International Remittance Network

IRnet™

Red Internacional de Remesas

Money Transfers You Can Trust

THE DEVELOPMENTAL POTENTIAL OF REMITTANCES & THE CREDIT UNION DIFFERENCE

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I. INTRODUCTION

Over the past two years, World Council of Credit Unions, Inc. (WOCCU) has been engaged in developing a credit union-to-credit union proprietary network for international money transfers known as the International Remittance Network (IRnet®). With a physical infrastructure of 38,000 credit unions broadly disbursed in 85 countries, the international credit union system likely has the best infrastructure of any financial institution in the world to handle such payments. However, credit unions have been noticeably absent from this market.

Credit unions are not-for-profit financial cooperatives that have been operating for over 150 years. They can be found in nearly all parts of the world. In general, when safe, sound and efficient credit unions enter a market and are able to offer lower-cost services, competition increases and prices fall. IRnet seeks to be the trusted source for international money transfers for 100 million credit union members around the globe. For 30 years, WOCCU has been the apex trade association and development organization of the international credit union system. WOCCU is currently conducting eight projects in Latin America and Caribbean and more than 20 globally to strengthen cooperative financial institutions – some of which are in coordination with the Inter-American Development Bank. This unique position along with WOCCU's internal resources and a July 2000 partnership agreement with Vigo Remittance Corporation provide WOCCU with an unparalleled opportunity to establish itself as an innovator in the remittance market.

Over the past six months, it has become apparent that, in order to fulfill WOCCU's vision - *Quality Credit Unions for Everyone*, an open (as opposed to a closed) network will be needed. The agreement with Vigo is an indication of this open orientation. It will enable credit union members to use IRnet money-transfer services to 41 countries at one-third to one-half the cost that the competition charges.

Through both existing relationships between credit unions and their member-owners and new relationships with immigrant community outreach centers, the IRnet service will work to gain the confidence of individuals that send money abroad. Methods such as disclosing the actual exchange rate at the point of sale and refunding a member's money and fee if a problem occurs are examples of how the service delivers on the promise of building trust between the provider and the user.

I will focus my comments on the involvement of credit unions outside of the U.S., leaving that to my colleague from Texas, I will discuss the developmental role of credit unions in the remittance market and WOCCU's lessons learned are reviewed for application to this new remittance market for microfinance institutions.

II. Overview of the International Remittance Network

While the IRnet service, like most credit union services, costs less than similar services provided by the competition, the primary reason for credit union members to use the service is trust, both that the money will arrive and that the credit union is looking out for the member's best interests. Informal surveys of consumers sending money out of the country indicate that the most important issues for money transfers are security, price and speed.

A. What is the IRnet service?

The IRnet service provides credit union members with the ability to transfer small amounts of money worldwide. The IRnet service is being offered by credit unions in the U.S. and other countries. In coordination with partner organization, WOCCU is growing the network of sending points in the U.S. and other developed countries as well as their receiving locations in developing countries. Although IRnet is a service of WOCCU, WOCCU is reliant on its credit union partners to attract clients, and on Vigo to provide transfer services.

B. Where can the service be received?

Money can currently be sent to 41 countries including all of Latin America, Dominican Republic, Jamaica, Ukraine, Haiti, Philippines, India, Bangladesh, Australia, Canada, Great Britain, Germany, Poland, Spain, Kenya, Morocco, Nigeria, Ivory Coast and Ghana. Domestically, money can be received at over 1,500 locations in 29 states. Outside the U.S., WOCCU and Vigo will initially work to upgrade or expand the "receiving" network by offering IRnet services in developing countries where there are strong credit union movements and a large volume of remittance transfers.

In comparison to its direct and indirect competition, IRnet has the following strengths: credit unions are a trusted source for financial services; IRnet is convenient for consumers as an additional service offering from credit unions; it is priced below the competition; and IRnet has received tremendous political support. The weaknesses of IRnet are that it has neither the consumer awareness nor the depth of outreach of the competition.

Environment

The international remittance market and its current methods of transfer are thriving today because of the large immigrant population in the U.S. and other developed countries, along with the poor banking infrastructure that is available to handle these types of transfers. With the U.S. immigration population at its highest level in decades and political pressure to increase the level of immigration to the U.S., it is unlikely that a decrease in this influx will occur in the immediate future. However, the increased prevalence of ATMs and the Internet in developing countries endangers the existing methods of transfer if they do not adapt. Additional environmental risks are that credit unions generally cannot provide the sending service to non-members, and that credit unions must be aware of how to appropriately provide services to illegal immigrants.

III. WHAT IS (COULD BE) THE DEVELOPMENTAL IMPACT OF CREDIT UNIONS

Credit unions have been engaged in the IRnet service only over the past 18 months. While there is growing anecdotal evidence on credit union impact, thorough studies analyzing the developmental impact from the service have not yet been completed. The anecdotal evidence includes stories like that of Linda Ramos of East Los Angeles who, on a $200 transfer to Mexico for her mother-in-law, saved $25 by using credit union services. In addition, when Mrs. Salazar of El Salvador received money from her daughter Maritza in the U.S. at a local credit union in Santa Ana, she instantly became a member of the credit union where she received the funds. Mrs. Salazar now has access to savings, loans and insurance services that she did not have before.

While these stories, like the thousands of transformational stories regarding the impact of microfinance, successfully generate human interest, they do not tell us much about developmental impact on financial systems. Over the past year, there has been greater recognition of the role of credit unions in both microfinance and development (*Microbanking Bulletin* by Calmeadow, February 2000; *Safe Money* by the Inter-American Development Bank, 2000; *Credit Unions and the Poverty Challenge* by Bernd Balkenhol of the ILO, 1999; *CDO/PVO Microfinance Study* by Larry Frankel et al. for USAID, 1999).

In addition, development finance pioneers such as J.D. Von Pischke and Dale Adams have demonstrated the developmental impact of access to financial services (both credit and savings). The importance of sound financial systems to economic and social progress drives the work of central banks and the Bank for International Settlement to ensure safe and sound institutions. The role that credit unions and financial cooperatives play as essential sound financial systems is becoming better understood.

Recipients of remittances generally have low incomes and are discouraged from saving as a result of receiving funds at department stores (e.g., Electra stores in Mexico) or are not eligible to open accounts at the bank disbursing the funds. Research from western Mexico indicates that only 10 percent of remittances are used for investment and one percent for savings. Additionally, it is estimated that 63 percent of Mexico's population does not have an account at a financial institution. To the extent that receiving remittances at credit unions introduces individuals to financial institutions, this program will increase the culture of banking within the targeted countries and provide facilities for savings.

If remittances are received at sound formal financial institutions that allow and facilitate saving part of each remittance, as opposed to being distributed by commercial retail stores that encourage spending, individuals would be more likely to save. This inertia is often cited as a key determinant for where individuals maintain accounts.

IV. APPLICATIONS OF LESSONS LEARNED FROM MICROFINANCE TO REMITTANCES

Given that remittances sent or delivered by formal financial institutions will likely ensure greater access to financial services, should remittances be "channeled" to these institutions? According to Puri and Ritzema, with the exception of Korea, which has required the use of a specific facility as a condition of employment, Asian countries, including the Philippines, Bangladesh, Sri Lanka, India, Pakistan and Thailand, have not been able to successfully channel remittances. They failed even when financial incentives were offered.

On the surface, there are many similarities between the types of services and clients microfinance institutions (MFIs) work with and the recipients of remittance transfers. These similarities include:

- Small payment size
- Close relationships to people of modest means and the poor
- Broad networks, often in rural areas
- Access to informal financial services is provided
- Need for trust and one-on-one interaction

Before we determine that remittances should be sent through MFIs it would be useful to review the experience learned in microfinance. Some may argue with the outcome of these lessons; however, at forums such as the Microfinance Institute in Boulder, there is a growing consensus about these lessons. Listed below are five lessons that apply to remittance transfers:

MFI Experience 1: The operation can be sustainable if you are willing to charge the costs needed to cover all expenses.

Moral: Remittance services must be offered on a business basis. There can be a social impact only once during the process.

MFI Experience 2: Don't create the environment of untruths. In an effort to ensure loans were contributing to what was considered development, some MFIs would only provide loans for "productive" purposes. To obtain a loan that was needed but not deemed productive, individuals need to create untruths.

Moral: Be aware of creating incentive systems for remittance transfers that require the funds to be used for "productive" purposes.

MFI Experience 3: The most successful microfinance programs are the ones that serve various economic groups of people, and simultaneously meet their changing needs.

Moral: Transfer pricing isn't necessarily bad. Large remittances with higher fees can cross-subsidize lower fees for smaller transfers.

MFI Experience 4: Given the choice between a solidarity or an individual loan and social training as a condition of the loan or no social training, most people choose individual loans and no social training.

Moral: Create products that consumers, as opposed to donors and development specialists, want.

MFI Experience 5: Access to credit is not the same as access to financial services.

Moral: Narrowly focused remittance services by themselves do not meet the financial needs of individuals.

In addition to these lessons for the microfinance industry, WOCCU has learned the following lessons in the development of its service.

•There needs to be equal interest on both sides of the transaction;
•Financial standards of the sending and receiving entities are a prerequisite to ensure the safety and efficient payment of remittances;
•I believe the market is more competitive than microcredit; and
•Scale is everything in this business and a broad needed is essential.

V. CONCLUSION

From the outset, MFIs are likely to find that successfully providing remittance services will be more competitive than in the early days of microfinance. This process will require institutions to have networks and alliances in place to begin offering these services. While these challenges are formidable, there is tremendous opportunity to gain additional clients and help families combat the unsafe practices and/or usurious fees associated with the current options for sending money to friends or family back home.

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BIOGRAPHICA SKETCH
DAVID GRACE

David Grace is the Financial Services & Regulatory Manager of the World Council of Credit Unions, Inc. (WOCCU) since July 1998. Mr. Grace is responsible for WOCCU's regulatory monitoring and financial services including the development of the International Remittance Network (IRnet) service – a mechanism for credit unions to send money transfers to 41 countries. He represented the international credit union movement on Y2K at the Bank for International Settlements' External Consultative Committee. He oversees development of legislative tools for the international credit union movement and has led program activities with credit unions in the United States, Latin America, Caribbean, Asia and Africa. Mr. Grace has been deeply involved in credit unions role in remittances for the past four years.

From 1992 – 1998, he was with the Federal Reserve Bank of St. Louis managing its financial services and information technology units. In those capacities he worked directly with the President of the St. Louis Federal Reserve in his role as Chair of the Financial Services Policy Committee and Mr. Grace oversaw the FEDNET implementation for the Eighth District.

Mr. Grace holds a M.A. in International Affairs from Washington University in St. Louis; and graduated honors from St. Louis University with a B.S. in Economics and International Business. He has lived and studied in Italy and Spain and is fluent in English and Spanish.