THE RISE OF GLOBAL REMITTANCE ARCHITECTURE: A DEMAND [OR SUPPLY] DRIVEN PHENOMENON?

By

Amrita Sharma

Submitted to:

Department of Public Policy

Central European University, Budapest

In partial fulfillment of the requirements for obtaining the degree of

MASTER OF ARTS IN PUBLIC POLICY

Supervisor:

Thilo Daniel Bodenstein

Budapest, Hungary

2009

Abstract

In contrast to the pessimism of the 80s there is a 180 degree turn-around in the new migration discourse which finds remittances to be the ‘development mantra’ of the millennium. Pioneered by World Bank and supported by a mix of international financial institutions, NGOs and sending states, we witness rise of a new financial architecture comprising of norms, standards and dedicated agencies to manage remittances. The assertion is that greater financial inclusion of migrants would enhance the effectiveness of remittances. This study takes an in-depth look at this discourse and the assumptions behind it. We find that there is a greater agency element in the process than is being currently admitted. The process is triggered more by the supply of institutions than an expressed need of the market for institutions to address market failures. The writer argues that the current trend is problematic and puts undue burden on migration to finance development.

Acknowledgements

To Thilo Bodenstein, for his guidance and plentiful intelligent questions

To Karim Knio, for being a constant intellectual inspiration

To Heni, for being the 'oasis'

To Elona Xhaferri, Daniel Seth Shapiro, Mladen Joskic, Swati Kamble, Vivek Nemane, Bilal Aurangzeb, Karthik Nachiappan, David Stuart Short, Juan Carlos Trivino Salazar, Daniel Abreu, Tatiana Ticona and Sandhya Chandrasekharan - my best class-mates ever!

Last but not the least, to my family and fiancé for the never ending supply of love and support

Table of Contents

List of Tables & Figures

Acronyms

ATM	Automated Teller Machine
CFO	Commission on Filipino Overseas
CPSS	Committee on Payment and Settlement Systems
DFID	Department for International Development
FDI	Foreign Direct Investment
IOM	International Organization for Migration
MFI	Micro Finance Institution
MTO	Money Transfer Operators
ODA	Overseas Development Assistance
OWWA	Overseas Workers Welfare Association
POEA	Philippine Overseas Employment Administration
RSP	Remittance Service Providers
SPV	Special Purpose Vehicle

1. NEW GEOGRAPHIES OF FINANCIALIZATION[1]

The current financial crisis has brought back discussions on remittance financed development. There are concerns that the south would be hit worse by the crisis and one of the ways would be through reduced remittances. World Bank estimates project a drop of 5-8 per cent in global remittances in 2009 [The economic times, June 3rd, 2009]; and even countries such as India, which claimed resilience in remittance flows, are experiencing return of migrants [Press Trust of India, July 8, 2009]. This paper, however, is not about the crisis and its impact on remittances. It is about a related global phenomenon that has gone relatively unattended in academia – the creation of a global financial architecture at the back of remittances – a process, initially engineered by sending states and now legitimized and furthered by international organizations.[2]

Post G-8 summit of 2004 in Sea Island, there is a sudden activity across the world to tame remittances, make the infrastructure better and bring in order to the transfers. In 2007, the World Bank-CPSS brought out the General Principles for International Remittance Services which was endorsed by the G-8, the G-20, and the Financial Stability Forum. Since then the World Bank has been playing a pro-active role in popularizing the general principles across the globe. Creation of remittances prices database in 2008 was a significant milestone meant to enhance competition among players and lower the information asymmetry ailing the remittance industry. Along with the World Bank, the Basle Committee, Bank of International Settlements, the Inter-American Development Bank, DFID, and IOM have been active participants. From the private sector, several international banks have been active collaborators funding remittance markets studies, seminars and conferences at regional and global levels. Allegedly, these initiatives intend to support the workings of existing remittance industry by instituting standards, improving transparency, encouraging competition, and easing some of the stifling regulations which otherwise hamper its functioning. In addition to efficiency, the processes also promise to boost the developmental potential of remittances by promoting financial sector development in poor countries and financial inclusion of an erstwhile un-banked population.

[1] This title is inspired from Hudsons' "developing Geographies of Financialization" [2008]

[2] One important exception is Hudson, 2008

The paper looks at this euphoria over remittances as a source of development finance and aims to go beyond the rhetoric. The current narrative sees the rise of remittance institutions as evolutionary; correcting market failures and removing possible hurdles in free flow of capital. In our understanding, however, the creation of the gigantic infrastructure around remittances is nothing but another drive of financialization - characterized by increase in the coverage of the financial system to bring in more sources and untouched territories into the ambit of the international banking system. What we witness is a prolific growth in institutions, norms, standards and dedicated agencies for formalization of remittances at behest of international organizations and banks. We analyze the sudden need to bring in order within the remittance industry as driven more by supply forces i.e. creation of fresh institutional infrastructure for remittance banking and less a response to the market's demand, as is being currently professed. To advance this problematique, we raise two questions - one, how would formalization enhance the developmental potential of remittances; and two, what are the determinants of the onset and success of formalization – is it purely governed by economic/financial logic or are there other factors which play a greater role.

The biggest challenge the formalization effort faces in late-formalizing countries is to prove the advantage it has over the informal system. As per the rhetoric, formalization is expected to reduce the costs of remittance transfer increasing the average flows into developing countries. Further, a higher use of formal banking structures and securitization of future flows is expected to address capital scarcity, promote financial inclusion of the poor and boost financial sector development in countries of origin. Both the assertions find little support on ground. On the impact of increased flows, the literature remains inconclusive – whether it spurs economic growth or has a Dutch-disease effect on local economies curbing export competitiveness.[3] Early formalizers such as Philippines show that poor savings are often not the problem; the problem lies in stimulating domestic savings and getting the local multipliers in action. Many more such assumptions made by remittance-enthusiasts stand challenged in literature. For instance, the case of Philippines shows that the assumption of counter-cyclicality of remittances does not stand true and flows are vulnerable to economic cycles in migrant receiving states. Further, the case of Indonesia shows that the informal sector is more efficient and flexible than the formal and caters to the needs of migrants much better; and excessive attempts towards formalization may actually be counter-productive.

[3] For lack of first-hand data, we do not analyze the macro-economics of remittances in specific case studies and limit ourselves to review of existing secondary literature.

The existing remittance industry is characterized by high variation in degree of formalization across regions. There are early starters such as Philippines [way back in the 70s], late starters such as India with moderate success and, there are states which have gone back more fervently to informal methods after an initial period of experimentation such as Indonesia. This aspect of the industry has a lot to reveal and add to our understanding of how formalization works. How and when does it happen? What determines its progress and outcome? We look at three cases within Asia - Philippines with high level of formalization, India with moderate level of formalization and Indonesia where attempts to formalization have met with little success. The cases show that the onset and success of formalization of remittances does not depend as much on the economic and financial reasons, as is popularly understood; often other factors determine the onset, progress and performance of formalization – such as the interest of the sending state and the state-society relations. In both the Indian and Filipino case the trigger for formalization of remittances came from needs of economic and political survival of the state, whereas in the Indonesian case the external agents such as World Bank played the pioneering role.

The study concludes that there is a much stronger agency aspect in the current drive for formalization than is being admitted. In the name of formalization we witness a process of global remittance market creation by set of international organizations, banks and states. This current trend is problematic as it puts undue pressure on migration to finance development. There is limited evidence that concerted remittance management has led to sustainable economic growth in a region. In view of this, the chants of 'remittance as new development mantra' are anything but responsible. Further, in the current scenario of preponderance of undocumented/illegal migrants the formal financial system has little to offer. The focus of international financial system should be more on adapting migrant's interests into devising better systems rather than drawing in migrants into the ambit of financial capitalism on unfounded optimism.

.

1.1 Proposed Methodology

The research is qualitative in nature and relies primarily on use of secondary literature. Apart from published articles and books, the documents used for the study cover World Bank studies, Inter-American Development Bank reports and working papers, Asian Development

Bank reports, DFID funded project reports, and remittance market studies sponsored by private international banks. Given that the phenomenon under study is recent, the analysis available on the subject is more in the grey, unpublished domain. Thus, the study makes use of a number of discussion papers, global seminar proceedings, working papers and papers presented at conferences and seminars on remittance and development. The primary literature used for the study is limited to newspaper articles and magazines such as ‘the Economist’. The theoretical framework used in the thesis comes from the critical international political economy literature and their work on financialization.

1.2 Relevance to Public Policy

Migration is one of the biggest challenges for international public policy. In the last two decades a variety of factors have added to the exigency of addressing it in a comprehensive fashion – security concerns after 9/11 attacks, rise in number of people seeking asylum and refugee status and finally the need to strengthen the links between migration and development. Despite plentiful conventions and norms management of migration at the global level has been a policy nightmare with the reasons for their non-performance ranging from compliance issues to problems in design. This study looks at one such attempt to improve governance of remittances at the global level and aims to highlight the lacunae.

1.3 Proposed Chapter Plan

Chapter 2 presents the problematique and describes the extant remittance infrastructure and the recent rise of formalization across the globe. Chapter 3 spells out the theoretical approach guiding the study and looks deeper into the rhetoric. The aim is to shed light on - how would formalization lead to better utilization of remittances? Chapter 4 covers the cases of Philippines, India and Indonesia to reflect on the question what determines the onset, progress and outcome of formalization. Chapter 5 concludes the study.

2. REMITTANCE MARKETS - THE SUDDEN NEED FOR ORDER

In the newly emerging pro-remittance discourse, remittances are hailed as good source of development finance because of several reasons – they are counter-cyclical, reach the target better than other sources and are predictable [Ratha, 2004; Oroczo, 2008]. Remittances are claimed to be a more stable source of foreign capital vis-à-vis FDI and ODA and are also more evenly distributed among developing countries than other capital flows [Hernandez-Coss et al, 2008]. From 1995 to 2007, global remittances are estimated to have risen from 102 billion USD to 337 billion [IOM, 2008]. Notably, the efforts to formalize transfer of remittances through international banking channels have also gained momentum in the last one and a half decade; a period which corresponds with the steep rise in global remittances.

This chapter looks at the prevailing financial infrastructure for remittances and presents an overview of attempts to modify it with help of new institutions. What we witness is the creation of a global remittance market run by unified norms like the General Principle for International Remittance Services at the behest of international organizations such as the World Bank and other international financial institutions.

2.1 The Extant Remittance Industry

In 2007, global remittances touched 337 billion USD and out of this amount, 251 billion USD went to the developing countries [IOM, 2008]. A break up the flows showed that India, China, Mexico and Philippines accounted for a giant share of this money. The flows largely originate from the US and the UK and since early 90s they have diversified to include more western European countries such as Germany, France, Netherlands, and Italy. Notably, this amount covers only the formal flow of remittances. A large part of remittances flow through the informal channels which are not accounted in the estimates of central banks.

At the global level, it is difficult to tell the share of the formal sector in the remittance industry. Some researchers put it at 50 per cent of the overall market [Hernandez-Coss et al, 2008], which is a broad guesstimate. A recent survey of central banks carried out by World Bank showed that in most cases, except for few Latin American and Caribbean countries, the central banks were not even aware of their market share – an indication of the poor comprehension of the remittance industry by formal authorities [Martinez, 2005]. The use of formal methods is also highly variable. In an attempt to compare countries globally, a UK based study found that the share of traditional transfer methods is low in case of the Philippines, moderate in case of India and Turkey while it fell in the high and very high category for other South Asian states such as Bangladesh, Sri Lanka and Pakistan [DFID, 2005].

Table 1: Formal vs. Informal Methods of transfer [Source: Passas, 2004]

Formal	Informal
10-20 per cent cost	0-1.5% cost
Service to main cities	Service to remote areas
Detailed records kept	Minimal/no records
Receipt to sender	No receipts to sender
CTR, SAR etc. filed	No reporting to authority
Collection and delivery at agency premises	At home pick-up and delivery service
Transfer in days/weeks	Transfer in hours
Agency specialized in money services	IVTS mixed with other business

Passas [2004] names the informal service providers as the 'informal value transfer systems' many of which have existed since centuries, pre-date the formal banking system and are largely legitimate. The examples are the *Hundi* and *Hawala* system prevalent in South Asia, *Fei Ch'ien* [flying money] in China, *Guanxi* in China, *Phone Kuan* in Thailand, 'door-to-door' in Philippines etc [ibid] . These traditional transfers are characterized by personal connections and thrive on language advantages, low operating costs, wide outreach and trust. Passas [2004] does a comparison of the formal and informal remittance service provision methods and finds that the informal service providers fare much better on numerous fronts [Table 1]. The benefits they enjoy is lower operational costs as they are able to mix other activities with this service plus they do not have to comply formal regulations. The informal providers are able to cut down on numerous bureaucratic formalities as they do not issue receipts nor maintain records of transactions. This poses great risks but Passas [2003] in his study of Hawala systems reports that he did not come across a single instance of fraud. Instructions are passed on using wide variety of medium such as telephones, e-mail, or fax. They have a much wider coverage compared to banks and consumers find it much more convenient as money is collected from and delivered at home. Often, unskilled migrants who would be intimidated with the formalities of banks find doing business with informal service providers much easier.

Post 90s, however, two developments have had a detrimental impact on the informal sector – financial liberalization across developing countries and 9/11 attacks after which these systems have come under heavy scrutiny as possible hubs of money laundering and terrorism-financing. Nevertheless, in many regions customers still express high degree of satisfaction with the informal sector options – both in terms of efficiency and service orientation [DFID, 2005]. In addition to the benefits mentioned above, what makes informal systems more appealing to the migrants is the guarantee of anonymity. Given that in last two decades the number of undocumented migrants has risen, the promise of anonymity by the informal system is likely to increase its stronghold on the market.

Unlike the informal sector which is comprised of individuals, private services of the kind of *Hawala* and the black market, the formal remittance systems involves the large, global service providers such as Western Union, international and local banks and non-banking financial institutions such as currency exchangers. In 2002, the biggest service provider i.e. Western Union was found to have only 12 per cent of market share while money gram had a share of 3 per cent [IMF, 2002 cited in Frisch, 2004].

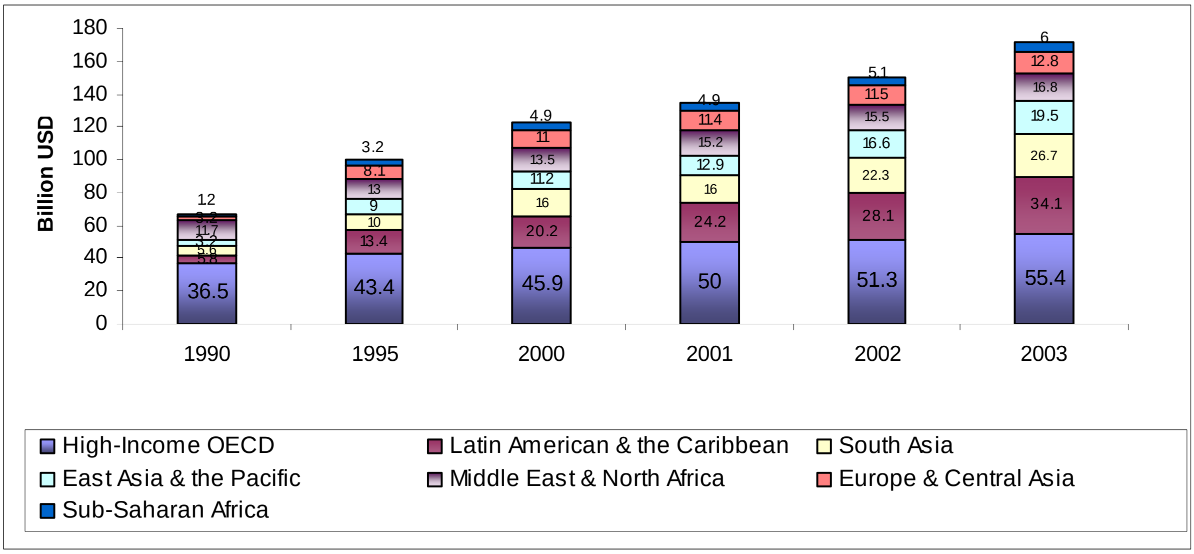
The high degree of informalization is seen as a business opportunity. Lately, the industry has attracted a variety of new-age remittance service providers [RSPs] with sophisticated technological options such as ATM and card-based transfers. This has led to proliferation of available channels of transfer and financial products and services that can be attached to remittances in the market. Much of this development has happened in Latin American countries at behest of large inter-continental banks and inter-American Development Bank. The process is now expanding to include other major migrant sending and poor economies further east.

2.2 The Global Drive to Formalization

It is difficult to pin-point when formalization of remittance transfers gained force in public policy. There were efforts to manage migration as early as 1950s in the case of Spanish

Instituto Espanol de Emigracion and later one of the most celebrated case of the Philippines starting in 1970s [Siracusa and Acacio, 2004]. The phenomenon, however, became more widespread in the 1990s, when both the number of international migrants and remittances grew in an unprecedented manner. Figure 1 gives a corresponding picture of a rise in flows of remittances globally.

Figure 1: Rise in global remittances



Source: HalehBridi, 2005

As part of the formalization drive, a variety of incentive mechanisms were instituted by banks to attract migrant remittances world-over such as special savings accounts for migrants, higher interest rates on savings, tax breaks, and accessible financial services. Countries such as Mexico, Philippines, Colombia, Turkey and India became leading examples for forging links between financial institutions at home and migrant destinations. Philippines, for example, negotiated a memorandum of understanding with USA for reduction in remittance transfer fees and for an improved connectivity of payment systems. Through concerted efforts, the Mexican government also persuaded American authorities to ratify the *matricula consular*, by virtue of which even the illegal migrants could use the formal banking channels [Martinez, 2005]. To attract more and more remittances, certain governments came up with a matching grants system, for example in Mexico for every one dollar of remittance the government promised 3 dollar worth of investment. Along with measures to strengthen remittance retail, financial institutions in certain countries such as El Salvador, Turkey, Brazil and Mexico took steps towards securitization of remittances flows using them as collateral, issuing new debts and raising additional capital [Martinez, 2005].

What is notable is that till early 2000s the effort was limited to certain major migrant sending countries such as Mexico, Philippines, Colombia, Turkey, India etc. These countries forged links between financial institutions at home and migrant destinations and negotiated deals for their migrants on a bilateral basis. At the turn of the current decade, however, with the participation of international organizations such as World Bank, the formalization drive gained much greater momentum and became widespread moving out to untouched quarters; for instance, a number of foreign banks moving into the untapped markets of Eastern Europe. Karafolas and Sariannidis [2008] present the case of Albania where a number of Greek and Italian banks have moved in to manage remittance money. The author argues that the growth of figures on remittances flowing through formal channels is related to the proliferation of Greek and Italian bank branches within the country [ibid]. In 2008, a World Bank team helped the finance ministry of Czech Republic to help apply the general principles and carry out surveys to understand the national remittance market. Similar initiatives were carried out in Uganda and Morocco in the same year. In the last 12 years, the World Bank has helped more than 100 countries in instituting payment system reforms in their financial systems. The focus of these initiatives has been on developing certain public goods which would lead to creation of a global remittance market with higher transparency, less information asymmetry, greater accountability and smarter regulations.

2.3 Creation of Global Public Goods around Remittances

The key emphasis of the international organizations involved in remittance market creation is on developing the ‘payment system aspects’ of remittances [World Bank, 2008]. As per the current diagnosis, several factors hinder the efficient flow of remittances – ill-developed financial system in countries of origin, high transaction costs, long processing period, and stifling regulations which deter migrants from accessing formal remittance services [World Bank, 2008]. In order to address these Financial Market Integrity group at the World Bank along with the Bank of International Settlements, Inter-American Development Bank, ADB, DFID, and several other key stakeholders in the private sector have taken concerted steps.

A pioneering initiative in cost reduction strategy was DFID's 'send money home' program which allowed comparison of rates charged by different RSPs on a website [www.sendmoneyhome.org]. It also encouraged financial literacy among migrants teaching them on how to open and operate bank accounts, choose financial instruments for better savings and investment. The DFID initiative met with success and was emulated by other governments who started similar websites – envoidargent in France, geldtransfair in Germany, geldnaarhuis in the Netherlands etc. In 2008, the World Bank created the remittance prices database which allows comparison across all major remittance corridors.

One of the most significant contributions came in the form of creation of norms for the remittance industry that would apply globally. In 2004, the World Bank along with the Committee on Payment and Settlement Systems [CPSS] came up with the General Principles guiding international remittance business. The principles revolve around 5 key areas [World Bank, 2007, p.] –

- Creation of greater transparency and institution of consumer protection mechanisms in remittance markets
- Improvement in the international payment system infrastructure to enhance overall efficiency
- Improvement in the legal and regulatory environment by promoting "soundness, predictability, non-discrimination and proportionality" [World Bank, 2007, p. 23]
- Creation of competitive market structure with special emphasis on improving payment infrastructure in origin countries
- Provision of improved governance and risk management practices

For implementation of these principles a public-private partnership was created in 2008 in Vienna during the Global payments week. World Bank has dedicated groups to support the remittance-development agenda – the Migration and remittances team involved in research and forecasting of migrant and remittance flows, the Financial Integrity group to advise of regulations and the Consultative Group to Assist the Poor which ties up micro-finance with remittance management. The assumption behind all these initiatives is that improving the payment system aspects will subsequently enhance the impact remittances have in stirring development.

2.4 Remittances, Development and the Neo-Liberal Paradigm

In wake of the current crisis, the efforts for managing remittances are gaining fresh credibility. In the recent G-8 meeting in Rome, Italian foreign minister Franco Frattini named the efforts as an 'innovative financing strategy' for the global south in the wake of the global crisis [The economic times, June 12th, 2009]. Analysts claimed that halving the costs of transfer could result into an extra 12 to 15 billion USD for development of the global south [ibid]. When looked at in depth, much of the narrative around remittance management – efficiency, transparency, competition, accountability etc. is a reflection of the dominant neo-liberal development paradigm. Remittance management is becoming a wheel which is helping and being helped by financial liberalization across the world - creasing out all the inconsistencies and hurdles that might obstruct the smooth flow of capital across borders. The way the logic is presented, the activity of the market and the international response to correct possible sources of market failure appear as instances of self-organization where the markets being the 'complex adaptive systems' are only heeding to the demands made by the remittance industry. The current order in remittance markets is "spontaneous or emergent and is a result of human action and not execution of human design" [Markose, 2003, p.2]. And, the role that the international organizations play is only to correct market failures and enable smooth functioning of the industry.

There are, however, certain facts which help us go beyond this narrative. The current bail-out packages offered by governments to save sinking banks makes the magnitude of the remittances i.e. 337 billion USD look rather insignificant. This comparison is helpful in putting things in perspective and look at the broader global development finance dynamics. Hudson [2008] speaks of the similarities between the micro-finance story and the remittance story - both being part of the crisis management strategy of failed development in the world run by neo-liberal prescriptions [ibid]. In our view, the creation of gigantic financial paraphernalia around remittances with limited evidence of its impact lends greater credence to this thesis.

2.5 Chapter Summary

A large part of the pro-remittance discourse revolves around the benefits that formalization would bring to the poor migrants and their families. Apart from bringing in efficiency and transparency, international banks along with the World Bank has also pitched the initiative as a measure of enhancing financial inclusion - an erstwhile population untouched by formal banking services would be able to utilize sophisticated financial services offered by banks and benefit from it. Unlike the rhetoric, however, we take the view that the current developments mark the inclusion of remittances into the ambit of financial capitalism. Hudson [2008, p.317] describes the logic of financialization as one where there is a continuous search “to find new income streams that can be securitized”. The case of remittance management appears to be yet another example of the same. In the next chapter we probe deeper into these debates.

3. THE SCIENCE BEHIND REMITTANCE MANAGEMENT

Drawing from the discussion in the previous chapter, we can say that there are essentially four things that are happening in the name of formalization of remittances - [1] concerted efforts to channel remittances through formal financial institutions, [2] construction of regulatory mechanisms around transfer of remittances, [3] incorporation of remittance multipliers such as securitization into formal banking channels, and [4] efforts to improve data on remittance flows. How do these efforts aim to enhance or unleash the development potential of remittances? What are the key assumptions behind these efforts? What does the orthodox economic theory predict about the impact of these efforts? And, what does the heterodoxy have to offer and add to the discourse? In this chapter we shall look in depth at the driving logic behind the formalization exercise and consider both its economics and politics, in detail.

3.1 How is Formalization expected to help?

Hudson [2008] divides the current formalization effort by banks into two broad categories – one, aimed at expanding the retail outreach so as to cover more remittances and bring them into the financial mainstream and two, leveraging the cash flows and generating more capital through securitization. Under the first category the key intervention has been reduction in the costs of transfer of remittances. Cost of transfer has been a key disadvantage faced by the formal financial institutions vis-à-vis the informal. A comparison reveals that while remitters paid 0-1.5 per cent of the remitted amount using the informal system, use of formal channels costed them 10-20 per cent of the sum [Passas, 2004]. Research shows that cost of transfer is also the key criterion in choice of a remittance service provider [World Bank, 2007]. No doubt, most non-governmental organizations, international organizations and financial institutions have focused on bringing these costs down to attract remitters. This has been achieved by making the prevailing rates offered by different RSPs available on the worldwide-web and allowing consumers to compare prices. These efforts help in reducing information asymmetry and encourage competition by giving customers a greater number of options.

Another way in which financial institutions have tried to extend their retail outreach is by forging links with Micro Finance Institutions [MFIs]. MFIs complement the banks as they are often present in places where banks fail to reach [Fritz et al, 2008]. The authors argue that for an improved access of banking system and financial services MFIs are a 'pre-requisite' as they are known to have greater access to the poor and over the years have developed the expertise of pooling and leveraging small amounts of money. MFIs also gain in this tie-up as many MFIs are not authorized to deal with foreign exchange and a tie-up with authorized dealers helps them actively engage in international transfers [ibid, p.10]. This tie-up between the financial institutions, migrants and MFIs is proposed as a win-win solution where the FIs gain from greater access to hard cash and more clients and migrants benefits from their financial aptitude and savvy money management abilities. It is worth mentioning here that cost reduction apart from a client-attraction strategy is proposed to increase the aggregate levels of remittance flows – it is assumed that if the costs are lowered, migrants will be induced to remit more. This, however, remains to be tested.

Further, when it comes to leveraging the remittances and enhance their growth potential, banks are again seen in a better position in comparison to the MTOs or the informal service providers. Banks are able to attach a broad portfolio of financial services to remittance transfer services [Alberloa and Salvado 2006, cited in Avila and Schlarb, 2008]. One of the ways banks offer to multiply the benefits from remittances is through securitization. The future flows are pledged to a Special Purpose Vehicle [SPV] based outside the country of origin which issues debt based on the same [Ketka and Ratha, 2001, cited in Hudson 2008, p. 327]. After the money is pledged the collection of the remittances and payments to the investors is coordinated by this SPV. The authors point that securitizing remittances helps banks overcome the 'sovereign risk' i.e. the fear of 'governments defaulting on their loans unilaterally' [ibid, p.327]. Because, the remittances never enter the country once pledged to the SPV, often these instruments get a higher rating i.e. investment grade when the rating of the country could be 'sub-investment grade' [ibid]. As a result, the issuers of remittance-securities are able to raise more money in the international capital markets. Mexico was the first country to implement securitization, way back in 1994. Reportedly, between 1994 and 2004 the value of securities issued using remittances as collateral increased more than 40 times in the region [World Bank 2006, p. 103 cited in Hudson, 2008 p. 327].

To sum up, the impact of the formalization efforts runs in an indirect fashion i.e. it is a two-step process. First, formalization is expected to have a positive impact on financial sector development of countries as migrant households get integrated into the financial system and avail more financial services [Aggrawal et al, 2006; Avila and Schlarb, 2008, Fritz et al, 2008]. The financial sector development, in turn, is expected to have a positive effect on the economy by helping overcome credit market failures, fostering growth and reducing poverty [Aggrawal et al, 2006]. Developing economies are known to suffer from poorly developed financial markets and low degree of monetization [Fritz et al, 2008]. A significant part of the population works outside the ambit of the financial system unable to access credit and suffers from low productivity[4] [ibid]. Terry et al [2005, p.391] offer that remittances can be the 'point of entry' into the formal financial system for the poor giving them a plethora of financial products such as loans for housing and other consumer goods, mortgages, insurance and pension plans. This chain of effects, however, is not as smooth as surmised. In the following sub-sections we review the existing theoretical and empirical literature on remittances and its impact on growth and development. We first look at the literature on remittances and economic growth and then extend some of its arguments to the impact of its formalization on stimulating growth.

3.2 Remittances and Orthodox Economics

The old standard macro-economic approach has dealt with remittances as part of international transfers and treated its impact on aggregate expenditure, domestic savings and national output accordingly. As remittances flow into an economy both expenditure and savings tend to increase. Higher savings are expected to cause increased availability of resources which further lead to reduced domestic interest rates, thus inducing investment. This, however, is the most stereotyped model of how remittances would work.

In modern analysis, the impact of remittances on the economy is divided into short-run and long-run impact. In the short run, the studies focus on impact of remittances on exchange rates, domestic interest rates, and domestic savings. One debate that has occupied this field is - whether remittances have a 'Dutch disease' effect on the economy or lend positive growth stimulus to capital-starved economies [Loser et al, 2006]. A bulk inflow of remittances, like other sources of international capital flow, causes appreciation of the real exchange rate

[4] Fritz et al [2008] also point out that a weak domestic financial market causes entrepreneurs to resort to loans in foreign currency and broad based borrowing of this kind often exacerbates the current account deficits of developing countries. In order to overcome indebtedness, these countries have to go through frequent depreciation of their domestic currency and such changes often stifles entrepreneurship locally [ibid].

hurting its competitiveness in the international arena. Lopez and Olmedo [2005] point out that this is similar to the classic 'transfer problem' where a sudden inflow of remittances may initially improve the terms of trade and overall welfare but affect the export competitiveness of the country adversely. The exchange rate regime followed by a country can reduce or exaggerate the impact. For instance, the authors also find that within fixed exchange rate regimes the impact of remittances is muted vis-à-vis floating rate regimes; latter having a remittance-exports elasticity of minus 0.5 [ibid].

Among other effects, remittances held in banks in foreign currency can be a cause of concern. Fritz et al [2008] point out that in many developing countries because of lower faith in the local currency citizens often prefer an international currency and once a foreign currency gains weight in local monetary transactions the trend becomes difficult to reverse. This phenomenon visible in Latin American countries called 'dollarisation' of the economy has serious adverse consequences. As a result of 'dollarisation' central banks do not have the same amount of control on the money in circulation and can loose their grip on an important macro-economic instrument i.e. the monetary policy. Though against the rationality of individual migrants, who would prefer to keep their savings in foreign currency for lack of faith in their domestic currency, good macro-economic health would require otherwise and is a policy concern [ibid].

In the long run models, the impact of remittances is analyzed in terms of its impact on productivity and inequality in the economies of origin countries. Study by Chami et al [cited in Rapoport and Docquier, 2005] shows that under asymmetric information remittances are likely to have a negative impact on growth in origin countries. The impact on inequality, however, is ambiguous [ibid]. While some empirical studies show that remittances have a trickle down impact and stimulate local economies [Mendola, 2006], other have shown that benefits from remittances are limited to a few exacerbating inequalities within a region [Hoddinott, 1994 cited in Rapoport and Docquier, 2005; Saith, 2001]. Most policy studies focus on the short term dynamics of remittances with the aim to design adequate monetary and fiscal policies to obviate the adverse impact and strengthen the positive effects. When considering the impact of formalization, we too limit ourselves to the short run dynamics.

The leading assumption behind formalization is that it would boost the savings available in an economy for investment and help stimulate the remittance multipliers in action[5]. An emphasis of the remittances-savings story is that money will be accessible to the entrepreneurs and used where it earns highest possible returns. In many developing countries most of migrant savings go into purchase of land and houses, which is not considered the best way to mobilize savings [Ratha, 2004]. In a standard neo-classical fashion, higher savings is equalized with higher prospects for growth and higher per capita income [Fritz et al, 2008]. This assumption stands challenged on ground. One striking case is that of Kerala, India where large amount of remittances lying in savings accounts remain under-utilized. The economy faces a problem of converting its high rate of savings into productive investment and employment [Kannan and Hari, 2002]. In addition, the state level public sector enterprises have also failed to attract any funds because of low efficiency and poor credibility. Saith [1991] showed that despite the boom in the construction sector, the Kerala economy failed to capitalize on the boom and money flew out of the state. Mobilizing these savings has been an intractable problem for policy-makers. Evidently, there is a gap between the influx of remittances and its growth-inducing utilization, and it is not clear how the formalization efforts would help correct it.

When considering the impact of formalization, it is again helpful to differentiate the macro-economic from the micro-economic impact. One of the immediate outcomes of formalization is better accounting of remittance flows, which show in the balance sheets of the central banks and the government. It is known through experience that remittances have helped governments tide through balance of payment problems and improved their trade deficit [World Bank, 2007]. This in turn has helped economies in improving their credit rating making them more credit worthy in international capital markets. The impact at the micro-level, however, is not that apparent. Economists such as Ratha [2004] offer that financial inclusion of poor migrant households would help them avail financial instruments and reap benefits of a sophisticated financial system. This, however, is quite far-fetched an idea. Experiences in Mexico in introduction of card-based systems of remittance transfer shows that migrants are apprehensive of using techniques they do not quite comprehend [Oroczo et al, 2007]. Much of the securitization and leveraging proposed around remittances suffers from similar limitations. Migrants unable to understand the finer workings of the leveraging

[5] One notable and positive aspect of remittances as a source of foreign finance is that the multiplier effects are more pronounced compared to other sources of foreign exchange. The reason being that the money goes to the lowest strata of the society which generally has a higher than average propensity to consume.

performed by financial institutions and would be averse to invest. The current financial crisis emboldens such fears and casts serious doubts on future of securitization of remittances.

In the drive to include the migrants into the financial system one has forgotten to ask and seriously reflect on why is financial inclusion of the poor migrants important. What does the formal system have to offer to them? In considering the prospects of remittance formalization a look at micro-finance story is insightful. When started, the aim was to overcome the capital access problem of the poor and get them out of the traps of exploitative money lenders. The formal system involved high transaction costs and could not afford to service poor clients in need of small loans. The initiative has assumed gigantic proportions now and has been recognized globally recognized as a watershed development initiative, especially after the awarding of Nobel Peace Prize to Mohd. Yunus. After more than two decades of global micro-finance drive, however, one is not able to argue convincingly about the impact it has had on Bangladesh's development, where the idea was born, let alone the countries where it was adopted. It is revealing that the largest industry of Bangladesh is 'development' and not surprisingly microfinance forms the biggest chunk of it [personal comm.[6]]. Arguably, the remittance mantra is not very different from micro-finance; both are responses to a failed development mission. Both have become the poster-child of academicians and practitioners [micro-finance more than remittances] and thrive on financializing the poor and drawing them into the ambit of financial capitalism [Hudson, 2008, p. 317].

3.3 Voice of the Heterodoxy: The Political-Economy of Remittances

Notably, much of the remittance discourse prompting formalization chooses to turn a blind eye to the political aspects of the phenomenon. The public-policy driven accounts only focus on learning from successful initiatives what they term as 'best practices' and replicating them world over; World Bank playing a key role in collating these practices, disseminating them, and also operationalizing them wherever needed. Much of the lessons come from the advance migration-managers such as Mexico or Philippines. No doubt, these initiatives have met with little success [Hudson, 2008]. The critical international political economy literature which lies at back of the financialization argument, adds a fresh and revealing perspective to the current discourse. It offers an incisive critique to the rhetoric and forces one to look deeper; go back

[6] Personal Communication with Anirban Das Gupta, Lecturer, Poverty Studies, Institute of Social Studies, 30th May, 2009

and investigate the processes that have led to creation and then perpetuation of migrant flows, and by extension the remittance flows.

Financialization has been one of the key aspects of globalization in the 21st century. Frieden [1995] defines financialization as a process wherein volume of capital movement surpasses trade in goods and services. It has meant increasing integration of financial markets across the globe, triggered and emboldened by changes in technology and deregulation [ibid]. The process created a need for multiple institutions and Lordon [2001, cited in Pineault, 2001] observes that since 1970s there have been significant institutional changes helping the dominance of finance capital over industrial or commercial capital[7]. And, with time the process has developed a life of its own. The critics of the financialization process argue that the financial world has become quite detached from the real economy and is almost 'self referential' [Hudson, 2008]. One visible characteristic of the process is its constant look out for newer sources of finance –

"Financial capitalism is dependent on the constant searching out, or the construction of, new asset streams, usually through a process of aggregation, which then – and only then – allows speculation to take place."

- Leyson and Thrift [2008 cited in Hudson, 2008]

Hudson [2008, p.315] argues that the financialization of remittances is driven by similar needs to rope in a fresh source of capital, previously untouched and "bring them into the global development architecture". It is a desperate attempt to weather the drop in development finance and arguably find newer sources to fund the millennium development goals, the ever-evading development chimera [ibid]. Similarly, Raghuram [2009] in her study "which migration, what development" calls remittances the 'lodestar' around which a whole remittance development industry is being formed.

As per the analysis of this school, the political agency aspect is often much more important than the financial logic in driving the whole phenomenon. Beginning with states, the process

[7] Pineault [2001] traces the movement of scholarship on financialization and points out that starting with Rudolph Hilferding, a Marxist, the study of the economic institutions dealing with finance capital benefited increasingly from a heterodox economists Veblen, Keynes and Minsky. The regulation school theorists, recently, have been one of leading contributors to the institutional analysis of financial systems highlighting the politics behind it; this stream has been termed critical institutionalist macro-economics.

has come to involve a large number of non-state actors such as NGOs and international organizations all working to strengthen and perpetuate the process in their unique capacities. One notable aspect of the financialization of remittances is the creation of a strong narrative, eulogizing remittances as a source of development finance - counter-cyclical nature, magnitude surpassing FDI, excellent targeting and such. The international institutions have played a leading role in creation of this narrative. There are doubts, however, if the increase shown in remittances is real or a result of greater/better accounting. Fritz et al [2008, p.2] point out that the official figures about the increase in remittances could be misleading as a part of it is due to a shift from the informal to the formal system.

For the states, remittance management comes as a smarter option vis-à-vis promoting or curtailing migration openly as it is more politically palatable [Cordova-Lopez, 2006]. It needs to be noticed how in recent times there is a fresh impetus on research for better utilization of remittances all funded by government-backed development agencies and foreign in the key migrant receiving countries, take for example the migration and development programme at University of Maastricht funded by department of foreign affairs. One can look at it as complementary strategies to dissuading immigration [by helping the local economy of the origin utilize remittances better]; a strategy which is more politically correct than blatant protectionism. For the sending states, the motivation is more than clear as it helps them in service foreign debts, maintain a healthy trade balance and improve their credit rating in international markets.

"Temporary migration, far from bing inconsequential because of the eventual return of the migarnt, is transforming the boundaries of sending states, altering the calculus of state policy makers, and serving as a vital source of the external finance necessary for servicing debt and imported oil."

- Rupert and Solomon, 2006

An important explanation to the wave of formalization also comes from security concerns rising especially after the 9/11 attacks on USA. The informal networks of money transfers especially the *Hawala* system prevalent in South Asia came into heavy surveillance for being possible havens of money laundering and terrorism financing. Passas [2003], however, notes that there is good amount of evidence now that much of the money used was transferred through formal channels.

Old migration literature is replete with critique of remittance-led growth mostly focusing on its non-sustainable nature. There is limited evidence of positive impact of migration on sustained economic development. For instance, Castles [2007a, p.14] points out that the case of Mexico shows that how both remittances and *maquiladoras* only deepened the dependence of the country on USA without bringing out any 'genuine development'. Among the major migrant sending countries, Turkey is the only one to have achieved good level of economic development but scholars doubt that this development was due to better remittance or migration management. Castles [2007a] points out that the failure of Turkey to harness remittances during the 1970s and 1980s for industrial growth is well documented and casts serious doubts on the efficacy of remittance-led growth discourse.

Back in 80s and till mid-90s the public policy emphasis was on curtailing migration as it was seen as a symptom of underdevelopment. Authors such as Castles [2007b] called it 'trickle down economics' and revival of the modernization theories. That view too was ridden with problems as it led scholars to vigorously promote 'stay at home' policies and denied laborers right to movement for livelihood. Beginning 2000s, however, there is a massive turnaround in the same migration literature; pioneered by the international organizations, primarily the World Bank. A plethora of studies are being carried out and publicized showing the impact of remittances on financial development. This movement from one end to the other is revealing and brings out the strong agency element in the migration discourse.

3.4 Chapter Summary

This overview of factors discussed in the literature indicates that the ingredients and drivers of formalization process are way more nuanced than initially understood. There is a strong political-economy dimension behind the process which is being erroneously ignored. In the next chapter we bring the experiences of three countries to show how the political often dominates the economics.

4. DIFFERENT FOLKS, DIFFERENT STROKES: THE CASE OF PHILIPPINES, INDIA AND INDONESIA

One of the notable features of the global remittance market is high variance in the level of formalization of remittances; at times, there are stark differences within a region. While remittance management is much advanced in the Latin American and Caribbean region, it is at a nascent stage in Central and Eastern Europe and many countries in the African continent. In the East Asian region, for Philippines, more than 80 per cent of remittances flow through formal banking channels, whereas, in Indonesia the informal RSPs dominate the market [IOM, 2008]. The immediate question that follows is - what determines the level of formalization of remittance transfers?

Often, the explanation tends to be economic – for instance, the share that remittances have in the overall GDP of the receiving country. This is a dominant myth. If we compare India, Philippines and Mexico we find that the share of remittances in GDP is 3.0, 11.8 and 1.7 % respectively [Goldring, 2001]. It is notable that while the share of remittances in overall GDP is low for Mexico, it is way advanced than India and several other countries in LAC, Central and Eastern Europe and African countries where remittances account for more than 10 % of the GDP [Raghuram, 2009].[8] In this chapter we take three cases for analyses based on their levels of formalization and measure of success - Philippines, India and Indonesia. Philippines, is considered to be much advanced in management of remittances. India is known to be a late formalizer with moderate level of success while Indonesia is infamous for the speed with which it has gone back to the informal methods of remittance service provision. At different levels of formalization the cases provide a good contrast and help highlight important determinants of formalization and its success. We find that migration and remittance management has largely been a state-driven process, determined more by the financial and political needs of the ruling government than the needs of the market, forget the poor migrants. The case of Philippines, the earliest among the formalizers, is also illustrative in showing the limitations of remittance-led development.

[8] The high level of formalization in Mexico is considered to be an outcome of host of political-economic factors - US government's interests in streamlining the influx of immigrants, business interests of American banks in capturing the remittance market [it should not come as a surprise that the key remittance service providers are all American in origin, such as the Western Union Bank], the advent of neo-liberal policies of the 1980s and Vicente Fox's pro-Diaspora rhetoric after which the process of remittance formalization jump-started [Rupert and Solomon, 2005].

4.1 Philippines

Philippines is the 4th largest remittance receiver after India, China and Mexico; the migrant population accounts for 10 per cent of the total population and remittances make up to 11.8 per cent of national GDP. It is also the pet-case of remittance-enthusiasts as a "paradigmatic example of state-driven policy of generating remittance finance through a determined state policy" [Rupert and Solomon, 2005, p. 87]. The two authors also point out that "no other country comes close to the same level of state involvement" [ibid, p.87]. Once dominated by private RSPs [Siracusa and Acacio, 2004] now more than 80 per cent of the remittances coming to the Philippines flow through the formal channels. This money has been crucial to maintenance of the macro-economic health of the economy. Nonetheless, there is considerable dissent on the impact formalization has had on economic development in Philippines [Saith, 2001; Castles, 2007a].

Beginning 1970s, a comprehensive institutional set-up was devised by the Filipino state for management of migration. Under this scheme, the OWWA [Overseas Workers Welfare Association], CFO [Commission on Filipino Overseas] and later the POEA [Philippine Overseas Employment Administration] were created. The OWWA was meant for the welfare of the families of the migrants and received contribution from migrants and the government. The CFO was created to ensure welfare of the migrant workers. Finally, in 1982, the POEA evolved as a comprehensive programme tying a number of activities under one umbrella. Under this programme migrants were provided induction, helped with documentation and pre-migration orientation courses; all under the supervision of ministry of Labor. Apart from these a number of legislations, Acts and policies were formulated to ensure safety of migrants abroad and streamline and leverage remittance flows. Philippines also became known for being one of the first countries for felicitating its Diaspora organizing 'migrant worker days' and calling them national heroes; providing special right to migrants such as reduction in import duties; and organizing beauty contests meant specially for the Diaspora namely 'miss overseas Philippines' [Castles, 2007a].

The trigger for this systematic labor-export infrastructure came under the Marcos regime. Scholars such as Castles [2007a] argue that the process was initiated as a measure to patch-up the poor economic performance under the predatory regime of Marcos. There was no or little capital investments, debts were mounting and high level of government corruption made it worse for the regime to command legitimacy. In fear of social unrest and to curb political opposition, Marcos declared martial law and Philippines started on the path of rapid market liberalization. A wide range of structural adjustment plans were adopted under the guidance of IMF and World Bank; one of the central programs being systematic export of labor [Siracusa and Acacio, 2004]. Before the state involvement, migration from Philippines was dominated by a vibrant informal sector and the Marcos regime, literally took over the trade in contract labor from the private migration merchants using it as instruments for economic and political viability [ibid]. Over the years there have been significant modifications in state policy reinstating private partners with state playing a supervisory role and also making it more human to suit the needs of migrants; this, however, goes beyond the scope of the current discussion.

Has this high level of organization and formalization delivered the expected goals? The evidence on this front is predominantly negative. In the beginning, the labor export program did help Philippines gain credibility as a global economic actor and improve its credit-worthiness in the global market [Sircacusa and Acacio, 2004]. However, the initial leverage did not sustain for long. Saith [2001] shows how the country once shown to be at the edge of economic take-off suffers from rising unemployment levels, increasing poverty and weak macro-economic fundamentals. Saith [2001] points out that years of neglect of agriculture and capital undervaluation have reduced the capacity of the economy to absorb the labor force. Low rate of domestic savings with excessive dependence of external flows is one of the serious shortcomings of the Philippine growth model making it particularly vulnerable to external shocks. Bayangos and Jansen [2009] point out that fluctuation in remittances are significant and the impact of recession in the US becomes pronounced once endogeneity and pro-cyclicality of remittances is taken into consideration. The benefits of migration have also accrued largely to the rich regions and higher income classes, having no or little impact on inequality [Saith, 2001]. The authors, however, also argue that for years to come growth in Philippines would be heavily dependant on remittance flows and poor could be worse off without them.

Philippines serves as an example of how dependence on remittances can drive attention away from more important structural issues – such as economic [land] reforms in rural areas which would challenge deep-rooted bases of inequality and under-development [Castles, 2007]. What we see is a quick-fix measure and shying away from more important developmental needs. Rupert and Solomon [2005, p.100] note that migrants too do not see these measures as helpful or remittances fulfilling any developmental task; some even mock the state policies such as giving away of titles of heroes of the nation as attempts to attract more money as remittances. In a comparison of five major labor exporting countries, Castles [2007] points out that in certain cases the motive of the state was to leverage the development potential of remittances and migration, while in others it was used as a means to cover up the failings of the existing regime and crush political dissent and ethnic minorities. The case of Philippines evidently falls in the latter category. After approximately four decades of concerted formalization attempts the Philippine economy continues to reel under many of the problems it started with if not more.

4.2 India

In 2005-2006, India received the highest amount of remittances worth 24. 6 billion USD; followed by China and Mexico [Sasikumar and Hussain, 2007]. 44 per cent of these remittances originated from the USA, 24 percent from the Gulf and 13 per cent from the European countries [Chisti, 2007]. Compared to other major migrant sending economies such as Philippines, Mexico, and Turkey, institutionalization of the process in India started late; gaining import only after the much-known balance of payments [BoP] crisis of 1991 and has been relatively slow and cautious in its approach. On average, however, the efforts are said to have met with success. The usage of formal banking channels for transfer of remittances has increased and the remittance market has grown more competitive with large number of new RSPs entering the market [Chisti, 2007]. In the fiscal year 1990-91, Reserve Bank of India reported remittances worth 2.1 billion USD. In less than 15 years the amount rose by more than 10 times. Compared to 1991, when remittances made 0.7 per cent of national GDP, they have now grown to 3 per cent of the GDP [ibid].[9]

For a long time Indian governments were unsighted to the contribution of remittances to the economy. The BoP crisis faced by India beginning 90s came as a turning point.[10] The Indian

[9] One, however, needs to treat these figures carefully. A significant part of the amount, as pointed out by Fritz et al [2008] may be a result of better accounting. As more remittances started to flow in through formal channels post-90s, they became increasingly visible in national accounts.

[10] Certain scholars point out that attention to remittances was rising even before the BoP crisis, starting in 1970s. For example, creation of the NRI deposit accounts meant to attract foreign capital. That too was done to 'shore up' the declining foreign exchange reserves [Chisti, 2007]. This, however, is part of the debate among scholars about whether Indian economy started to liberalize beginning 70s or 90s. Scholars proposing the former date argue that

forex reserve dropped to record low levels and India started on a massive liberalization exercise. Some scholars also call 1991 as 'India's second independence' [Chisti, 2007]. In a desperate attempt to shore up all possible sources of foreign exchange, remittances received special attention. There was a realization that they made a large part of India's foreign exchange earnings and were crucial in maintaining a healthy trade balance. During this period a number of steps were taken to attract contributions from the Diaspora and streamline the remittances flowing into the country. The initiative started under the Congress regime and gained force when the National Democratic Alliance [NDA] came to power. Under the NDA government of India celebrated the *Pravasi Bharatiya Divas* [Non-resident Indian Day] for the first time. It was an important part of the 'India Shining' campaign of the NDA, when Indian growth rate was at its peak, and greater contributions from the Diaspora were called for. When Congress came back to power in 2004 and retracted from numerous policies of the previous government, the special treatment to the Diaspora was maintained.

Sasikumar and Hussain [2007] point out that before 90s there were hardly any policies to maintain or increase remittance flows. Post liberalization, a number of incentives was provided to migrants – higher interest rates (vis-à-vis international market rates) and exchange rate guarantee for foreign currency denominated accounts [FCNR [B], higher interest rates to rupee denominated accounts compared to other citizens [NR [E] RA deposits], arrangements for repatriation of deposits and exemption from wealth and income tax both on deposit and interests earned on it [ibid, p. 19]. Sasikumar and Hussain [2007, p.19] point out that - "These incentives were provided mainly with a view to augment the foreign exchange reserves of the country, especially in the context of the difficult times the Indian economy had in the sphere of external finance." There is agreement among scholars that exchange rate liberalization was the key policy move which attracted large number of migrants to the formal banking infrastructure [Chisti, 2007; Sasikumar and Hussain, 2007].

India is one of the countries where the informal sector has been particularly strong. The Hawala system of remittance transfer dates before paper money and formal banking in the Indian subcontinent [Passas, 2003]. Apart from attributes such as trust and convenience, one of the key attractions of the informal RSPs was that they offered the market exchange rate to

Indian economy started to feel the heat of ISI policies in the 70s and that's when attempts started to allow foreign capital gradually. This discussion falls beyond the scope of our work and we stick to the more conventional view that Indian economy started to liberalize after the BoP crisis of 1991.

migrants, higher than the rate offered in banks. When India chose to let the Indian currency float and banks started to offer rates determined by the market, there was a significant shift from the informal methods to the banks. From 1990-91 to 1995-96, remittances grew from 2.1 billion USD to 8.5 billion USD [from 0.7 per cent to 3.22 per cent of the GDP] [Chisti, 2007]. Though there is no systematic study on the factors leading to the spectacular increase in remittances, scholars allude to certain key factors apart from exchange rate liberalization – better accounting, increase in IT professionals migrating to US and bullish sentiments about the Indian economy post 1991 reforms attracting Diaspora investments. While the onset of formalization was motivated by state's interests, the success of formalization depended on the critical mass of high-skilled migrant Diaspora preferring the formal banking channels, making the nature of migrants important for success of formalization attempts. It should not be forgotten that a large mass of the Indian Diaspora from the unskilled/semi-skilled category continues to prefer informal agents [DFID, 2005].

There is one key aspect of the Indian remittance formalization experience which deserves particular attention. Compared to the case of Philippines where there was rabid involvement of state agencies, Indian governments have been less active. Here the process has been driven more by entrepreneurial private financial institutions capitalizing on opportunities thrown open by liberalization. Despite initial success, the use of financial instruments such as securitization has also been low vis-à-vis Philippines and many Latin American countries, making the process slow. There are recurrent demands on the state by banks to raise ceilings on amount that can be freely remitted by individuals and extend the facility of special FCNR[B] and NR[E]RA deposit to non-residents other than Non-resident Indians [Mohan, 2008]. It is difficult to comment on whether this relatively cautious approach is better than the approach followed by Philippines or Indonesia. More studies would be needed to answer this question.

At the aggregate level only 2 per cent of the Indian population migrates abroad thus it is difficult to see a country-wide impact. There are certain regions, however, such as Kerala which send large number of migrants, mainly to the Gulf countries and are heavily dependent on remittance income. More than 25 per cent of the state GDP of Kerala comes from remittances; nevertheless, the remittance-development link remains elusive. As mentioned earlier, high amount of savings have failed to translate into economic growth in the state

[Kannan & Hari, 2002]. Castles [2007a] also point out that all migration has led to is 'ostentatious consumption' and display of wealth in Kerala.

4.3 Indonesia

Indonesia marks an interesting departure in the formalization tale. As mentioned earlier the country after starting to formalize went back with a vengeance to the informal methods. In a study of the Indonesia-Malaysia remittance corridor Hernandez-Coss et al [2008] point out that remittance flows through formal channels from Malaysia dropped by a massive 30 per cent in absolute terms betwen 2002 [0.4 billion USD] and 2006 [0.26 billion USD] and this was despite a a significant increase in number of migrants moving to Malaysia. The authors pointed out a need to pay attention to the unique characteristics of the Indonesian remittance economy and design measures accordingly.

Indonesia is the 4th largest populated country in the world and has recently come to enjoy the reputation as one of the largest labor exporters globally. As per 2006 statistics, around 4.3 million Indonesians work and live abroad, remit 5.6 billion USD to the country but only 10 per cent of remittances flow through the formal channels [Hernandez-Coss et al, 2008]. In early 2000s, a partnership was created between the Financial Market Integrity Unit of the World Bank and the East Asia Social Development Unit to streamline remittances flowing into Indonesia but as shown earlier have met with little success.

Hernandez-Coss et al [2008] identifies several factors that determine the migrant's choice of transfer channels – cost, physical access, institutional access, regulatory access, competition and financial literacy. Majority of the migration from Indonesia is of unskilled/semi-skilled labor and 80 per cent of the migrant population is comprised of women who work in the informal sector. Within the formal system 90 per cent of remtitances flow through the banking system and the biggest Indonesia bank POS has only 50 branches that can dispense remittances immediately. By contrast, the informal service providers collect and deliver money door-to-door and have a much wider outreach. Women migrants feel more at ease with the informal agents who would speak their own language and would be much less intimidating than the formal bureaucratic banking system. The informal sector also offers the most crucial requirement and that is anonymity to the undocumented migrants. Hernandez-Coss et al [2008, p. 14] note that –

“Despite the disadvantages of the informal sector, the formal sector has little to offer the migrant workers in its current state. It is less competitive in terms of accessibility and provides little added value in terms of access to the much needed pre-departure credit or other instruments that might appeal to the migrant workers, especially women and the undocumented.”

Passas [2003] argues that attempts to over regulate the traditional systems of remittance transfers may be counter productive. It might push them ‘underground’ making them more vulnerable to criminal activities. In the study of the remittances flowing from Malaysia to Indonesia Hernandez-Coss et al [2008] found that the significant drop in flow of remittances through formal channels coincided with the introduction of Anti-money laundering and anti-terrorism regulations, an integral part of the formalization drive. This points out that regulations of the informal sector should be commensurate with the risk as the chances of driving migrants to greater informality is high.

There is also a political dimension behind migration from Indonesia which is relatively under-researched vis-à-vis Philippines or India. Tirtosudamo [2000] brings this out by highlighting the role of the ruling elite and internal politics in driving migration from Java. The author points out that politics in Indonesia is driven by the need to reinforce geographical clusters based on race, religion, tribe and language and that always involves rooting out dissidents and removing possibilities that would pose any challenge or cause social unrest. These political processes are an important driver of international migration from Java and deserve greater attention than is currently provided.

4.4. Chapter Summary

Furthering the arguments presented in the last chapter we show that choice of formalization has a strong political dimension along with the economic; mostly political surpassing the economic. In the case of India and Philippines state interest for economic survival was explicit; in Philippines the fear of political turmoil added greater exigency. In the case of Indonesia, though the migrant streams is shown to be triggered by internal politics by Tirtosudamo [2000], the international organizations pioneered the formalization of remittances.

Notably, what made the cases more interesting were the differences. In case of Philippines there was overzealous state machinery and the formalization process remained state-engineered and state-run. In India, however, after the initial exchange rate liberalization the process was largely steered by private financial institutions. Even today, the Indian state continues to follow a cautious approach in raising limits of accounts and extending benefits to larger non-resident populations. The two countries mark two different approaches to formalization. However, in absence of primary research, we cannot comment on which of the two approaches is better. More primary studies would be needed to answer this question. The third case of Indonesia where formalization was steered by external agents shows that understanding the nature of migration from a region is important. At places where undocumented migration is high formalization attempts need to be cautious. Indonesia's reaction to the drive for formalization illustrates the inadequacies of the formal system vis-à-vis the informal and serves as a warning that rash attempts to formalize may drive migrants to riskier options.

5. CONCLUSION

The positive contribution of the remittance-enthusiasts is that they lessen the apathy and negative outlook towards international migration. A decade ago migration was looked as a symptom of failed development and all interventions aimed to stop or lessen migration from any given region. The new paradigm creates greater acceptance of migration and reduces what Arjan de Haan termed as the ‘sedentary bias’ in public policy [de Haan, 2002]. We acknowledge this as a welcome change especially in contexts where migrants are at a constant risk of being cheated by unscrupulous RSPs.

What we find problematic is eulogizing remittances as the ‘new development mantra’ or the solution to third world under-development. In the name of formalization we see creation of a world-wide financial architecture around remittances consisting of norms, standards, regulations and a plethora of dedicated agencies. The phenomenon is strikingly similar to the micro-finance story – both drawing credence in the name of financial inclusion of the poor and leveraging small savings. Micro-finance has already become a global business sustaining a giant body of rating agencies, banks and NGOs and we surmise that remittances too are set to become one. In our understanding, both these 21st century development mantras put too great a burden on the shoulders of the poor. More studies are needed to draw linkages between the micro-finance and remittance story as in our view the micro-finance experience has a good deal to offer to remittances-enthusiasts.

In an attempt to understand the euphoria over remittances this study addresses two questions – one, how would formalization enhance the developmental potential of remittances; and two, what are the determinants of the onset and success of formalization – is it purely governed by economic/financial logic or are there other factors which play a greater role. We find that both the theoretical and empirical evidence for remittance-led development is less than sound. The much hyped counter-cyclicality of remittances is only vis-à-vis other sources of development finance. As such, remittances have a pro-cyclical nature, vulnerable to the economic boom and busts of the migrant receiving countries. High share of remittances in the national product makes these economies particularly vulnerable. The tendency of migrants to hold remittances in foreign currency also poses the risk of ‘dollarisation’ and central banks losing their control on monetary policy. The impact of remittances on growth depends on a wide variety of factors many of which do not lie in the control of policy makers. The case of Philippines shows how after four decades of concerted remittance management the economy continues to suffer from weak macro-economic fundamentals and widespread inequality at the micro-level. The evidence of impact of increased remittance savings on growth is also lacking. There is agreement among scholars that while micro-level impact of remittances is extensively studied, studies on the macro-economic of remittances are relatively scarce. The global attention to remittances by policy-makers creates the right platform to undertake more studies on formalization of remittances and their impact on the macro-economy.

In answer to our second question, we find that there is a strong agency element in the attention that migration and remittances have received world-over. Unlike the liberal argument which would see the role of international financial institutions and the states as facilitating market operations by removing possible hurdles against efficient functioning through creation of norms, regulations, information dissemination etc, we find a process of deliberate remittance market creation by dedicated agencies. The World Bank, CPSS and Inter-American Development Bank are some of the organizations leading the initiative at the global level. At the national levels, in all the three cases of Philippines, India and Indonesia, we find evidence of an explicit state involvement to leverage greater amount of remittances. The degree of involvement and speed of reforms, however, varies creating opportunity for future research on which approach is more conducive to stimulating growth.

Further, the proposed superiority of formal methods over informal is also debatable. The case of Indonesia shows that the needs of the migrants may be better served by the informal agencies and there is a need to acknowledge this. Thoughtless drives to formalization and regulation of informal remittance industry may lead to migrants resorting to riskier options. The formalization drive needs to be driven more by the needs of migrants and not of the financial sector. As Hernandez-Coss et al [2008] rightly identify – it is not important what medium is chosen – formal or informal, what is important is whether the given medium delivers. If the informal sector has greater outreach, delivers its job more cost-efficiently, it makes much more sense to invest in the informal system in those regions. More studies, however, are needed to understand the requirements of migrants in different remittance corridors and adapt the remittance management attempts suitably.

Fortunately, there is an upcoming drive to understand the functioning of informal RSPs and address the ill-informed biases that have grown against them after the 9/11 and the securitization euphoria across the globe. Certain scholars make the case of informal service providers and call upon methods which would make them function better. This is a positive development and needs to be strengthened.

REFERENCES

Aggarwal R. , Demirgüç-Kunt A., Martinez Peria M. S., [2006], Do Workers' Remittances Promote Financial Development, Policy Research Working Paper Series 3957, The World Bank. URL: http://econ.worldbank.org/resource.php?type=5

Alberola E., Salvado R. C. [2006], Banks, Remittances and Financial Deepening in Receiving Countries: A Model, Banco de Espana Research Paper No. WP-0621

Avila F. R., E. Schlarb [2008], Bank Accounts and Savings – The Impact of Remittances and Migration: A Case Study of Moldova, Working Paper No. 448, Kiel Institute for the World Economy

Bayangos V. and K. Janse, [2009], The Macroeconomics of Remittances in the Philippines, Institute of Social Studies [ISS] Working Paper No. 470

Castles S. [2007a], Comparing the Experience of Five Major Emigration Countries, Working Paper No. 7, International Migration Institute, University of Oxford
URL: www.imi.ox.ac.uk/pdfs/WP7%20Comparing%205%20countries.pdf

Castles S. [2007b], 'Migration and Social Transformation', Migration Studies Unit Working Paper No. 2008/01, Paper presented in Migration Studies Unit Inaugural Lecture, London School of Economics, 15th November, 2007,
URL: http://www.lse.ac.uk/collections/MSU/papers/workingpaper1_castles.pdf

Chishti M. [2007], The Rise in Remittances to India: A Closer Look, Feature Story, Migration Policy Institute, February 1, 2007,
URL: http://www.migrationinformation.org/Feature/display.cfm?id=577

De Haan A. [2002], 'Migration and Livelihoods in a Historical Perspective: A Case-Study of Bihar, India', *The Journal of Development Studies*, 38[5], pp.115-142

Frieden J. A, [1995], Capital Politics: Creditors and the International Political Economy, *Perspectives on Global Power and Wealth*, edited by J. A. Frieden and D. A. Lake. New York: St. Martin's Press, pp. 282-298

Frisch A. B. [2004], The Movement to Formal Systems, Paper presented at APEC Symposium on Alternative Remittances Systems: Shaping the Remittances Market by shifting to Formal Systems, 3-4 June 2004; ADB Institute, Tokyo, Japan

Fritz B., C. Ambrosius, U. Stiegler [2008], Financial Development and Macroeconomic Stabilisation through Remittances? Potential Contribution and Modes of Governance, March 2008, Paper presented at 12th EADI conference, Geneva, June 2008

Goldring L. [2003], Rethinking Remittances: Social and Political Dimensions of Individual and Collective Remittances, CERLAC Working Paper Series, York University, Canada, URL: http://www.yorku.ca/cerlac/documents/Goldring.pdf.

Halehbridi [2005], Consequences of Labour Migration for the Developing Countries, Conference on Labour Migration, Brussels, 26th February, 2005 http://siteresources.worldbank.org/INTBELGIUM/Resources/HalehBridiRemittances.pdf.

Hernandez-Coss Raul, G. Brown, C. Buchori, I. Endo, E. Todoroki, T. Naovalitha, W. Noor, C. Mar [2008], The Malaysia-Indonesia Remittance Corridor: Making Formal Transfers the Best Option for Women and Undocumented Migrants, World Bank Working Paper No. 149

Hudson D. [2008], Developing Geographies of Financialisation: Banking the Poor and Remittance Securitisation, *Contemporary Politics*, 14[3], pp.315-333

IOM [2008], World Migration 2008: Managing Labor Mobility in the Evolving Economy, International Organization for Migration
URL: http://www.iom.int/jahia/Jahia/op/edit/cache/offonce/pid/1674?entryId=20275

Kannan K. P. & K. S. Hari, [2002] 'Kerala's Gulf Connection: Remittances and their Macroeconomic Impact', pp. 119-227 in Zachariah K..C., K. P. Kannan & S. I. Rajan [eds] *Kerala's Gulf Connection: CDS Studies on International Labour Migration from Kerala State in India*, Centre for Development Studies, Thiruvananthapuram, Kerala, India

Karafolas S. & Sariannidis N. [2008], The Banking Network as a Transmission Channel of Migrant Remittances: The Case of Greek and Italian Banks in Albania, *Transit Stud Rev* (2009) 15:674–684

Lopez-Cordova E., A. Olmedo [2006], International Remittances and Development: Existing Evidence, Policies and Recommendations, INTAL-ITD, Occasional Paper 41, Inter-American Development Bank

Loser C., C.Lockwood, A. Minson, L. Balcazar [2006], The Macro-Economic Impact of Remittances in Latin America- Dutch Disease or Latin Cure?, Paper presented at Inter American Development Dialogue 2006, Washington DC
URL: http://www.g24.org/lose0906.pdf

Markose S. M. [2003], Computability and Evolutionary Complexity: Markets as Complex Adaptive Systems (CAS), *The Economic Journal Feature*, June 2005, Vol. 115, F159-F192.

Martínez José de Luna [2005], Workers' Remittances to Developing Countries: A Survey with Central Banks on Selected Public Policy Issues, World Bank Policy Research Working Paper 3638

Mendola M. [2006], Rural Out-migration and economic Development at Origin: What do we Know? Sussex Migration Working Paper No. 40, University of Sussex
URL: http://www.sussex.ac.uk/migration/documents/mwp40.pdf

Mohan R. [2008], Capital Flows to India, RBI Monthly Bulletin, 2048, December

Orozco M. [2006], International Flows of Remittances: Cost, competition and financial access in Latin America and the Caribbean—toward an industry scorecard, Report presented at the meeting on “Remittances and Transnational Families” sponsored by the Multilateral Fund of the Inter-American Development Bank and the Annie E Casey Foundation, organized on May 12th, 2006

Oroczo M., K. Jacob, J. Tescher [2007], Card Based Remittances: A Closer Look at Supply and Demand, The Centre for Financial Services Innovation URL: http://www.aecf.org/upload/publicationfiles/IM3622H5010.pdf.

Passas N. [2003], Hawala and Other Informal Value Transfer Systems: How to Regulate Them? *Risk Management*, 5 [2], Special Issue: Regulation, Risk and Corporate Crime in a ‘Globalised’ Era, pp. 49-59

Passas N. [2004], Informal Value Transfer Systems [IVTS] and their Mechanics, Paper presented at APEC Symposium on Alternative Remittances Systems: Shaping the Remittances Market by shifting to Formal Systems, 3-4 June 2004; ADB Institute, Tokyo, Japan

Pineault E. [2001], Finance Capital and the Institutional Foundations of Capitalist Finance: Theoretical Elements from Marx to Minsky, Working Paper, Publications de la Chaire MCD, Chaire de Recherche du Canada en Mondialisaion, Citoyennete et Democratie URL: https://depot.erudit.org/bitstream/002332dd/1/document-2002-01-pineault.pdf.

Press Trust of India [2009], About 150,000 Indian return from UAE due to recession, Wednesday, July 8, 2009, URL: http://www.ndtv.com/news/india/about_15_lakh_indians_return_from_uae_due_to_recession.php

Raghuram P. (2009). Which migration, what development? Unsettling the edifice of migration and development, *Population, Space and Place*, 15[2], pp. 103–117.

Rapoport, H., Docquier, F. [2005] The Economics of Migrants’ Remittances, IZA Discussion Paper No. 1531

Ratha D. (2004) Understanding the Importance of Remittances, Migration Policy Institute, feature Story, October 2004, URL: http://www.migrationinformation.org/Feature/display.cfm?ID=256

Rupert M., M. S. Solomon [2005], *Globalization and International Political Economy*, Rowman & Littlefield Pub Inc.

Saith A. [1991], Absorbing External Shocks: The Gulf Crisis, International Migration Linkages and the Indian Economy, Working Paper Series No. 107, Institute of Social Studies

Saith A. [2001], Emigration Pressures and Structural Change: Case Study of the Philippines, International Migration Papers 19, Employment and Training Department, ILO, URL: http://www.ilo.org/public/english/protection/migrant/download/imp/imp19.pdf

Siracusa C. & Acacio K. [2004], ‘State Migrant-Exporting Schemes and their Implications for Rise in Illicit Migration: A Comparison of Spain and the Philippines’, *RIMI*, 5[3] pp. 321-342

Tirtosudamo R. [2000], Political Dimensions of International Migration: Indonesia and its Neighboring Countries, published in *Labour Migration in Indonesia: Policies and Practices* edited by Sukamdi, A. Harris & P. Brownlee, Population Studies Center Gadjah Mada University

Terry D. F., S. R. Wilson [2005], *Beyond Small Changes-Making Migrant Remittances Count*, Washington D.C., Inter-American Development Bank, pp.375-394

The Economic Times [2009], G8 eyes halving remittances transfer costs: Italy, 12th June, 2009 URL: http://economictimes.indiatimes.com/News/International-Business/G8-eyes-halving-remittances-transfer-costs-Italy/articleshow/4650143.cms

The Economist [2008a], Trickle-down economics**,** *The Economist* print edition, Feb 19th 2009

DFID and UK Remittance Working Group [2005], UK Remittance Market
URL: www.dfid.gov.uk/pubs/files/uk-remittances-report.pdf

World Bank [2007], General principles for international remittance services, Committee on Payment and Settlement Systems, The World Bank, January 2007, Report No. 38821