create more efficient channels of remittance transfer
    - Strengthen the financial institutions that migrants already use

2. Provide opportunities for more productive investment of remittances
    - Cross-sell complementary financial services such as remittance-backed mortgages
    - Securitize remittance flows

Lessons Learned and Challenges

1. In times of financial crisis, some remittance-linked products and programs may be adversely affected
2. Regulatory issues are critical to the success of remittance activities
3. Savings-based products are an important supplement to remittance-based financial products
4. Effective promotion and outreach are key
5. Creating alliances with institutions that add value to a project increases chances of success
6. It is important to innovate and create new institutions and products that cater to migrants' needs

1 Program and Policy Options

In reviewing initiatives associated with remittances, it is clear that fewer governments are choosing the policy path of control. Countries such as Brazil, for instance, once controlled remittance flows through rules governing foreign exchange. All international transfers had to go through the central bank. Likewise, in Viet Nam, the state used to control all foreign exchange trade and require temporary migrants to invest 30 percent of their earnings into a government fund. Such restrictions encouraged the use of informal channels for money transfers, which meant that remittances were not easily counted as part of the gross domestic product and did not bolster the country's foreign exchange position. Today, an increasing number of governments realize the advantages of more liberal remittance regimes.

Now, instead of taxing remittances, some governments have made a 180-degree turn and instituted tax breaks. For instance, in Egypt, migrants remitting through banks receive tax breaks for up to ten years from the time of the first formal transfer. Likewise, Colombia has reformed its tax laws to encourage expatriates to send a larger portion of their earnings to relatives in Colombia.

Indeed, the focus has shifted away from control to easing obstacles and providing incentives, especially financial and monetary incentives, typically with the support of civil society and the private sector.

Generally, two broad policy trends can be noted: (1) an increasing interest on strengthening the infrastructure supporting remittances, and (2) a renewed focus on using remittances more productively by cross-selling products linked to remittances and securitizing remittance flows.

A. Strengthening Remittance Infrastructure

The weaknesses of the infrastructure supporting remittances have been widely discussed and acknowledged by scholars and practitioners alike. The transaction costs of transferring remittances remain high in many corridors, and the challenges faced in distribution (particularly the so-called "last mile" problem) have yet to be seriously addressed, especially in remote areas. A transition from informal to formal systems is desirable for both development and security reasons. Many programs and policy prescriptions currently on the table are designed to address these deficiencies.

1. Inform the Diaspora about Existing Remittance Transfer Mechanisms

Many governments recognize that competition can lower costs and make transfers more rapid and reliable. For example, the cost of sending money has been more than halved since 1999 in the US-Mexico remittance corridor, which has many highly competitive money transfer companies and banks providing remittance services. One of the easiest ways to lower transaction costs is to encourage the entry of new legitimate operators in a given corridor, and to inform diaspora members about their ability to choose among existing remittance-transfer mechanisms. This facilitates increased competition among banks and money transfer organizations, thereby lowering costs and improving efficiency.

Competition may also help increase transparency. With the aim of increasing diaspora members' trust in formal channels, governments would do well to support the process.

There are various ways to increase transparency, one of the most important of which is to make information on transfer fees publicly available.

Launch a Score Card. The Inter-American Development Bank (IDB), for instance, in 2006 launched a remittance scorecard that ranks money transfer operators and banks according to a set of predetermined criteria.[208] A number of governments have since built on this approach by maintaining and supporting websites that compare the transaction costs charged by various remittance service providers.

Compare Transfer Fees. Mexico's Remesamex allows remittance senders to compare the fees of a wide range of transfer companies. The website, created by the National Commission for the Protection and Defense of Users of Financial Services (CONDUSEF), provides information on fees based on the amount of money, the origin, and the destination of the transfer.[209]

Other governments have worked with partners in civil society and the private sector. For instance, the Netherlands Ministry of Foreign Affairs has supported the creation of Geld Naar Huis, a website comparing remittance services offered by banks and money transfer organizations, including the costs charged for various destinations. The website is maintained by IntEnt, a nongovernmental organization (NGO).[210]

Deutsche Gesellschaft für Internationale Zusammenarbeit (GIZ), a federal enterprise of the German government, launched a similar website, called Geld TransFAIR, in 2007. The site was established by way of a public-private partnership between GIZ and the Frankfurt School for Finance and Management, a private consulting firm, which provided information about legal transfer channels from Germany to 33 countries. In 2010 the Frankfurt School took over full operation of the website.[211]

Although potentially useful to increasing transparency of remittance transactions, maintaining such websites can be difficult. As Box 1 shows, websites are useful only if migrants actually use them.

Box 1: The Limits of Information: Lessons from the Netherland's Geld Naar Huis and German International Cooperation's (GIZ's) Geld TransFAIR

If you build it, they will come. Government websites, however, often go unnoticed. The governments of Germany and the Netherlands both supported the creation of websites to provide consumer information on remittances and thus to boost competition between financial institutions and increase transparency. Both countries have faced challenges in informing migrants about the websites' existence and in encouraging them to use the sites regularly.

In an interview for this handbook, Sander Werrie, of the Netherlands Ministry of Foreign Affairs, explained: "We don't have the capacity to let people know that they can compare the costs. I think that is why there are too few people using the website. There has to be more of a campaign to improve visibility." Indeed, the ministry has requested IntEnt, the NGO tasked with maintaining the site, to allocate 50 percent of its €100,000 annual budget to a publicity campaign.

In the case of Germany, the problem is deeper than lack of awareness among migrants. As Regina Barbosa of GIZ, explained: "There have not been many changes in the costs of transferring money, so the website is not very dynamic because the financial sector is not very dynamic when it comes to costs and the various possibilities for transferring remittances."

The lack of information on services offered by various providers may have contributed to keeping remittance costs high since migrants may not be aware of cheaper alternatives, but it is not the only reason. Filling the information gap alone would have limited impact on transaction costs as long as service providers do not compete for customers by lowering their charges for remittance transfer.

Sources: Interview by the author with Sander Werrie, May 3, 2011; and by Julia Schad with Regina Barboza, April 28, 2011.

2. Create More Efficient Channels of Sending Remittances

One way to reduce transaction costs is to create more efficient remittance channels. Some governments have collaborated to create such channels themselves, while others have chosen to partner with nonstate actors such as registered banks, savings and credit cooperatives, microfinance institutions, and post offices.

Among multigovernment partnerships, an interesting initiative is Directo a México (see Box 2), which allows remitters to send money from a bank account in the United States to any bank account in Mexico. The service, which is a joint initiative of the US Federal Reserve and Banco de México, offers a safer, cheaper, and more efficient remittance channel than traditional money transfer operators.

Box 2: Directo a México

In 2001 Banco de México and the US Federal Reserve agreed to study the possibility of linking payment systems across their border to create an efficient interbank mechanism. By October 2003, the two government institutions had established such a framework, focused initially on pension payments to recipients in Mexico. By February 2004, this service had been extended to commercial payments sent from any US financial institution enrolled in Directo a México to any individual with a bank account in Mexico.

The consumer sending the money pays all fees, and there are no deductions or fees for the beneficiary in Mexico. The payment is initiated in US dollars and converted into Mexican pesos using a highly competitive foreign exchange rate based on the FIX, the interbank reference foreign exchange rate, determined and published by the Banco de México, minus 0.21 percent. Consumers using Directo a México pay one of the lowest fees on the market, at less than $5 per transaction regardless of amount remitted. Since the central banks in both countries process the payments, remittances arrive safely and on time.

Source: Directo a México, "About Directo a México," www.directoamexico.com/en/quees.html.

Governments may also choose to link their postal networks with those of other countries. Chile, Spain, Uruguay, the United Republic of Tanzania, and Uganda have taken such an approach to ensuring more efficient and secure transfers (see Box 3).

Box 3: Post Offices as Remittance Providers

Individuals in Chile and Spain are now able to use the postal network to send and receive money to and from abroad. The service is currently offered in 110 post offices in Chile, 2,300 in Spain, and 60 in Uruguay. The service is fast and secure; money transfers can be executed and delivered in 15 minutes. The service relies on the International Financial System (IFS) application developed by the Universal Postal Union's (UPU's) Postal Technology Centre. To help postal operators move toward providing money transfer services by electronic means, UPU has been making its electronic network more secure and reliable. In 2005 it started a centralized clearing system, while concentrating additional efforts on key migration corridors. Using its IFS application, it has opened 150 corridors connecting 36 countries. Some 60 other countries are currently testing the application and may join the UPU's international financial network.

The United Republic of Tanzania and Uganda recently launched a pilot project facilitating remittances between the two countries. The project, organized by the International Organization for Migration (IOM) in partnership with UPU and the Pan African Postal Union (PAPU), assesses the flow of remittances between the two countries, with a focus on electronic postal money transfers, and trains postal staff, stressing the benefits of remittances to national development.

Source: H. Bohela Lunogelo, *Pilot Study on Supporting an Affordable Electronic Tanzania and Uganda* (Geneva: IOM, 2009), www.migration4development.org/sites/m4d.emakina-eu.net/files/Final_IOM-UPU_Assessment_on_Remittances_btw_UG-TZ.pdf.

3. Bank the Unbanked

In most developing countries today, financial systems serve a very small proportion of the population — the social and economic elite. A number of governments aim to increase the participation of financial institutions in remittance markets in an effort to attract more remittance senders and recipients as clients.

Ultimately, having access to the formal financial system confers a variety of benefits to senders and recipients: lower transfer costs, greater security of transfers, the possibility of building assets through savings, and the leveraging of larger amounts of remittance funds via credit. The goal is to move from the current "cash-to-cash" system to the electronic transfer system of account to account. To this end, the focus has been on how to remove the obstacles that are keeping migrants from opening bank accounts.

Offer Consular Identity Cards. Some governments issue identity cards to migrants so that they can open bank accounts. Stringent identification requirements prevent many migrants from opening bank accounts. Some governments have issued identity cards to their nationals living abroad, regardless of immigration status. As Box 4 highlights, issuing consular identity cards presents a simple solution to encourage banking, especially among the unauthorized.

Box 4: Consular Identity Cards: A Simple Solution to a Big Problem

Unauthorized migrants generally have difficulty accessing many financial services in their destination countries since they don't necessarily have the documentation that banks require. Some origin governments have issued consular identity cards for their citizens abroad. Most financial institutions in the United States accept consular cards as a valid form of identification. Such cards may serve to encourage migrants (regardless of immigration status) to open bank accounts.

- Countries that issue consular cards include: Argentina (matrícula consular Argentina)
- Brazil (matrícula de cidadão Brasileiro)
- Colombia (tarjeta de registro consular)
- Dominican Republic (localizador archive)
- Ecuador (consular ID)
- Guatemala (tarjeta de identificación consular)
- Guinea (consular ID)
- Mali (carte d'identité consulaire)
- Mexico (matrícula consular)
- Nigeria (citizen's certificate)
- Pakistan (National Identification Card for Overseas Pakistanis)
- Peru (tarjeta consular)
- Senegal (carte consulaire)

It is important to note, however, that cooperation with the destination government is critical. It was only after the US Department of Treasury announced in 2002 that consular cards were valid government-issued identification that these cards were accepted at US banks and government offices.

Offer Financial Literacy Training. Some governments consider financial literacy a critical factor encouraging migrants to use banks and other formal financial institutions. They hold financial literacy campaigns to promote sending remittances through formal channels and to encourage migrant workers to use the many other services that banks offer.

In Burkina Faso, the High Council of Burkinabés Abroad, a government institution created to engage the diaspora, works with diplomatic missions abroad to conduct information campaigns, not only on remittances but also on the rights and duties of the diaspora in their host countries. With an annual budget of 40 million francs (US$82,000),[212] the High Council regularly sends a team of about eight individuals to conduct these information meetings, especially in missions where there is a large population of nationals of Burkina Faso, such as Senegal and Togo.[213] The campaign typically lasts for ten days and is conducted with the support of local banks. Similar initiatives can found in the Philippines, Mexico, and Nicaragua (see Box 5).

Box 5: Teaching Financial Literacy

In 2008 the Philippines' embassy in the Republic of Korea initiated a financial literacy campaign to maximize the potential benefit of diaspora remittances to national development. Working with Filipino community groups in Seoul, the embassy conducted more than a dozen seminars involving 400 participants in a one-year span. Assessments of the seminars' effectiveness suggest that participants' financial literacy and money management skills improved.

Likewise, in 2010, the Institute for Mexicans Abroad (IME), a government institution catering mainly to overseas Mexicans, reported that 69 percent of Mexico's consulates in the United States had an annual program to provide financial education to Mexican migrants; in addition financial information was displayed in all the consulates' waiting areas. IME has also partnered with IDB, a multilateral lending institution, to provide financial education to both migrants and their families living in Mexico.

It is important to offer financial training to households that receive remittances. IOM, for instance, has partnered with Grupo Promerica (BANPRO), a Nicaraguan bank, to provide financial education to remittance-receiving families. Since the project began in October 2010, more than 3,000 family members with relatives working in the United States, Costa Rica, and Spain have received training in financial literacy, including creating a budget, increasing savings, and using the financial products available to migrants and their families.

Sources: Interview of Jed Dayang, Philippines Foreign Service Officer, interview by author, May 23, 2011; Javier de Leon, answer to Questionnaire, Part II, and de Leon interview; Joan Hall, *Ten Years of Innovation in Remittances: Lessons Learned and Models for the Future* (Washington: Inter-American Development Bank, 2010), http://idbdocs.iadb.org/wsdocs/getdocument.aspx?docnum=35163520.

Make Banks Migrant Friendly. Another method of improving remittance channels is to help banks become more accessible to migrants. For instance, GIZ, Germany's national development agency, conducted a survey among the Serbian population in Germany and found that many Serbs do not send remittances through formal channels. Many cited fears of losing money sent through banks. The survey also revealed that many Serbian migrants lacked information on ways to remit through Serbian banks.[214]

To address the problem, GIZ organized a conference in 2009 that brought together Serbian banks and several Serbian migrant organizations from Germany to discuss reasons behind migrants' reluctance to use formal remittance channels. The conference effectively facilitated information sharing between the two groups. After the conference, GIZ created an information brochure on how the Serbian financial system works.

4. Strengthen the Financial Institutions that Migrants Already Use

Governments also increasingly recognize the enormous challenges at the distribution stage, or the so-called "last mile" of remittance transactions. Establishing operations in remote areas involves additional costs that many banks and money transfer companies are not prepared to bear. As a result, people in many rural areas face higher transaction costs and more limited access than their counterparts in cities.

A critical factor in servicing the last mile is to strengthen the financial institutions that migrants already use, such as post offices, rather than encourage them to use financial institutions that for various reasons — geographic, cultural, or otherwise — they prefer not to use.

5. Strengthen Rural Savings Banks

In 2002 Mexico created the Banco del Ahorro Nacional y Servicios Financieros (National Savings and Financial Services Bank, BANSEFI), a second-tier national credit corporation and development bank that aims to help rural savings banks adapt to the provisions of new laws and trains personnel at Mexico's banking regulatory agency, Comision Nacional Bancaria y de Valores (CNBV), to supervise them. As Box 6 shows, an external evaluation highlights BANSEFI's success in improving regulatory compliance on the part of rural savings banks, and thus encouraging the formal transfer of remittances.

Box 6: Strengthening Mexico's Rural Banks

BANSEFI's task is monumental: modernize the information systems of the 600 BANSEFI branches and 400 other bank branches that belong to regulated banks, develop new savings products within BANSEFI for remittance recipients, and create infrastructure for receiving and channeling remittances sent by Mexicans residing abroad.

- An external evaluation done within 36 months of the project's implementation showed that the initiative had achieved the following: Upgraded the technology of 938 savings banks and 493 branches of BANSEFI
- Established a new remittance-transfer network that helped increase the number of monthly remittance transfers serviced by the network to approximately 70,000 (nearly a 50 percent increase over two years)
- Expanded the geographic coverage of the service, with more than 1,000 branches of the 125 savings banks participating in the remittance-transfer network
- Developed new products such as savings instruments, debit cards, credit cards, and housing savings accounts that attract remittance recipients as clients.

Rural inhabitants in the areas reached by BANSEFI's 1,431 branches and/or the rural savings banks now have access to better remittance-transfer services. In the first half of 2007 alone, 620,451 transfers totaling 2.586 billion Mexican pesos (nearly $240 million) were made.

Source: Hall, *Ten Years of Innovation in Remittances.*

6. Strengthen Cooperatives

Ecuador has taken a similar route by assisting cooperatives. The Central Bank of Ecuador (BCE) implemented the Alternative Remittance Distribution Channel for Small Ecuadorean Financial Intermediaries project in 2007. At that time, rural cooperatives could not access electronic transfer management systems. The project aims to address this gap by connecting them into a high-technology interbank payment system called the Sistema Nacional de Pagos (National Payment System, SNP). Access to the SNP will reduce costs and transfer times increase the use of formal channels in rural areas. (see Box 7).

Box 7: Linking Cooperatives to the Remittance Market

Most cooperatives in Ecuador do not receive customers' remittances directly from an SNP since they are not regulated and do not maintain current accounts with the central bank. The project created a mechanism to bring these unregulated cooperatives into SNP via a regulated cooperative acting as a "network hub."

Although the project is still in its early phases, and final outcomes are not available, intermediate result so far has been significant. Thirteen unregulated cooperatives have been incorporated into the SNP. Another 49 unregulated cooperatives have applied to become participants. BCE is taking a more aggressive approach in marketing its services to the cooperative sector, and this is showing results, according to an independent review of the project.

Source: Hall, *Ten Years of Innovation in Remittances.*

B. Provide Opportunities for More Productive Investment of Remittances

Although remittances are private money, governments can encourage the development of investment vehicles and financial services that allow migrants to invest remittances more productively and thus to leverage their income stream from abroad to achieve greater financial security.

1. Cross-Selling Complementary Financial Services to Remittance Receivers

There has been an emerging interest in cross-selling complementary financial services and products along with remittance services. The idea is to design financial products that serve the needs of migrants and their families while directing them to more productive uses. Germany, for instance, supported a study in Uzbekistan that analyzed the demand for special financial products and assisted private banks in developing such products. The US Agency for International Development (USAID) supports remittance-backed housing and business loans.[215]

2. Offer Remittance-Backed Mortgages

The introduction of home loan products that use migrant remittances as collateral or to establish credit has been among the most promising innovations in recent years. The idea is to develop legal and financial procedures that permit migrants to purchase a house for themselves or their families without having to return to their country of origin. The remittances are used to pay off the loan, while the house serves as loan collateral.

Governments encourage transnational alliances between financial institutions in countries of origin and a variety of actors in the countries to which migrants immigrate, primarily through subsidized lending. For decades, developing countries have subsidized loans in order to expand access to mortgage lending for low-income households. Governments in Mexico, the Philippines, Colombia, and Burkina Faso continue this policy by subsidizing mortgage programs for their migrants. All four countries have special procedures to adapt to the unique requirements and needs of their migrant populations. As Box 8 shows, Colombia and Burkina Faso built programs from scratch while Mexico and the Philippines expanded on existing programs for local populations.

Box 8: Remittance-Backed Mortgages: Four Models

Colombia Nos Une offers a housing program for emigrants who are interested in buying a home in Colombia but require financing. The initiative runs the program Mi Casa con Remesas ("My House with Remittances") together with the National Bank of Colombia and IDB. Cesar Vallejo, adviser at Colombia Nos Une, said he considers the program a success.

10.000 logements. The Ministry of Housing and Urban Development in Burkina Faso began the project 10.000 Logements ("10,000 Homes") in 2006 as a housing program fully funded by the state with the goal of providing people decent housing at reduced cost. The program is said to be popular among overseas nationals of Burkina Faso who express a strong desire to benefit from public housing. The project, however, is said to have completed only 25 percent of its objectives to date.

The Pag-IBIG Overseas Program is a voluntary savings program that aims to provide Filipinos abroad the opportunity to save and obtain a housing loan of up to 2 million pesos ($50,000).[216] The loan is financed using reserves of Pag-IBIG, the largest government pension fund. To be eligible for a home loan, applicants must be active contributors to the fund for two years. Loan entitlement is dependent on the amount of monthly contributions to the fund. The monthly savings contribution can be as little as $5 to obtain a 500,000 peso loan or as high as $20 to obtain the maximum loan of 2 million pesos. The fund also offers a lump-sum option, whereby new members can obtain the loan immediately by paying the total of a two-year contribution.

The program can be used by all Filipinos abroad, including those naturalized in other countries and those eligible to apply for dual citizenship. In addition, there is a focus on small and low-income borrowers, given that the program offers preferential repayment terms and interest rates for smaller loans. For instance, a home loan of 300,000 pesos or less will incur a 6 percent annual interest rate and is payable in 30 years — about half the interest rate and 10 years longer than the terms commonly offered by private-sector lenders.

Sociedad Hipotecara Federal (SHF), a government financial institution with the mandate to foster the development of primary and secondary mortgage markets, runs Mexico's mortgage program. Unlike the Philippines' Pag-IBIG, SHF is a wholesale mortgage bank and guarantor; it does not directly lend to the public but rather provides long-term funding to financial intermediaries and hedges the inherent interest-rate risk.

The program hopes to tap into demand unmet by US- and Canada-based financial institutions, which are reluctant to take Mexican real estate as collateral, or by Mexican lenders that do not have a system to offer services in the United States and Canada. The loan program is a private-public partnership between SHF, IDB (a regional lending institution), BANSEFI, IME, and four SOFOLES or private financial intermediaries — Su Casita, Hipotecaria Nacional, Crédito Inmobiliario-Terras, and Hipotecario Crédito y Casa.

Under the partnership, SHF assumes the "full faith and credit" of the federal government on risks taken through 2013. In other words, SHF offers unconditional commitment to pay interest and principal on debt in case of default, while IDB shoulders part of the financing needed and provides critical technical support. The intermediaries operate like any other mortgage lender. The loan application is started and processed in the United States, funded in pesos, and serviced in Mexico. Once approved, a remittance provider's relatives can start looking for a house in Mexico. When a house is found, the intermediary sends an appraiser to the location to verify the price before lending money to the applicant. The Mexican immigrant can then pay off the mortgage — in US dollars — at the intermediaries' US branches. As of 2009, 2,000 loans have been disbursed to remittance-receiving households (an increase of approximately 80 percent from baseline data); 7,000 migrants have received information and training on financial concepts related to mortgages; and more than 10,000 brochures have been distributed.

Sources: Vallejo interview, May 2011; Ousman Nacambo interview, May 2011; Pag-IBIG Fund, "Pag-IBIG International Operations," www.pagibigfund.gov.ph/pop/; Hall, *Ten Years of Innovation in Remittances*.

3. Securitize Future Remittance Flows

A number of countries have also resorted to the securitization of future remittance flows in order to raise external financing. Many developing countries do not have a wide range of external financing sources and rely solely on official development assistance (ODA) and foreign direct investment (FDI) to finance public investment. However, both ODA and FDI have declined as a share of GDP over the past few decades. Securitization is an alternative method to finance public investment since workers' remittances represent a future-flow receivable that financial institutions can collateralize to access additional capital.

Ngozi Okonjo-Iweala and Dilip Ratha of the World Bank put it succinctly:

> *When a migrant transfers foreign currency to a relative's creditworthy bank in his home country, the bank pays out the remittance from its holding of local currency. That transaction creates a foreign currency asset equivalent to the size of the remittance, which can be used as collateral for borrowing cheaply and over the long term in overseas capital markets. Such borrowing has no effect on the flow of money from migrants to their beneficiaries. Yet development banks, national banks in developing countries and donor agencies can partner to harness enough remittances and create enough collateral to raise significant sums of money to invest in agriculture, roads, housing and other vital projects.*[217]

In other words, securitization enables banks in developing countries to raise hard currency by selling bonds. The largely predictable and sustainable flows of remittances to developing countries make remittances relatively reliable as collateral for securitization and attractive for investors. Typically, future remittance securitizations are rated investment grade BBB- or higher as future flows are heavily overcollateralized.[218] According to Standard and Poor's, only a slowdown of remittances of greater than 95 percent would lead to a default on remittance securitizations, which makes securitization an ideal vehicle for raising funds even in times of recession (see Box 9).

Many countries could potentially issue bonds backed by future remittances, with amounts ranging from 10 to 20 percent of their annual remittance flows, depending on the level of overcollateralization required to implement these transactions.

A number of developing countries have securitized future remittances and other future receivables.[219] Since 2000 they have raised in excess of $15 billion in international financing with an average maturity of five to 15 years.[220] These countries include, but are not limited to Brazil, Egypt, El Salvador, Guatemala, Jamaica, Kazakhstan, Lebanon, Mexico, Peru, and Turkey. Other countries, such as Nepal, are considering securitizing remittances.[221]

Box 9: Securitization of Remittances in a Time of Global Recession

After the financial crisis of 2008, remittances were more stable than ODA and FDI flows. According to the African Development Bank (AfDB), the flow of ODA and FDI were five and three times more variable than remittances between 1995 and 2009. Net remittance inflows to Africa in 2010 amounted to $37 billion. The financial crisis caused a decline in ODA flows to African countries by almost 50 percent in 2009, but remittance flows were relatively constant.

Due to the reasons behind the 2008 financial crisis, many may be averse to securitization. However, securitization per se was not the main cause of the financial crisis, but rather the excessive overvaluation of existing assets (mortgage-backed securities), not future-backed receivables. In fact, unlike the securitization of existing assets, the securitization of future receivables held up during the financial crisis.[222] Given that the securitization of future remittance flows requires overcollateralization, the risk is very low.[223]

Moreover, one of the strengths of securitizing future-flow receivables such as remittances is that institutions are able to withstand liquidity crises. Any negative public reaction to securitization after the 2008 financial crisis should therefore be seen as short-lived.

In the aftermath of the 2008 financial crisis, the International Finance Corporation (IFC) provided assistance in helping a credit union in El Salvador securitize future remittance flows to help provide microloans to micro, small, and medium-sized enterprises (MSMEs). The US Department of State also launched the BRIDGE program with El Salvador and Honduras to help their governments securitize future remittance flows to raise lower-cost and longer-term financing for infrastructure, public works, and other commercial development projects.

Sources: International Finance Corporation (IFC), "FDC Remittance: Summary of Proposed Investment," www.ifc.org/ifcext/spiwebsite1.nsf/0/1DDDBD894DD604EB852576BA000E330D; IFC,, "IFC's First Remittance-secured Financing Enables Credit for El Salvador's Microenterprises, Lower-Income People," June 16, 2010; US Department of State, "U.S. BRIDGE Initiative Commitments with El Salvador, Honduras," (media note, September 22, 2010), www.state.gov/r/pa/prs/ps/2010/09/147549.htm.

2 Challenges and Lessons Learned

Leveraging remittances for development is an important but difficult goal to achieve. Despite improvements in facilitating remittance transactions and strengthening diasporas' links to development, a number of challenges remain.

A. In Times of Financial Crisis, Remittance-Linked Products and Programs Can Be Adversely Affected

Experience in Latin America suggests that transnational loan products linked to remittances can be affected by crisis. During the 2008 crisis, for instance, many Mexican migrants in the United States lost their jobs and reduced their remittances to Mexico. An assessment by the Inter-American Development Bank (IDB) found that this led to an increase in raised the risk level of the SOFOLES's portfolio of transnational mortgage products during the 2008 crisis, as migrants lost jobs and their remittances were reduced. The four SOFOLES continued to disburse transnational loans at a slower rate than projected. In a global economic downturn, mortgage-financing companies tend to wait out the crisis since mortgage loans, relative to other types of loans, entail more risks due to the higher amounts and longer lending periods.[224]

As the IDB highlights in its review of SHF's experience, it is important to:[225]

- Investigate the possibility of using guarantee funds to encourage continued lending in times of crisis.
- Develop remittance-backed products that can withstand a financial crisis, such as housing microfinance (i.e., housing improvement) models and projects and the securitization of remittance flows, since these lower the risk for both the lending institutions and the borrowing institutions.

B. Regulatory Issues Are Critical to the Success of Remittance Activities

Regulatory issues are especially important if the executing agency expects to work in foreign countries and navigate their various regulatory environments. IDB's experience in the Americas suggests strongly that a "regulatory environment can constrain or facilitate transnational mortgage products." Such environments differ significantly across countries, and special attention has to be given to state- and local-level regulations.[226]

For instance, in some destination countries the marketing of remittance-backed mortgages and loans is made difficult — and, in some cases, impossible — by laws and regulations that prohibit the selling of savings products and properties abroad. In the United States, consumer protection laws prohibit foreign-based lenders from offering savings products to US residents. At the same time, proof of savings is critical to establish credit for low-income migrants.[227] Regulations regarding the selling of property abroad also vary by state. For instance, in Washington, DC, Maryland, and Virginia, a mortgage-broker license is the only requirement to sell properties abroad, while in California the regulations are less straightforward. Thus, Su Casita, one of SHF's intermediaries in the United States, is headquartered in Ohio even though its biggest market is in California.[228]

According to the IDB, it is important to ensure that:[229]

- Project design adequately reflects regulatory environments.
- Regulatory frameworks for remittances, for nonbank financial institutions, and for other areas that might influence a future project (such as mobile banking) are sufficiently analyzed before designing project activities.
- Project strategies do not depend on the regulatory environment remaining constant over the course of a project, since this is beyond control.

C. Savings-Based Products Are an Important Supplement to Remittance-Based Financial Products

Migrants need to save money in order to make a down payment which ensures that migrant mortgage-holders have a high stake in continuing to make mortgage payments even in the face of an economic downturn. Successful programs, such as the Philippines' Pag-IBIG Overseas Program (see Box 8), have incorporated a strong savings component into their mortgage programs. This allows migrants access to financial products that they would otherwise not have.

D. Effective Promotion and Outreach Are Key

The effective promotion of financial products is a difficult but extremely important component of the effort to magnify the development benefits of remittances. In the United States, for instance, IDB's experiences suggest that various factors can undermine efforts to promote mortgage products including but not limited to the following:[230]

- large size of the country;
- overabundance of marketing commercials;
- number of marketed brands;
- characteristics of the target group (i.e. level of dispersion, legal status, geographic stability, and level of trust of financial institutions and authorities).

The lack of legal status among the target group can be a particularly challenging impediment, since irregular migrants are less trustful of marketing initiatives and are unlikely to provide information. To address this problem, Mexico generally involves various government agencies when promoting transnational mortgage-finance products and providers among Mexicans in the United States.[231]

IDB's experiences in the Americas also point to the value in ensuring that:[232]

- Project activities include the building of alliances with groups that can help lower marketing costs (such as hometown associations [HTAs], church groups, migrant radio stations, and NGOs working with migrants).
- Projects contain an activity for branding both a product and an institution.
- Publicly available databases are created and maintained to provide information on the location and profile of migrant populations.
- Sufficient time in the project timeline is allocated to marketing.

E. Creating Alliances with Institutions that Add Value to a Project Increases Success

From providing financial support to helping to reach new markets, creating alliances can bring various benefits. In Mexico, for instance, IME's participation in the promotion transnational mortgage products, such as those offered by SHF, contributed to the success of the products. Indeed, IDB finds that an alliance among a wide range of partners, from builders and mortgage brokers to NGOs and migrant associations, is crucial in developing housing markets. BANSEFI's and its network of rural savings banks have is years of experience working in rural areas.[233] The ability of partner agencies to leverage funds is also crucial. Mexico's SHF and Philippines' Pag-IBIG have their own funds and can provide counterpart funding.

F. Innovate and Create New Institutions and Products that Cater to Migrants' Needs

Effectively encouraging migrants to use formal banks may require adoption of innovative means to identify migrants, such as via the issuance of consular ID cards. Indeed, US financial institutions' acceptance of the Mexican matrícula consular encouraged Mexican migrants to establish bank accounts there.

One other approach is to create innovative institutions that squarely address migrants' mistrust of banks. As IDB highlights, the SOFOL, a Mexican for-profit structure for credit facilities that is not a bank, is an entirely new financial entity to disperse loans.[234]