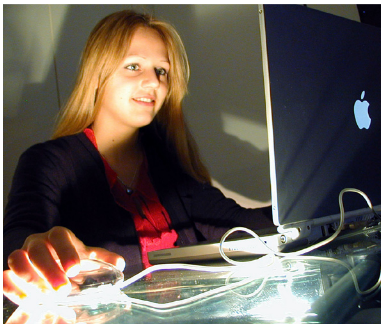
IDB

Attracting remittances: market, money and reduced costs

Manuel Orozco, PhD

January 28th., 2002

MIF
FOMIN

Inter-American Development Bank

Attracting remittances:

Market, money and reduced costs

Manuel Orozco, PhD
morozco@thedialogue.org

Report commissioned by the Multilateral Investment Fund of the
Inter-American Development Bank.
Washington, DC.
January 28, 2002

Introduction

This report analyses the market of remittances from the United States to nine Central American and Caribbean countries from the perspective of their business practices. The report focuses on remittance companies, business practices that benefit their customers sending and receiving remittances by criteria such as lower charges, convenient business locations, and community outreach. Money transfer charges as well as exchange rate differentials continue to be of concern for nine major Latin American remittance recipient countries. A key finding is that remittances are less costly when competition is greater.

As the report shows, charges in fees and exchange rate incurred to send and receive remittances can add up to 14 percent of the amount sent. It is in the interest of nations and families receiving remittances to increase the quantity and flow of remittance monies, in part by reducing the share lost to transaction costs, and in part by increasing the gross flow of migrant remittances and investments.

From the business perspective, competition among both existing financial service companies and potential new remittance transfer entrepreneurs needs stimulating. Greater competition should lower prices and increase services offered to actual and potential customers who send remittances abroad. The private sector transferring remittances can contribute to increased remittance flows by lowering transaction costs and offer development alternatives to individuals and groups through their services.

The report is based on more than fifty interviews. Nearly eighty remittance companies were studied to identify factors such as charges, exchange rates used and their effect on consumer expenditure, mechanisms employed to transfer money, distribution networks, and other services offered.

1. Background

The majority of Latin American immigrants residing in the United States, documented or not, honor a commitment to their family and community by sending them remittances. Latino immigrants who earn less than $25,000 a year tend to send somewhere around $200 a month, that is, nearly ten percent of their income. Thus, cost matters to the sender. Moreover, money recipients, who are generally low-income families earning below average incomes, also value the remittance they receive and are affected by any cost incurred to them in the exchange rates.

Today's total remittances from the U.S. to Mexico, Central America, and the Caribbean are estimated to be at least $15 billion annually. In comparative terms, remittances tend to be more than 10 times greater than U.S. foreign aid to these countries; they are equivalent to five percent of Mexico's exports, seventy percent of El Salvador's exports and nearly one quarter of Nicaragua's national income. El Salvador, the Dominican Republic, Jamaica, and Guatemala are among the major remittance recipients in the Caribbean Basin. In 2001 the combined amounts remitted to these four nations added up to over five billion dollars, which is equivalent to 50 percent of those countries' trade through the Caribbean Basin Initiative.

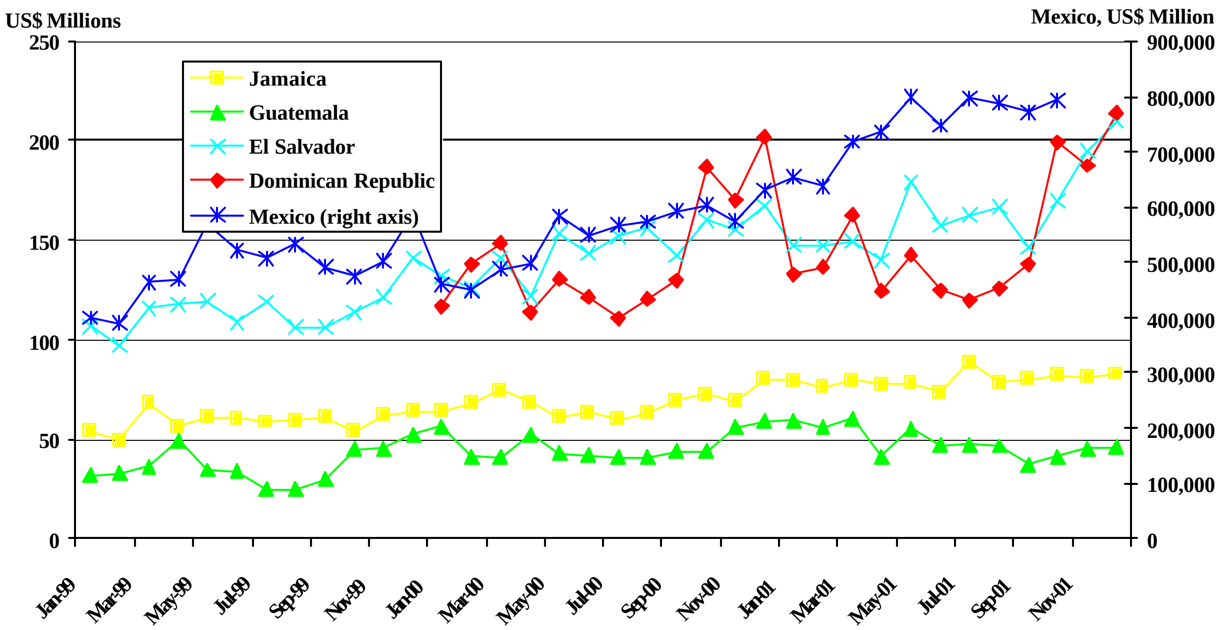
Table 1. Remittances to Latin America, 2001,

Year	Remittances
Colombia	$500,000,000*
Cuba	$800,000,000*
Dominican Rep.	$1,807,000,000
El Salvador	$1,972,000,000
Guatemala	$584,000,000
Honduras	$400,000,000
Mexico	$9,273,747,000
Nicaragua	$600,000,000
Jamaica	$959,200,000
Ecuador	$1,400,000,000
Ten Countries	$18,295,947,000

Source: Central Banks of each country except for Cuba (ECLAC), Colombia (World Bank) Ecuador (The Economist, Jan 2002), Nicaragua (author's estimates). * data for 1999.

Within this context, governments, businesses, and markets are important agents in stimulating the flow of remittances. Businesses sell services facilitating the transfer of remittance funds, but transfer charges to consumers continue to vary. Yet, remittances continue to flow to Latin America without showing signs of decline. As Figure 1 shows, monthly flows of remittances in selected countries have continued an escalating trend in the past three years.

Figure 1. Remittances to Five Latin American Countries, Jan. 99-Dec. 2001



2. Reducing Charges on Sending Remittances

The players within the remittance industry constitute a crucial piece in the puzzle of economic development. As intermediaries they can contribute to increase foreign currency sent by migrants. Specifically, in addition to the generation of employment through their own businesses, financial intermediaries can contribute to and enhance individual and community development by reducing transfer charges when high, providing transparent and efficient services, offering incentives to recipients to use the financial system (saving and investment options), and promoting development in the community.

This report analyses more than 70 money transfer companies. Data gathering was conducted to estimate fees charged, exchange rate used, services offered, and type of distribution network in place. Moreover, interviews were conducted with company officials in the sending and receiving sides in order to understand the company dynamics and market operations. Money-remitting companies in nine different countries were studied, but the focus was on four countries; Guatemala, El Salvador, the Dominican Republic, and Jamaica. The other countries that were analyzed were Mexico, Haiti, Colombia, Nicaragua, and Cuba.

Table 2. Number of Companies and Countries Studied

Country	Number of Companies
Colombia	4
Cuba	4
Dominican Republic	15
El Salvador	20
Guatemala	15
Haití	5
Jamaica	7
México	23
Nicaragua	13

Source: Data compiled by the author. Some companies remit to more than one country.

The costs companies incur in transferring remittances are generally reflected in the fees they charge. These fees are based on a number of factors including operating costs, the exchange rate used in the transaction, the transfer mechanism employed by the company (and whether it is more labor or capital intensive), the level of market competition existing in both the sending and receiving areas, and company's profit margin. Therefore, the criterion by which this study assesses or measures the price of transactions involves identifying and analyzing the a) fees charged, b) level of market competition, c) transaction type (whether the remittance is changed into local currency or not), and d) transfer mechanism.

In addition to these criteria, other practices are explored such as a company's transparency, its outreach in support of the community's development, its relationship with the clientele, and any additional financial services offered by the company. These latter issues are also important as they have a developmental impact on the household and a community. The use of a particular institution can motivate both senders and recipients to improve their personal stock.

Indicators that assess what works for a customer's benefit are based on whether the company offer lower than average fees and exchange rates and their services generate incentives for customers to add value to their money, such as providing other financial services in the same location. Some of these criteria are presented in the table below:

Table 3. Indicators of Remittance Transfers: What works to the customer's benefit.

Criteria	*Indicators*
1. Transfer fee	Lowered fees for customers may indicate lowered costs for remittance companies.
2. Exchange rate used	If there is no exchange rate, no currency purchase costs are incurred by sender and recipients. Fees may be higher, however.
3. Transfer mechanism (hand delivery, money order, electronic transfer: debit card, bank to bank, internet, courier agency transfer, etc.)	More capital intensive transactions mean lower costs for the company, but not necessarily lower fees for the consumer.
4. Marketplace competition (supply side)	The higher the number of companies in any market, the lower the transfer costs. The exception is when companies are formed in oligopolies or remittance 'cartels'.
5. Business location and geographic coverage	Companies located within areas with a better economic infrastructure exhibit lower transaction costs
6. Development support	Support to the local community adds value to the product and loyalty to the company
7. Financial Services	Offering services such as banking or bill payment increases interest in the company
8. Transparency	A company that advertises its exchange rates cultivates or promotes more trust from the customer.

This report's findings show that:

- In the past three years, charges have declined significantly in some countries.
- Transfer costs incurred by customers range from $7 to $26.
- Fee charges decrease with competition. Remitters to Mexico, El Salvador, and Guatemala charge lower fees than companies sending money to Jamaica and the Dominican Republic. For countries, like Cuba or Haiti, where there are more market restrictions, charges are higher.
- Distribution networks offering lower commissions tend to promote the decline in charges. The use of electronic interfaces also helps in reducing costs.
- A growing number of companies offer money transfers in dollars. This practice does not guarantee that received remittances will be not involve disadvantageous exchange rate charges as banks can sell dollars at adverse exchange rates. (This topic requires further study and is beyond the scope of this report.)
- Banks are increasingly opening money transfer franchises and are offering some of the lowest charges at about $9.00, however these institutions continue to have a small and limited reach.
- Credit unions and cooperatives continue to offer the lowest fees. Like banks, however, their reach is small. Moreover, the home country distribution networks are not well established within the credit union system. In Guatemala, Jamaica, and the D.R., cooperatives are entering the remittance transfer business, and in El Salvador, credit union transfers are taking place although they are low at under $2 million a year.

a) Transfer Charges: Changes and Challenges

Perhaps one of the most significant changes in the remittance market is the decline in transfer costs. Three years ago the cost of sending remittances to different Latin American countries averaged about 15.0% of the amount sent. Those transfer costs have now declined. In 1999, for example, Western Union charged $22.00 for transferring up to $200.00. By 2001 that charge was dropped to $15 (see Table 4).

Table 4. Transfer Costs for Sending Remittances with Western Union

Charge for sending...	$200		$300	
Year	1999	2001	1999	2001
México	$20.00	$15.00	$25.00	$15.00
El Salvador	$22.00	$18.00	$27.00	$21.00
Dominican Republic	$22.00	$18.00	$30.00	$24.00
Guatemala	$22.00	$20.00	$29.00	$21.00
Colombia	$22.00	$20.00	$29.00	$15.00

Source: Orozco 2000 and data compiled by the author.

Although there is a relative decline in the price for customers, fees plus the exchange rate applied to the amount received in local currency still show a widespread range in prices. Immigrants pay from $6 to $26 to send $200. The Figure 2 summarizes the charge range incurred by senders and recipients in fees. One important aspect in Figure 2 is price elasticity. Remittance charges decline with volume sent, and particularly observed in charges for amounts ranging from $150 to $300. This finding is important as it shows that prices tend to decline when customers send greater amounts; only 15 percent of companies charge over 9.5 percent for $300. However, the majority of customers send less than $200 a month in remittances and therefore they don't tend to enjoy the benefits of price elasticity in the $300 amount (See Table 4). This means that the majority of senders tend to pay over $15 in fees. Table 5 shows the fee per amount sent.

Figure 2. Percent Charges by Companies per Remittance Sent

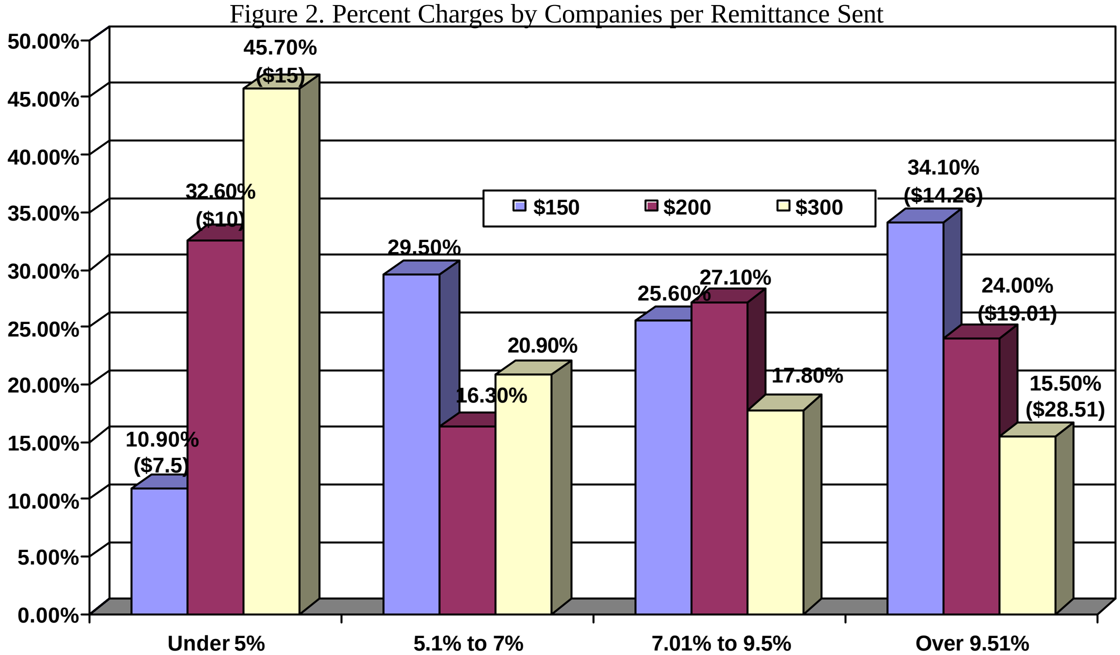


Table 5. Percent distribution of remittances sent by immigrants

Amount sent	Percent of senders
Up to $150	42.2
$ 151 to $250	22.4 (22% sends $200)
$251 to $300	17.0
Over $300	18.4

Source: IADB Survey on remittances.

Table 6. Fees Charged on Amount Sent

	Fee charge scale			Total
Amount	Over $15	Between $10.01 and $15.00	Under $10.00	
$150.00	24.8%	37.2%	38.0%	100.0%
$200.00	35.7%	31.8%	32.6%	100.0%
$300.00	54.3%	24.8%	20.9%	100.0%
	38.2%	31.3%	30.5%	100.0%

Source: data compiled by the author

These charges represent a significant cost to the type of money sender, relatively poor Latin American immigrants. First, Latino immigrants are generally low-income people. According to the U.S. Census nearly 33 percent of Latino (or Hispanic) households earn less than $20,000 a year. Second, about 46 percent Latin American immigrants are not incorporated in the financial systems through banks. Their earnings are therefore usually checks cashed in cash checking stores that charge a high fee. About two thirds of immigrants tend to receive their salaries and wages this way. They then send remittances. This means that costs of receiving and sending income remains a challenge to the majority of immigrant remittance senders.

Table 7. Household Income by Race

	Household income		
Group	Under $20,000	Between $20,001 and $35,000	Over 35,000
Hispanic/Latino	32.5%	24.9%	43.0%
Non-Hispanic White	11.3%	16.6%	72.1%

Source: U.S. Census Bureau, CPS March 2000.

Importantly those companies that charge above 9.5 percent tend to have a significant market share in the recipient countries. Therefore, while only 24 percent of companies charge fees above 9.5 percent of the principal, they have the largest market share. Therefore these fees affect a larger number of immigrants. According to the IADB survey on remittances, 41 percent of senders used Western Union and MoneyGram.

Table 8. Remittance Companies Charging over $15 on $200 Remittance

Charge	Company
Over $20	Uno Money Transfers; Ria Finance Service; CAM; Caribbean Airmail; Grace Kennedy Remittance Services/ Western Union (Jamaica) Western Union; Vimenca/ Western Union (D.R.); Remesa Agil; RIA Express; BPD International (D.R.); Jamaica Air Express Couriers; Paymaster/ Money Gram (Jamaica)
Between $17.51 and 19.99	Money Gram; La Nacional / caribe express (D.R); Mateo Express (D.R); Pronto Envio; Quisqueyana (D.R);
Between $15 and 17.5	Gigante Express (home delivery) (ELS, GUA); Girosol; Jamaica National Overseas; King Express (to the Interior) (GUA); Money Gram – Bancomer (MX); Rapid Remittance / Vigo (MX); Ria Enviaw/Banco Mex (MX); Ria Enviaw/telegrafo (MX); ServiMex (MX)

b) Country differences

The price of sending remittances varies significantly and a key determinant in those prices is the extent of market competition to send remittances to that recipient country. When the results are disaggregated by country, the price of sending varies from $7 to $26, significantly informed by market competition. Mexico is the country with the lowest fees among the nine countries studied. It is also the country with the greatest market choices for customers. The competition in Mexico ranges from small businesses to large corporations. Significantly, among the reasons for expanded competition is the entrance of the banking industry into the remittance market. Bancomer, Banamax, and Bancomex are major competitors in the industry, variously offering direct money transfer services (like remittance agencies) and/or working jointly with money transfer companies like MoneyGram and Ria Envia. The major competitor, Western Union, has gradually lost its market share in Mexico due to the entrance of many competing companies. The competitive market may make it more difficult for remittance companies to survive. In Mexico as prices have gone down, many companies have been unable to stay in the competition.

Following Mexico is El Salvador, which also exhibits greater competition and is the second largest remittance recipient in the Hemisphere. While Western Union remains as a dominant player for El Salvador with about 25 percent of market share, it also has to compete with other companies. Its first major competitor is Gigante Express, a courier company that mostly sells and sends money orders, and which has also nearly a quarter of of the market share. Second, competition exists with commercial banks. BanSol, BanComercio, Banco Agrícola, and Banco Cuscatlán have operations in the United States as money transfer agencies and compete with Western Union and Gigante Express. Banco Agrícola, the largest bank in El Salvador, has about 10 percent market share. The bank offices in Los Angeles transfer nearly two hundred million dollars a year. BanComercio hals almost the same market share as Banco Agrícola.

The Dominican Republic has more than fifteen well-established companies remitting from the United States. These companies are grouped into a conglomerate through an association named the Associación Dominicana de Empresas Remesadoras de Divisas, Inc. The members of this association generally follow similar prices. As Table 8 shows, remittances to the Domincan Republic tend to have relatively higher prices than other countries with similar characteristics (high volume, significant competition, and immigrant demographic concentration). The companies generally offer two kinds of charges: $8+5 percent (when sending in dollars) and $5+5 percent (when sending in local currency) of the amount sent. Remittance companies in the Dominican Republic usually offer a home delivery service as part of their fees. In other countries, home delivery generally incurs an extra dollar fee. The Asociación claims that their charges offset price fluctuation. This claim is bolstered by the fact that the standard deviation of the fees is the lowest among the different countries studied, that is, $3.7. In other countries the standard deviation is over $5, except for Mexico.

Table 9. Fee Charges per Country as Percent of a $200 Remittance

Country	Under 5%	5.1% to 7%	7.01% to 9.5%	Over 9.51%	
Mexico	56.00%	24.00%	20.00%		
Guatemala	40.90%	22.70%	22.70%	13.60%	100.0%
El Salvador	38.10%	23.80%	23.80%	14.30%	100.0%
Colombia	25.00%	25.00%	25.00%	25.00%	100.0%
Dominican Rep.	10.00%	10.00%	43.30%	36.70%	100.0%
Haiti	20.00%		40.00%	40.00%	100.0%
Jamaica	14.30%		42.90%	42.90%	100.0%
Nicaragua	38.50%	7.70%	7.70%	46.20%	100.0%
Cuba				100.00%	100.0%
All countries	32.6%	16.3%	27.1%	24.0%	100.0%

In Jamaica, money transfers also tend to be more expensive. Western Union, through its arrangement with the local firm Grace Kennedy, controls the majority of Jamaica's remittance market. With about 200,000 transfers a month coming from the United States, Grace Kennedy (representing Western Union), manages somewhere between 65 percent and 70 percent of the market share. Another competitor with operations in the United Kingdom and the United States is Jamaica National Overseas, which is part of Jamaica National Building Society. In 2001, Jamaica National Overseas transferred $95 million from the United States, which amounts to 10 percent of the market share

These results show that there are differences among countries for the charges to transfer money. Competition among remittance sending companies is a key variable explaining the country differences. However, there may also be other factors involved, such as the type of institution participating in the money transfer process or the technologies employed.

c) Difference between sending in local and foreign currency and exchange rate issues

Charges vary depending on whether money is sent in local or foreign currency. Money transfer institutions tend to charge more when the amount is sent in U.S. dollars (as the company's to profit with the foreign exchange is affected). Conversely, if the money is sent in local currency at lower fees, the recipient loses a percentage of the remittance in the foreign exchange rates.

Table 10. Fee charged and Type of Currency

	Fee charge scale			Total
	Over $15	Between $10.01 and $15.00	Under $10.00	
Local currency	22.6%	49.1%	28.3%	100.0%
Dollars	56.3%	18.8%	25.0%	100.0%
Did not want to provide an answer	28.6%		71.4%	100.0%
Money Order	33.3%	66.7%		100.0%
	37.7%	34.2%	28.1%	100.0%

According to company officials in different countries and businesses, most remitters request the money be sent in the country's local currency. Because of the exchange rate losses, remittance recipients relatives receive less than the (average monthly) $200 that is sent to them. On average, recipients lose nearly $60 a year from the exchange rates. Considering that the average household income for Central American and Caribbean families is below $200 a month, one sees that the price of sending and receiving remittances amounts to more than an additional month's income.

Table 11. Average Fees charged to send $200

Country	*Local C.*	*Dollars*
Mexico	$11.60	NA
El Salvador	$13.00	Same
Guatemala	$13.00	$13.00
Dominican Rep.	$14.75	$19.5
Nicaragua	$15.08	Same
Haití	$16.00	21.00
Colombia	$16.67	Same
Jamaica	$16.71	NA

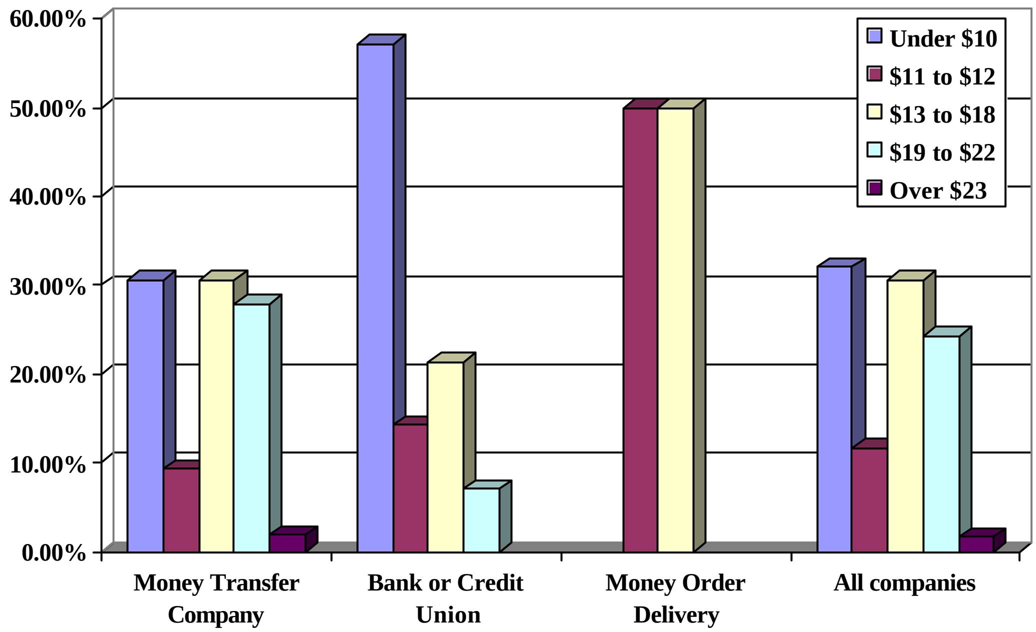
Table 12. Foreign Exchange Spread by Range

Country	Range			Total
	Under $3.00	$3.01 to $5.00	Over $5.00	
Colombia		33.3%	66.7%	100.0%
Dominican Rep.	16.7%	88.3%		100.0%
Guatemala	44.4%	55.5%		100.0%
Haiti	100.0%			100.0%
Jamaica		80.0%	20.0%	100.0%
Mexico	13.6%	23.6%	58.8%	100.0%
All Countries	21.9%	36.3%	31.7%	100.0%

d) Remitting institutions

Is there a relationship between fees charged and type of institution offering the money transfer? Are there any yardsticks to measure costs? Despite average prices to customers of over seven percent the amount sent plus over two percent in the exchange rate applied, there are some businesses that offer lower priced transfers (i.e, four percent of a $200 remittance). Banks, for example, tend to charge less than $10 for the transfer, whereas money transfer companies charge over that amount. Nearly sixty percent of banks but only 30 percent of money transfer companies charged $9 or $10 for any transaction under $200 (See Figure 3). These companies are usually located in El Salvador, Mexico and Guatemala, the most competitive markets.

Figure 3. Type of Money Transfer Institution and Charge by Range to send $200



There are numerous reasons why banks offer lower charges. The home country offices of banks involved directly in money transmission a) are generally the largest banks in the country, b) have the capacity to acquire capital upfront to back the outflow of transactions, c) have an already-existing distribution network, d) are better known by the sending clientele, and e) concentrate on attracting volume from demographically concentrated areas where migrants of the bank's country reside. Smaller players like money transfer companies often have to find an investment partner as well as banking or other financial institutions to arrange distribution schemes and are therefore likely to incur extra costs.

Nevertheless, the availability of banking institutions involved in money transfers is not widespread and banks do not provide or guarantee an inexpensive service, but rather a cheaper service, at least in most cases. Banks also often respond to the presence or absence of competition, and do not necessarily offer a lower fee service. For example, Jamaica and the Dominican Republic have banking institutions with branches operating as money transfer companies in the United States. However, their charges are not necessarily lower than the other non-banking institutions remitting to these countries (see Table 7).

Table 13. Financial Institution Charging Less than $10.00 for a $200 remittance
(as % of total charges)

Country	Money Transfer Company		Bank or CU	
	Under $10	Above $10	Under $10	Above $10
Colombia	25	75.00	NA	
Cuba			NA	
Dominican Rep.	8	92.00		
El Salvador	27.27	73.73	75	
Guatemala	42.86	57.13	100	
Haití			100	
Jamaica	16.66	83.33		
México	41.17	58.83	66.66	33.33
Nicaragua	36.36	63.63		
All countries	25.53	74.47	57.14	42.86

As noted, prices set by companies vary significantly. Operating costs to transfer money include service to the customer through a point of sale with an agency; use of the electronic interface to transfer the amount; availability of capital to back the money upfront, establishment of a distribution network on the receiving side; and customer service. Generally for money transfer companies, the costs to carry out individual transactions run somewhere between three to six dollars (some analysts argue the costs are even lower). Banks already have an infrastructure in place in the home countries, therefore their costs may be lower. One company which charges $10 and remits to Mexico and Central America explained that their company spends 40 percent on transfer costs and the agent, another financial institution, retains 50 percent of the fees. In addition to the remaining 10 percent, this company uses the foreign exchange rate as an additional source to make its profit. Their primary means for this business to increase profits was to increase volume and keep costs down. In contrast, other companies share less than 50 percent of the fees with the agents. Furthermore, some remittance businesses do not require agents because they own agencies and only need to cover overhead expenses. These entities are likely to have lower expenses.

At least one third of companies transfer remittances at $9 and $10, and some offer $7 transactions, which still make a profit (even without including the exchange rate applied). Companies charging over $10 per transaction and often over $14 per remittance transfer do not explain why their costs are considerably higher. Western Union generally argues that their charges are higher by virtue of offering a 'premium service', that is a service that is 100 percent guaranteed in terms of location, speed, reliability, and safety. Western Union does have a sophisticated and widespread company infrastructure. They have agencies throughout the United States and partner companies in Latin America. This capacity has rendered this company the remittance institution with the highest revenues in the Western hemisphere. Latin America is Western Union's most important market after the United States, Canada, and Western Europe, and represents 22 percent of the company's revenues. The company does appear to have two advantages over many of its competitors. First are Western Union's extensive geographical locations. Second, but more ambiguously, Western Union may offer better customer services than some of the competition. For example, Western Union operating as Vimenca or Grace, Kennedy notifies recipients that their money has arrived and provide toll free numbers to their clients so that they can inquire about the status of a transaction. However, other companies offer very similar services to Western Union while charging lower fees.

3. Conclusion and Recommendations

Although remittances are regarded as an important source of income by recipient countries, charges continue to be a concern to development agencies, immigrants, and other interested parties. With prevailing advanced technology in which money transfers can (and do) cost very little or nothing to the sender and recipient, is worth asking how money transfers can improve the welfare of recipients. For example, a person with a U.S. bank account could allow their relatives in the home country to withdraw cash with an ATM debit card sent by the account holder.

Expanding sending methods as well as the competition (or leveling the playing field) are factors that help reduce money transfers. Moreover educating customers about costs and charges is another important method. In Latin America there is a need to enable an environment that facilitates money transfers of any kind, be this for remittance, savings, investment, or consumption. An effort to support senders and recipient should pay attention to some areas in which remittances are less costly and can also have a developmental leverage.

a) Offer incentives to unbanked migrants in the U.S. to use formal financial institutions.

Only six out of ten Latin American immigrants use, or presumably consider themselves to have meaningful access to, bank accounts. The effects of being unbanked are significant, not only because of the higher costs and difficulties an individual incurs on a daily basis by not having bank accounts, but also because of their inability to establish credit records and obtain other benefits from a financial institution. Helping migrants to enroll in the banking infrastructure will help ensure lower fee transfers. Some government and private institutions are already engaged in that effort and could target a strategy linking remittance transfers with banking options as a way to attract them into the financial system.

b) Create a board that provides oversight for remittance companies, and in particular their fees and exchange rates

As with a large range of organizations, oversight boards are important institutions that may help to guarantee corporate transparency and accountability as well as compliance with standards for products and service. The U.S. needs such an institution on a nation-wide basis for money transfers. A remittance oversight organization could include representatives of money transfer companies as well as customers and other independent and knowledgeable parties. It could be or establish an independent board that reviews practices and other issues relating to remittances to Latin America (and elsewhere).

c) Establish a customer rights office on the recipient side to educate recipients about costs and better measure effectiveness and efficiency of services

Remittance recipients are seldom aware of many of the practices and methods of the remittance companies. For example, many senders do not know about the different exchange rates that prevail among many companies. Furthermore, there is no independent research or checks on effectiveness or efficiency of the various services. Non-governmental organizations could contribute significantly by educating money recipients about being informed customers.

d) Money transfer companies liaison with small banks and credit unions

The experience of Quiesqueyana, Vigo, and RapidMoney of liaising with small banks and credit unions points to important options to help reduce costs. These three companies offer an alternative to remittance recipients that enhance their use of this income source, through lower fees or through the access to an ATM for cash or a Visa debit card for purchases. Expanding these alternatives will also increase market competition and improve an imperfect remittance market.

e) Bank liaison with banks and credit unions

Another important strategy to help lower charges is to increase bank-to-bank agreements in the U.S. and Latin America regarding money transfers. Currently, banks generally charge over $30 for an international wire transfer. However, when the prospect of increased volume is considered, banks often show interest and are prepared to lower these fees. Harris Bank and Wells Fargo are important examples of this type of initiative. These banks arranged money transfers through Mexico's Bancomer. Money recipients in Mexico are also encouraged to use the banking industry once their currency arrives at a bank rather than at a money transfer agency.

f) Expand debit card use and motivate recipients to open dollar accounts

Using debit cards in the recipient country is an important way to reduce charges. But it is important that credit unions and banks must encourage money recipients to have credit union or bank accounts too. The percentage of Central American and Caribbean people with bank accounts is generally below 20 percent (except in Jamaica which has a much higher percentage). Banks and financial institutions are key development agents and, as they reach out more to society, the multiplying effect on development increases. Credit unions and other banks can enhance the welfare of remittance recipients by encouraging them to opening accounts and earn interest on their money.

ADDENDUM:

Are there best practices?

Money is transferred from bank to bank, from money transfer agency to bank, from credit union to credit union, agency to agency, and so on, and charges vary depending on these combinations. As discussed above, this report identified an eight point criteria to assess which of the companies have the best practices. These are fees, exchange rates, transfer mechanisms, the marketplace competition, business location and geographic coverage, development support, financial services, and transparency. No company studied in this report meets all the criteria for best practice. Some companies like Western Union may offer the best access to sending and receiving money, but at very high prices. Others may have low fees but offer limited geographic coverage.

When searching for best practices on remittance transfers, of the eight points, four issues are of particular importance in identifying the best company methods and approaches: below average prices and mark-up, services that add value to the money sent and received, transparency in reporting the real nature of prices and services to the customers, and developmental support to the community. Given the current environment that prevails in the money transfer business with various players in place and different transfer methods and charges, identifying the best practices is an important but difficult task. Three best practices can be presented here that meet some of the criteria highlighted at the beginning of this section.

Credit Unions—Credit Unions offer some of the best practices in money transfer opportunities to migrants. First, where credit unions are available, their costs are among the lowest. Some credit unions charge less than $7 in some cases no credit union surveyed charges more than $10. Second, in addition to the low charges, credit unions seek to offer significant benefits to the sender as well as to the recipient. One important benefit offered to senders is the incentive to enroll them in the banking system. Moreover, the credit unions have also used the fees charged to provide various plans to its members. Finally, credit unions tend to be transparent in the charges they make as well as in delivery of the money. They usually arrange the money transfer transaction either through an already existing company such as Vigo International Corporation or participate in the Irnet system of transferring money from credit union to credit union (Orozco 2000). In this latter case, money transfers are among the least expensive, charging $6.50 for anything under $5,000.

Examples of credit unions that are active in transferring remittances and working with Latino immigrants are Communidades in Los Angeles, transferring to El Salvador and Guatemala at $6.50 and serving mostly low-income Salvadorans; Bethex Federal Credit Union in New York, which uses Vigo, and Government Employees Credit Union (GECU) in El Paso, which also uses the Vigo system. GECU is unusually large with $700 million in revenues. Its participation in the remittance market, to immigrants from Mexico, is relatively recent (from about 2000), and has been very profitable as is reflected in the expanded revenues from GECU's branch that does most of the transfers.

Another credit union that started to offer money transfers is the Latino Community Credit Union (LCCU) in North Carolina, which offers transfers to Mexico and Central America. The LCCU not only offers low remittance charges but also provides important services to the Latino immigrant community. Latinos generally are low income and not all have bank accounts. According to the IADB survey, only 60 percent of Latino immigrants have bank accounts. The credit union thus provides an alternative to the community by inviting them to opening checking accounts with low deposits of $25 (as opposed to $500 or $1,500 in most banks). Moreover, this particular credit union uses the remittance fee charges to provide other free services and lending opportunities to their members. Because many low-income migrants regularly cash checks with third party institutions (rather than depositing these into their individuals accounts), as with remittances, they incur high fees to pay for that service (at very similar rates to current average money transfer fees). The Latino Credit Union, like Comunidades, does not charge for this service or for the use of ATMs. Moreover, migrants are able to send up to $5,000 for $10. LCCU too uses Vigo as their money transfer interface and manages to keep $8 of the $10 charge which it uses to offer community development programs and pay for its overhead costs. Vigo retains $2 and the exchange rate markup.

Despite the benefits they offer, credit unions continue to remain among the least involved in money transfer services, which is their primary limitation. Two major difficulties they experience deal with outreach. First, there are only a few credit unions offering services to migrants to send money. Except for Comunidades and Government Employers Credit Union, most credit unions do not offer remittances transfers or are not based in areas where there is a high concentration of migrants. Second, remittances transferred to the receiving country are mostly sent through a money transfer company. Although this method is relatively low cost, it would be even cheaper with the involvement (and often existence) of credit unions in the recipient side. In most countries, however, credit unions are still seeking strategies to offer money transfers. As the next section will show, in El Salvador money transfers to savings and loans cooperatives are beginning to attract customers although their participation is very limited.

Banks—Offering low charges is an important feature of the money transfer. Providing additional services that enhance or leverage the condition of the sender and the recipient is another significant element to consider. In that sense, banks are ideal institutions to offer remittance transfers at low cost and with significant benefits. Several Latin American banks have established offices in the United States as money transmitters. Their charges are significantly lower than those offered by companies like Money Gram and Western Union. However, these banks lack the capacity to offer additional services to customers because of U.S. legal restrictions. Notwithstanding this constraint, these Latin American banks have come to offer important services for many immigrants who are familiar with those banks in their home country.

Some American banks have established partnerships with Latin American counterparts to facilitate migrant money transfers. Although this practice is lesser known and rare, there are added benefits to this practice. Harris Bank of Chicago, for instance, has formed an agreement with Bancomercio in Mexico. Under this arrangement, Harris Bank transfers remittances at $12 for any amount up to $1,500. The amount charged is $2 higher than that offered by a credit union and the money transfer-banks (but far less than most conventional international bank wire-transfers as well as less than the charges of the major money transfer companies). However, in addition to sending money, Harris Bank has sought to reach out to the Latinos in Chicago. To that effect it established 24 branches known as "bilingual branches." This feature has added significant benefits to Mexicans in the area as not only they can not only send remittances but also be encouraged to get bank accounts and to join the financial system. In doing so, Harris Bank has used the money transfer business as an instrument or conduit to educate and attract the unbanked to use banks and new technologies. While this benefits the bank, it is also valuable to empowering and acculturating the immigrant community to conventional and cheaper financial practices.

Money Transfer Companies—As Figure 3 showed, there are a smaller percentage of companies that offer transactions below the average cost. These lower-fee businesses are mostly small money transfer companies that concentrate in particular cities where there is a significant migrant population sending remittances. They offer an alternative to other money transfer businesses that charge above average, such as Western Union and MoneyGram, and have a very small market share in the business, yet remain competitive.

One illustration of a company in this category is RapidMoney. It sends remittances to Mexico and El Salvador for a $10 fee and offers a card to the recipient to use it to withdraw the money. The sender also gets a receipt that reports the amount charged and the exchange rate applied for that transaction. In addition to this transparency and low charge, the company works with more than one distribution network to facilitate the transfer. One key feature of this company is its liaison with El Salvador's cooperative savings and loan system. Transfers made to El Salvador are done through the Federation of Cooperatives of El Salvador. The advantage of this arrangement has been that the Federation has been able to transfer remittances to low income Salvadorans and seek to attract them to join the cooperatives. As with banks and credit unions, however, the disadvantage of this company is that it does not have nationwide locations and operates only in Texas and Arizona. Moreover, its services, unlike banks and credit unions, are limited to money transfers.

One significant constraint to improving best practices in money remittances is the end point. Companies often find themselves constrained by high costs imposed by their Latin American counterparts, especially banks. Unless banks have a significant participation in the money transfer, they tend to charge high commissions for the transmission. In particular, the smaller the remittance company, and therefore the lower its volume of transferred funds, the higher the bank's commission charges are likely to be. In addition, Latin American banks and financial institutions are often not oriented to serve small customers like the remittance recipients and senders. This problem is addressed in more detail in the next section which reviews the existence of an environment that contributes to or enables the capacity for immigrants to interact economically with their home country, from sending remittances to investing.

Bibliography

List of people interviewed by country

<u>El Salvador</u>

Marisol Argueta, Embajadora, Ministerio de Relaciones Exteriores,
Ricardo H. Pineda Sarmiento, Director de Desarrollo Empresarial, Banco Hipotecario de SA,
Katherine Andrade-Eekhoff, Investigadora, FLACSO,
Carlos Alberto Ortiz, Gerente Banca de Servicios, Banco Hipotecario de SA,
Hector David Córdova Arteaga, Gerente Corporativo, FEDECACES,
José Napoleón Duarte, Director Ejecutivo, Fundación Jose Napoleon Duarte,
Jose Roberto Navarro E., Presidente, Banco Hipotecario de SA,
Mario Roger Hernández, Director General, Ministry of Foreign Affairs,
Alberto R. Parker, Gerente General, Western Union International,
Jose Luis Garcia Monge, Central Bank,
Xiomara Garcia, , Central Bank, Chief Balance of Payments
Enrique Hinds, , Banco Agricola, International División,
Bertha Silvia Mena de Morán, Gerente de Negocios y Administración, FEDECACES,
Rafael Ruiz Suárez, Director Ejecutivo, Programa Nacional de Competividad, Ministerio de Economia,
Sandra del Castillo, Banco Multisectorial, Infocentros

<u>Jamaica</u>

Grace E. Solas, Manager, Central Finance Facility, Jamaica Co-operative Credit Union League Ltd.,
Brian Goldson, Director, Information Services Division, Grace, Kennedy and Co. Ltd.,
Joan-Marie Powell, Executive Director, Grace, Kennedy Remittance Services Ltd.,
Robert Beers, Editorial Consultant, The Gleaner Company Ltd.,
Colin Bullock, Deputy Governor, Research and Economic Programing Division, Bank of
Myrtle D. Halsall, Division Chief, Bank of Jamaica
Oliver F. Clarke, Chairman, Managing Director, The Gleaner Company Ltd.,
Louise Brown, Director, Economic Information and Publications Department, Bank of
Sandra Grant Griffiths, Assistant Director, Jamaicans Overseas Department, Ministry of Foreign Affairs and Trade,
Chris Lowe, Managing Director, National Commercial Bank Jamaica Limited,
Dunbar T. McFarlane, Deputy Chairman, National Commercial Bank Jamaica Limited,
Peter-John Gordon, Director, Economic Planning and Research, Planning Institute of
David Panton, , ,
Rosalea Hamilton, Trade Relations, Ministry of Foreign Affairs and Trade,
Earl Jarred, Executive Director, Jamaican National Building Society,

<u>Dominican Republic</u>

Freddy Ortiz, Presidente Ejecutivo, Asociacion Dominicana de Empresas Remesadoras de Divisas Inc.,
Isidoro Santana, Secretario, Fundacion Siglo 21,
Marina de Garrigó, Vicepresidente, Bancredito,
Carmen Cristina Alvarez, Vicepresidente Ejecutivo, Banco BHD,
Marcia Cámpiz de Rodríguez, Vicepresidente, Banco BHD,
José Felipe Peña, President, BHD Worldwide Transfer System,
Susana López Rodríguez, 2do. Vicepresidente, Banco Mercantil, SA,
Danilo Del Rosario V., Embajador Director Ejecutivo, Presidencia de la Republica Oficina para la Promoción de la Inversión Extranjera de la Republica Dominicana ,
Luis E. Núñez Santana, Director, Departamento Internacional, Banco Central,
Edigarbo Garcia, Vicepresidente de Operaciones, Remesas Dominicanas,
Roberto Turull, Director de Programa de Bolsa de Inversiones y Subcontrataciones Internacionales (Biss), Presidencia de la Republica/ Oficina para la Promoción de la Inversión Extranjera de la Republica Dominicana ,
Virginio Rafael Gerardo, Director Ejecutivo, Asociación de Instituciones Rurales de Ahorro y Crédito, Inc.,
Julio C. Estrella, Consultor Económico, Departamento Internacional, Banco Central,
Ana Rita Tejeda Céspedes, Subsecretaria Asuntos Internacionales, ,
Santiago Tejada Escobaza, Subsecretario de Estado de Relaciones Exteriores, Encargado de Negociaciones Comerciales,
Luis Guillermo Flores, Director de Promoción, Presidencia de la Republica/ Oficina para la Promoción de la Inversión Extranjera de la Republica Dominicana
Marlenne Then, Vice-Presidente de Negocios, Western Union, Remesas Vimenca, SA.,
Mary Candelario, Secretaría de Estado de Turismo, Secretaría de Estado de Turismo,
José J. Castro M., Presidente, GSI Internacional,
Lorenzo Gatz, , Asociación de Institutos Rurales de Ahorra y Credito (AIRAC),
Zoraida Rosado, BANINTER,

Nicaragua
José Felix Solis, , Banco Central, ,
Guillermo Areas Solano, Business Development Group,

Guatemala
Carlos Enrique Guerra R., Experto III, Sección de balanza de pagos, Banco de Guatemala,
Claudia Sutter, GyT
Guatemalan Consul in Los Angeles
Julie Torres, independent consultant

United States
Ernst Heldring, Harris Bank
Guy Erb, Rapid Money
Paul Dwyer, ViaAmericas
Luis Pastor, Latino Community Credit Union
John Herrera, Self-Help,

David Grace, Irnet
Ernie Salazar, Vigo International




INTER-AMERICAN DEVELOPMENT BANK

1300 New York Avenue, N.W.
Washington, D.C. 20577, USA
Tel: (202) 623 - 1000
www.iadb.org