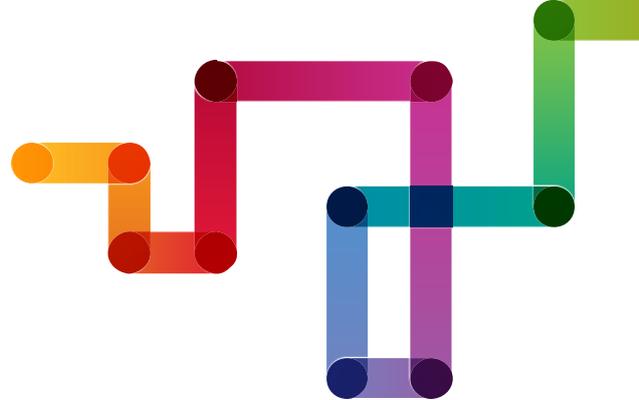


Remittances: a potential game changer for global development



What if migrants could be agents for development? What if international development aid was funded by people from developing countries? Reducing transaction costs for remittances would save up to \$20 billion a year for global development, more than the UK's entire overseas development budget in 2015.

Our vision

Our vision is to increase the potential of remittances to achieve equality, financial inclusion and social development. According to the World Bank, the number of international migrants is expected to surpass 250 million this year and they will send home a total of \$601 billion in 2016. Yet the links between remittances and development are complex and there are several barriers to achieving development goals.

The challenges and their context

Financial transfers from a migrant to his or her country of origin are known as remittances. In the last 10 years they have increased by more than 180% and are the principal source of finance for many developing countries. Total remittances in 2014 reached \$583 billion, compared to \$135.2 billion Official Development Assistance (ODA) that year. Remittances, in contrast with Foreign Direct Investment (FDI), are stable flows of capital and during downturns they keep increasing. The World Bank estimate that remittances will increase to \$601 billion in 2016.

Remittances sent by migrants support recipients in meeting basic needs. In particular there is a good correlation between remittances and improved health, nutrition and education. In contrast, there is not strong evidence to link remittances and productive investments.

There are several barriers to developing countries making the most from remittances. Among these are transaction costs, lack of competition among money transfer operators and an increase in flow of remittances through informal channels.

Today there are 300 formal corridors for transactions between 35 sending and 96 receiving countries. The international community, led by the World Bank, has made efforts to reduce transaction costs, achieving some positive results. Today 80% of corridors have transaction costs below 10%, with the average being 7.52%. Yet we are still far from the Sustainable

CHALLENGES BRIEF

Development Goal (SDG) objective of reducing average costs below 3% and to eliminate remittance corridors with costs higher than 5% by 2030 (SDG 10.c). Research has demonstrated that reaching such goals would save up to \$20 billion annually (more than UK annual ODA), helping more of the money reach its intended recipients.

One reason for high costs is the lack of competitiveness in the global remittance market. Commercial banks remain the most expensive of all remittance service provider types (average cost 11.2%), followed by Money Transfer Operators (MTOs) (6.24%) such as Western Union, and post offices (5.88%). Online services, such as mobile banking transactions, are the least expensive product type (5.57%). Most transfers occur through MTOs, as banks have shown little interest in entering the market due to the small sums being transferred - typically between \$150 and \$300. The 'big four' MTOs are Western Union, MoneyGram, Ria and Sige. The MTOs have expanded on the ground and have consolidated exclusive arrangements with commercial banks which make it difficult for competitors to enter the market. Western Union alone accounts for \$80 billion of remittance transfers annually and has 510,000 agents around the world.

Another obstacle to the market's development is the dominance of informal channels that cannot be tracked. Remittances to Africa play an important role in national economies. In many fragile states remittances are estimated to exceed 50% of GDP, and overall remittance flows are 50% greater than ODA. Yet Sub-Saharan Africa is still the region with the highest average cost of transactions (9.74%), which stimulates an informal market estimated to be between 25% and 75% of the size of the formal market.

Current innovation

- Blockchain: Bitcoin Remittance Companies (BRCs), also called "Rebittance" Companies, are just appearing in the bitcoin ecosystem. One example is REBIT, which is operating in the Hong Kong-Philippines corridor.
- Mobile services: WorldRemit is an online service that lets people send money to friends and family living abroad, using a computer, smartphone or tablet. Money can be received as a bank deposit, cash pick-up, Mobile Money, or mobile airtime top-up.
- Microfinance institutions: The European Microfinance Platform (e-MFP) Remittances Action Group supports microfinance institutions as relevant channels to use remittances as savings or loan products.

The potential for challenge prizes

- A fintech prize to promote the development of easy-to-use technological innovations such as blockchain or mobile banking, able to reduce remittance transaction costs and able to reach rural communities.
- A competition prize to encourage new financial service providers to enter the market, or existing ones to grow their networks, so as to boost competition and cut costs.
- A bank prize to develop less costly solutions for commercial banks to access remittance flows.

Prepared for the Nesta Challenge Prize Centre by Eleonora Corsini. Last updated 20/04/2016.