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Competition and Remittances in Latin America: Lower Prices and More Efficient Markets

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List of Abbreviations

ACH	Automated Clearing House
CPSS	Committee on Payment and Settlement Systems
FATF	Financial Action Task Force
GAO	Government Accountability Office of the United States
GDP	Gross Domestic Product
ICT	Information and communications technology
IDB	Inter American Development Bank
LAC	Latin America and the Caribbean
MIF	Multilateral Investment Fund (of the IDB)
MTO	Money transfer operator
MSB	Money service business
OFAC	Office of Foreign Assets Control
OECD	Organisation for Economic Cooperation and Development
POS	Point of sale
RSP	Remittance service provider
US	United States
USAID	US Agency for International Development
USD	United States dollar
WOCCU	World Council of Credit Unions

Executive summary

Along with accelerating migration from Latin America and the Caribbean (LAC), the growing flow of worker remittances – money sent home by migrants abroad - has rapidly gained the attention of governments, the private sector and civil society as an important issue in development. Remittances to Latin America and the Caribbean reached nearly $54 billion in 2005. Increasing competition in remittances markets has been identified as a means of lowering transaction costs and improving the efficiency of the market. This theme also has far-reaching development consequences in achieving national policy objectives, especially in the context of increasing financial access to the poor. While the study of remittances and the competition landscape of the industry is still in its infancy, this paper attempts to highlight gaps between ideal competitive market conditions and current circumstances.

Although prices for remittances to LAC - often high and widely variable - have fallen with competition in many corridors, certain remittance service providers (RSPs) exercise market power, charging above market prices. While service options and quality standards have improved with new entrants, services and innovations, geographic disparities persist within and among countries depending on their financial infrastructure, as well as other factors.

The economics of the remittances industry, especially its geographic fragmentation and the importance of building acquisition and distribution networks, generates economic challenges for new entrants and incumbents. Structural and systemic constraints to more competitive conditions - lack of transparency, underdeveloped financial infrastructure, challenging legal and regulatory frameworks and poor financial access – may set up barriers to entry that maintain incumbent institutions' large proportion of LAC remittances markets.

In addition, regulatory frameworks for remittances are increasingly restrictive in developed country sending markets – often in ways that impede competition – but the receiving country distribution markets are very lightly regulated or feature related financial sector regulation that indirectly constrains competition in remittance markets.

The paper proposes that future inquiry should focus on the following areas in order to further clarify aspects of remittances markets that influence the competition landscape:
the extent of substitution and competition between informal transfers and formal remittance channels,

spatial and geographic analyses of prices and services,

implications of foreign exchange pricing, management and regulation

analysis of the domestic distribution market, especially identification of anti-competitive exclusivity arrangements, quantification of market shares and barriers to widening networks,

the role of information and its dissemination in increasing the visibility of alternative channels,

access to payments systems and their impact on access, pricing and efficiency;

examination of existing and proposed regulations to determine whether any represent barriers to entry or measures that may drive formal remittances toward informality;

regulatory assessment with the aim of ensuring non-discriminatory and proportionate prescriptions relative to risk posed by RSPs.

With an improved understanding of existing conditions, encouraging further competition may be one crucial means of ensuring low prices, better service, increased efficiency and expanded service options to both senders and receivers of remittances in the LAC region.

Introduction

1. Along with accelerating migration from Latin America and the Caribbean (LAC), the growing flow of worker remittances – money sent home by migrants abroad - has rapidly gained the attention of governments, the private sector and civil society as an important issue in development. These flows have become important to the development community for a number of reasons. First, remittances illustrate the movement of labour across borders. Second, the marginalisation common among certain immigrant groups has made them vulnerable to high prices traditionally charged by remittance service providers (RSPs). Third, remittance flows represent the earnings and savings behaviour of people who are often low income without access to financial services that might offer improved service, lower prices and more options.

2. Governments and overseas development agencies have primarily responded to remittances with concern about high and variable prices and their burden on migrants' families. While prices for money transfers to LAC have fallen with competition, certain RSPs have exercised market power, charging above market prices, for many years. The state of competition has improved the range of options and standards markedly with new entrants, services and innovations, but geographic disparities persist within and among countries depending on their financial infrastructure, as well as other factors.

3. The economics of the remittances industry, especially its geographic fragmentation and the importance of building acquisition and distribution networks, generates economic challenges for new entrants and incumbents. Structural and systemic constraints to more competitive conditions - lack of transparency, underdeveloped financial infrastructure, challenging legal and regulatory frameworks and poor financial access – may set up barriers to entry that maintain incumbent institutions' large proportion of LAC remittances markets.

4. The regulatory framework for remittances is increasingly restrictive in developed country sending markets – often in ways that are impeding competition – but the receiving country distribution markets are very lightly regulated or feature related financial sector regulation that indirectly constrains competition in remittance markets.

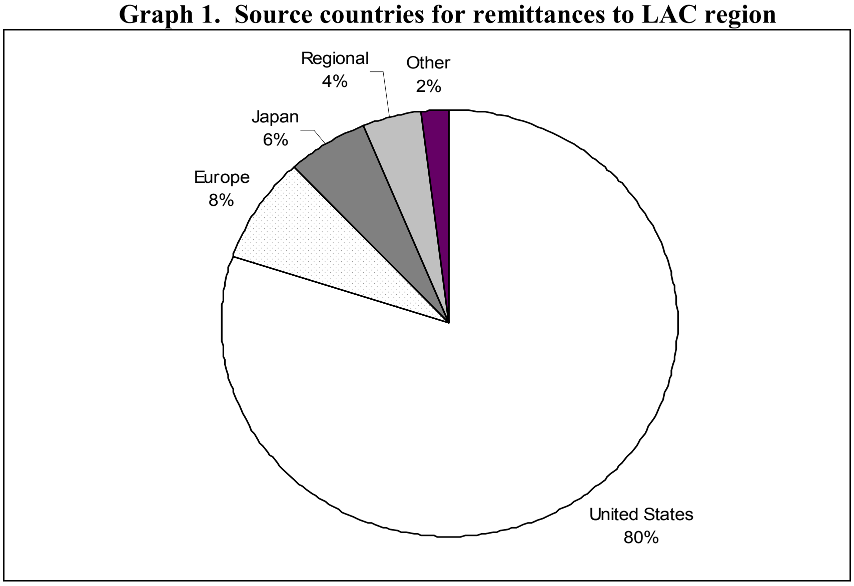
5. As a result, there is scope for understanding better the gaps between the ideal competitive conditions and current circumstances. Encouraging competition is one central means of ensuring low prices, better service, increased efficiency and expanded service options to both senders and receivers of remittances in the LAC region.

Fundamentals of remittances markets

6. Globally, remittances amounted to at least $167 billion in 2005, and remittances to Latin America and the Caribbean reached nearly $54 billion (World Bank 2005, IDB 2006).[1] Mexico is one of the top three remittance recipients globally at $20 billion in 2005 (preceded by China and India). In Latin America and the Caribbean, Brazil and Colombia likewise receive substantial resources in the form of worker remittances ($6.4 billion and $4.1 billion, respectively). Even for those countries who receive smaller amounts in absolute terms, remittances in other regional economies are a vital resource, amounting to 10%-15% of GDP for several and as much as 25% of GDP in Haiti. Remittances exceed overseas development assistance in every country in Latin America and the Caribbean. In most countries, they also dwarf the capital received by foreign direct and portfolio investors as well. Around the region, remittances are among the top three sources of foreign exchange.

7. With labour migration from LAC to the US and Europe increasing rapidly in the 1990s, the number of migrants from the region now approaches approximately 25 million people. In the United States, those coming from LAC are highly concentrated in about six states, but new communities are growing rapidly elsewhere.[2] In Europe, most migrants from LAC moved to Spain and Portugal where colonial ties and language barriers were least burdensome. Italy, Switzerland and other European states are becoming new destinations. There are also important communities from the region in Japan. Citizens of the Caribbean have long established migratory patterns to Canada and the United Kingdom as well. Migration within LAC is also an important phenomenon. Not surprisingly, these host countries source the largest remittance flows in the region as graphs 1 and 2 indicate.

Graph 1. Source countries for remittances to LAC region

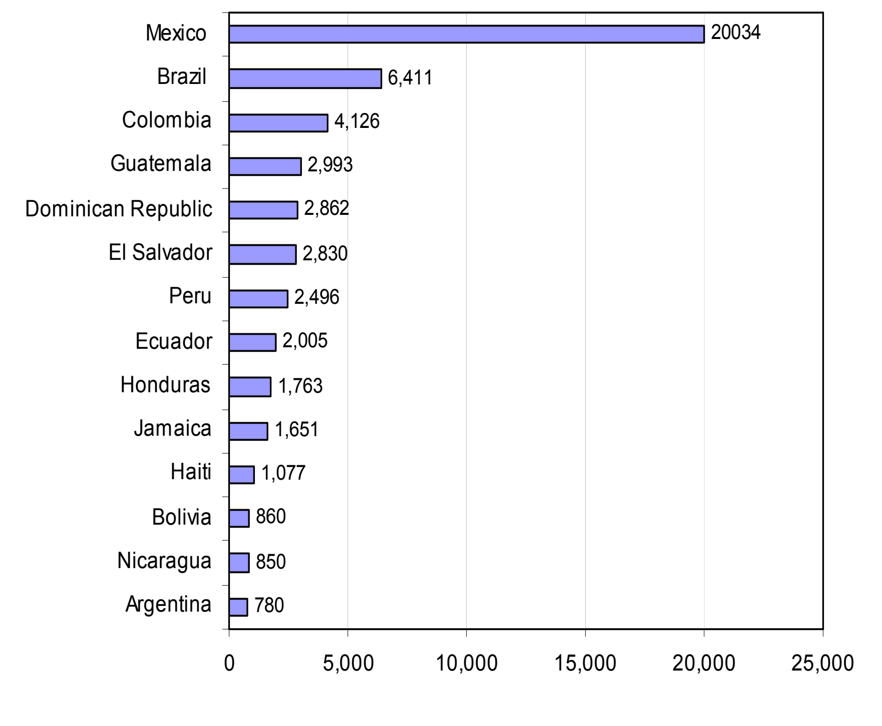


Source: Inter American Development Bank, 2005.

Graph 2. Migration and remittances

Left hand table: estimated migrants living abroad (millions); Right hand graph: international remittances (US$ millions)

Mexico	10
Brazil	2-2.5
Colombia	4
Guatemala	1
Dominican Republic	1
El Salvador	1-3
Peru	2
Ecuador	1.5
Honduras	1
Jamaica	1.5-2.5
Haiti	1
Bolivia	1-1.5
Nicaragua	2
Argentina	1



Source: Inter American Development Bank, Migration Policy Institute, IOM.

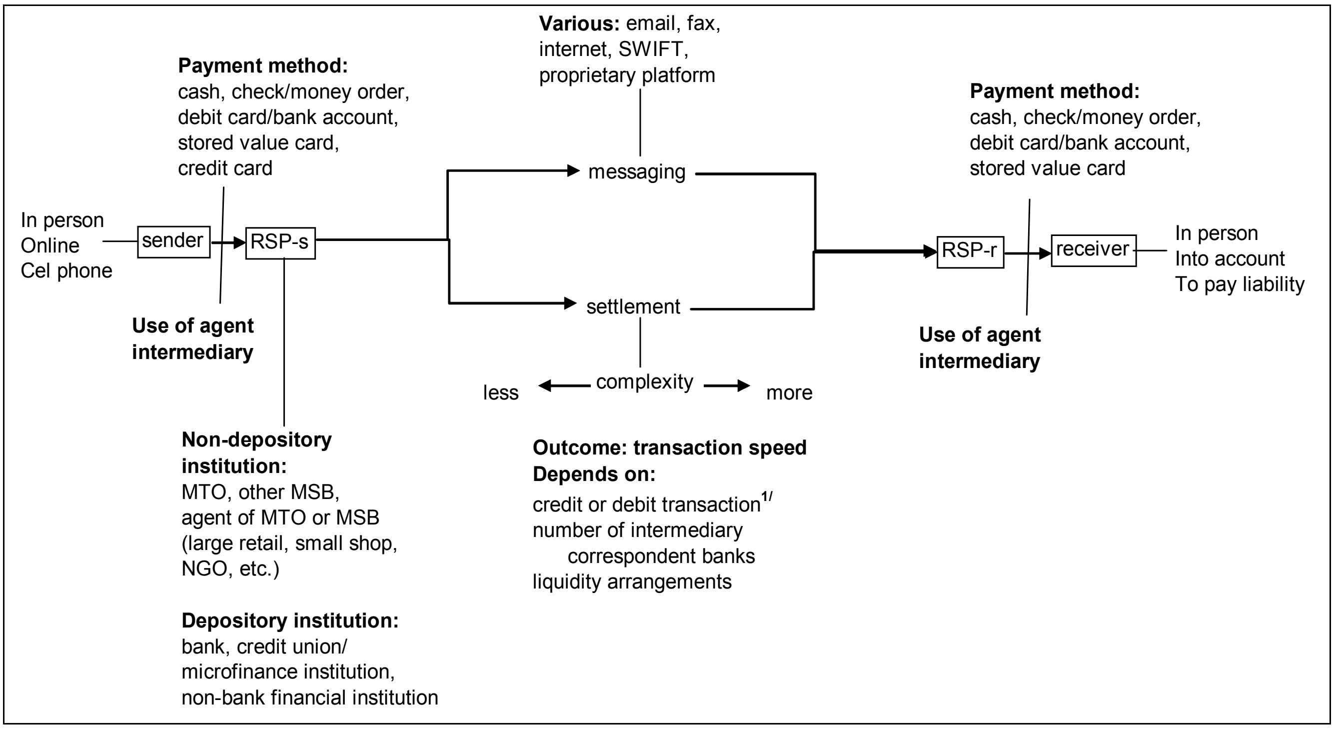
8. Remitting has taken place for generations in the LAC region. The rate at which migrants remit on regular basis is relatively consistent at 60% to 70% of adults, according to various studies and surveys.[3] The average amount of money being sent now ranges from $300 to $400 (World Bank 2006, Orozco 2006, Andreassen 2006).

9. Upwards of 70% of senders use an international money transfer company that makes electronic transfers (Bendixen 2005). Approximately 15% use informal means by asking friends or family to carry money home or by sending a money order by mail. Depository institutions have only a small participation in the market of 5%-10% of the total depending on the country. Both senders and receivers of remittances tend to remain outside the formal financial sector.

Definitions and fundamentals about remittance transactions

10. This report utilises the same definition for remittances used in the General Principles on International Remittances (CPSS 2006): a cross border person-to-person payment of low financial value.[4] Each transaction starts with a sender and ends with the disbursement of the money to the intended receiver.[5] Hernandez-Coss (2004) coined the use of terms normally used in the telecommunications sector to describe the three major stages of a remittances transaction – the First Mile, the Intermediary, and the Last Mile. Graph 3 explains the various steps. At each stage, multiple determinants impact outcomes such as the choice of channel and RSP, the price, the transaction location, the payment method, the complexity of the transaction, the time to delivery and the disbursement location and payment method.[6]

Graph 3. Description of remittance transaction



1/ In a credit transaction, the paying institution sends instructions for disbursement to the beneficiary. In a debit transaction, the receiving institution initiates the disbursement process, which adds complexity and, often, time.

11. At the First Mile, understanding demand factors requires examination of the circumstances under which migrants remit and the characteristics of individual communities. Their educational attainment, the age distribution of migrants, the length of time in the adopted country, their average incomes, the percentage having bank accounts – all these factors may play a role in the choice of RSP, channel and payment method. There are interesting comparisons to be made with other countries. In the United States, for instance, migrants must contend with their discomfort in English, the dearth of bilingual staff in regulated depository institutions and perhaps their lack of identification or appropriate documentation. This is less the case in Spain. In addition, because immigrants from LAC often live in densely populated and tightly knit communities, they benefit from the information advantages of social networks, which may inform their choice of RSP more than price or service comparisons.

12. The supply side at the First Mile is characterised mostly by the nature of competition among dominant money transfer operators (MTOs) in particular markets. Remittance senders from LAC in the United States tend to choose MTOs because of their ease, convenience, safety and speed. In certain high traffic corridors, remittances have become so competitive that they are basically commodities as services are largely substitutable with little service variation.[7] Networks of agents form a key part of the competitive landscape on the sending side. The larger the network of agents, the more sales points an MTO has. There is sometimes intense competition among remittance service providers to contract with agents that have a loyal customer base. As a result, some agents possess and exercise substantial negotiating power with the remittance service providers with respect to pricing because they can demand a higher percentage of the commission paid. This may lead to higher prices.

13. Outside of the MTOs, there are few options. More recently, financial institutions have shown strategic vision in pursuing migrants as customers by offering low cost remittances. [8] In the United States and Europe, some banks and credit unions are expanding services to migrant clientele using remittances as leverage. This has entailed new outreach and marketing strategies, investing in staff with foreign language skills and making services more convenient. Nonetheless, services offered by financial institutions on the sending side tend to have low market share.

14. The legal and regulatory environment at the First Mile has become a challenge to all institutions following the September 11 attacks and renewed efforts to tighten controls on money transfer. "Know Your Customer" rules and the Patriot Act, along with the implementation of the range of the Financial Action Task Force (FATF) recommendations, [9] have raised the cost of compliance with regulations to prevent money laundering and terrorist financing. The stringent and, at times, inconsistent application of these rules by supervisors and bank auditors, as well as bureaucratic overlap, have raised compliance costs further and resulted in the closure of some MTO bank accounts. This has raised the cost of cash management for these MTOs.

15. At the Intermediary stage, the money leaves the hands of the originator of the remittance transaction and proceeds through various steps in the execution of the transaction. The two primary threads of activity - messaging and settlement – transmit instructions to pay a recipient "on the other side," to disburse cash to the recipient and to net out payments to receiving-side RSPs and correspondents. These steps entail various levels of cost and complexity and, not surprisingly, these are the most technology intensive steps of the transaction so far. Other major costs entail setting up bank accounts and managing liquidity for disbursement (Andreassen 2006). Finally, compliance with documentation/identification rules, reporting requirements and security checks has created additional dimensions of cost and complexity for RSPs.

16. At the Last Mile, the determinants of recipients' behaviour, choice of channels and uses for the remittance money are similarly determined by socioeconomic and demographic characteristics of the communities. Cash remains the primary payment medium. The funds are used primarily for consumption but most recipients also say that some part of the money (10%-40%) is used for housing investment, health care, education, savings and small businesses (Terry and Wilson 2005, World Bank 2005, Suki 2004, Orozco 2002). Many believe that the substantial use of remittances for consumption rather than savings or investment has driven the popularity of basic cash-to-cash services (i.e. cash sent and cash disbursed), as opposed to other payment forms such as cash-to-account. This may also be determined by weak financial infrastructure and poor financial access in migrant-sending regions outside major cities.

17. Receivers likewise have their reservations about using formal financial institutions despite potentially lower cost services. Receivers – and senders alike - often have limited financial knowledge and literacy and may shy away from banks and credit unions. Receivers in rural areas often have poor access to distribution points associated with lower cost options. They may pay high transportation costs to collect their transfers in the most convenient, albeit not the least costly, fashion.

18. Spatial relationships also help to determine the value of distribution networks. Recipients will optimise ease, convenience, safety and cost, as well as the total amount received once the foreign exchange spread has been deducted. As a result, distributing agents with large

networks – banks in particular - may negotiate better commissions from MTOs and may exercise power in setting prices. Because of their existing networks and ability to manage liquidity effectively, bank branches distribute a substantial proportion of remittances as agents for MTOs. These services are generally not aimed at improving financial access and literacy, which might facilitate the use of less costly account-to-account services. Unlike in other regions, postal networks in Latin America and the Caribbean do not yet participate actively in the distribution of remittances.[10] However, other retail firms, foreign exchange agencies and others do act as distributors for MTOs. In Asia and Africa, by contrast, postal networks have been used as a means of increasing rural communities' access to financial and other services.

19. Few formal efforts exist at scale to improve financial intermediation among the low income and low-middle income segments of society that often form the bulk of recipients of migrants' remittances. In fact, receiving side banks have yet to conclude that remittance receivers will be sufficiently profitable with or without additional financial education to justify the additional cost of attempting to bank them. Smaller, more appropriate distribution partners, such as rural credit unions or microfinance organizations, may require further investments in technology, training, management and administration and negotiating power to make this business worthwhile.

20. Bilateral and multilateral donors have stepped in to disseminate information, to support market innovation, to facilitate dialogue and to promote effective policy response. Their activities have been aimed at both the First and Last Miles, i.e. sending and receiving markets.

Competition drivers in remittance markets

21. Remittances originally came to the forefront of the attention of development practitioners in recent years primarily because of concerns that high prices and lack of competition were placing a severe burden on low income migrants and their families.[11] In addition, migrants and their families have little access to mainstream financial services that might ideally offer more options for the transfer and use of remittance moneys.

22. Nonetheless, increased use of technology and globalisation of capital markets has decreased the scale at which many financial services can be provided efficiently and profitably. Accordingly, the cost of offering financial services has fallen sharply. This has spurred many developed and developing country policymakers to emphasize strongly the efficient provision of financial services appropriate to low income individuals, families and businesses. The competitive landscape of the remittances industry has been examined as part of this movement because remittances are being seen as a platform from which to not only lower the cost of commonly used financial services but also to improve access for low-income groups to a range of financial services. Thus, the ability to cross-sell and offer other services may be one of the keys to increasing competition and efficiency in remittances markets.

23. Indeed, in many corridors, remittances illustrate more mature qualities closer to the ideal of perfect competition – substitutability of services by many providers, sufficient market information, low switching costs and no ability to exercise market power. Many geographically definable service corridors are being served by multiple providers offering money transfer services of similar price and quality standards for the most common cash-to-

cash service. New entrants and growth of incumbent RSPs of various sizes has helped bring down prices, as has policymakers' focus on ensuring more transparent information is provided about prices, services, payment and pick-up locations, time-to-receipt and foreign exchange levels. Consumers in highly trafficked markets or dense communities of immigrants may often substitute services, switching to alternative services of more or less comparable quality should any particular agent decide to raise prices. As with model competitive behaviour, the threat of new entrants is sufficient to keep profits at "normal" levels in these corridors. Some product differentiation has started to occur as a response to increased competition and commoditization of basic services; as a result, new payment instruments and cross-marketed services have been brought into the marketplace. The United States - Mexico corridor is the most prominent example of such a market in the United States. The Spain - Ecuador corridor could be another illustration.

24. Nonetheless, many corridors in global remittance markets, including certain LAC corridors, do not illustrate ideal circumstances for increased competition. Despite relatively homogeneous cost structures, substantial price differences persist, especially when the service is to smaller countries with weaker financial infrastructure. In contestable markets, entry and exit occur with minimum friction and low sunk costs, or that the potential for entry is sufficient to ensure that competitors are earning normal profits and producing efficiently.[12] In this case, onerous regulatory hurdles, difficulties for RSPs to secure bank accounts and the cost of organizing acquisition and distribution networks represent the major barriers to new entrants. Likewise, information about prices and services continues to be inadequate in even some dense and well-known corridors (World Bank 2005, Migrant Remittances newsletter 2005). Finally, access to payment and settlement infrastructure has been denied many classes of institutions, such as credit unions, that might encourage more competition. These issues, as well as others, have raised awareness of barriers to entry and potential sources of non-price competition in the remittances market.

25. Definition of the geographic market in question also poses important questions, firstly because remittances take place across borders. Second, because migratory patterns tend to generate highly concentrated communities of migrants in host countries as well as many far smaller and dispersed communities, remittances are not always transmitted across corridors that are easily geographically identifiable.[13] Determining the relative importance of primary corridors vs. smaller ones and defining the spatial extent of the sending and receiving market also influences pricing and competition more broadly.

26. Certain corridors are easy to identify, the largest in particular, from the United States to countries such as Mexico, Dominican Republic or Colombia. In other cases, they may be difficult to pinpoint because they overlap with other markets, or because the community has a lower profile, is more dispersed, is smaller or isn't very organised. These secondary corridors feature far less competition. This might be the case for Argentina, Honduras and Belize. In the United States, as immigrants from the LAC region move to less densely populated areas of the country, geographic corridors have proliferated. On the receiving side, remittances are often distributed to rural areas that disperse the receiving side flow into small sub-markets.

27. In addition, some large individual markets have multiple "centres" that are served to different degrees such that the actual geographic scope of one urban market may be much larger than the immediate area. For instance, there is a substantial Dominican presence in several New York boroughs and counties outside of their well-known concentration in upper Manhattan, such as Queens, Staten Island and Brooklyn. Availability of services

differs, as do prices, despite the short distance between these centres. Some people may still prefer to travel to the more heavily concentrated service network to obtain better prices. There is little documented evidence of this phenomenon, but it exists wherever senders or receivers must cope with substantial distances to obtain convenient and cost-effective remittance services.

28. In addition, many institutions in this industry are not mainstream financial institutions but rather retail firms offering payment and other alternative financial services.[14] Given that retail money transfer services have been added to the global agenda against money laundering and terrorist financing, as embodied in the recommendations of the Financial Action Task Force (FATF), remittances require additional effort by a range of public authorities in Latin America. In this light, the involvement of national competition authorities in remittances should represent expanding interest among governments in broadening the current dialogue to ensure that regulatory action does not undermine the goals of increasing competition.

29. Among other unique challenges, competitive conditions in a remittance market or corridor are jointly determined in both the originating country and the receiving country. Competition agencies thus must determine what efforts on the part of receiving country authorities might have a relevant impact on competition overall. This requires an evaluation of what aspects of the competitive landscape derive from market structure in the receiving country as opposed to the sending country.

30. The remittances market is still evolving. Challenges to a more competitive landscape are associated with market power as well as regulatory burdens, supply of and demand for mainstream financial services, poor infrastructure and lack of physical access.

31. In forthcoming sections, this paper explores key themes related to competition in the remittance markets. Certain questions have not been addressed directly, especially those that would normally require high frequency pricing data, which is currently unavailable. Coming sections focus on the following elements: use of informal and formal services; analysis of prices; industrial organisation and market structure; origination and distribution networks; services and products; and financial access.

32. The following major issues related to competition in remittances markets will be highlighted in coming sections:

    RSPs face competition from unregulated informal money transfer providers throughout Latin America, especially where financial infrastructure is less developed and regulatory barriers are onerous.

    The economics of the remittances industry presents important structural challenges for competition: high upfront business establishment costs, geographic fragmentation of remittance markets, less developed receiving side financial infrastructure, difficult identification of acquisition and distribution partners and large players' first mover network advantage.

    The major global players are able to exercise market power by charging higher than average prices in certain geographic corridors depending on local competitive conditions.

Exclusive distribution contracts with major global players also appear to restrict competition by reducing the number of viable distribution points for other RSPs.

Competition among medium-sized and smaller players may feature sporadic episodes of predatory pricing as new entrants and services introduce more options to senders and receivers.

The most significant entrants, commercial banks, have not yet engaged actively in the market, nor has competition on the basis of innovation and service differentiation been very effective.

Regulation in sending countries is increasingly stringent, especially following September 11, and often applied in redundant or inconsistent fashion.

Receiving countries' regulatory framework may also generate obstacles, primarily by restricting certain types of institutions from participating in the market.
Existing public sector infrastructure – Central Bank, state-owned financial institutions, public sector programs and postal networks – may be more effectively deployed. Mexico, Brazil, Ecuador and Guatemala have all leveraged public infrastructure toward increasing the potential number of remittance distribution points to varying degrees.[15]

33. Lack of data precludes a detailed analysis or the ability to reach more than preliminary conclusions, but this report also suggests areas that may benefit from additional follow-on work.

International institutional responses to increase competition

34. Even before most individual countries had begun to think about remittances as a policy priority, further attention from public authorities, international development agencies and civil society organisations (such as migrant support associations), as well as from the RSPs themselves - has helped to improve information about the industry. This has helped to increase competition dramatically in most remittance corridors. More importantly, stakeholders in remittances – governments, the private sector, civil society and migrants themselves – have vigorously pursued the objective of increasing competition in the industry.

35. Multilateral donors and related institutions have established principles that relate directly to the competitive landscape for remittances. The recent consultative group report of the Committee on Payment and Settlement Systems sets out a thorough statement of General Principles for International Remittance Systems (Text box 1) that encompasses several aspects of remittances and actions that can be taken to facilitate efficient payment of remittances. The Multilateral Investment Fund's Core Remittance Principles (Text box 2) goes further in addressing the various stakeholders with tailored recommendations for constructive engagement. The Inter American Development Bank, the World Bank, the Asian Development Bank, the International Monetary Fund and others have published multiple volumes on remittances to illuminate aspects of the remittances industry and improve the flow of information.

Box 1. General Principles for International Remittances published by the Committee on Payment and Settlement Systems (CPSS)

General Principle 1. The market for remittance services should be transparent and have adequate consumer protection. General Principle 2. Improvements to payment system infrastructure that have the potential to increase the efficiency of remittance services should be encouraged. General Principle 3. Remittance services should be supported by a sound, predictable, non-discriminatory and proportionate legal and regulatory framework in relevant jurisdictions. General Principle 4. Competitive market conditions, including appropriate access to domestic payments infrastructures, should be fostered in the remittance industry. General Principle 5. Remittance services should be supported by appropriate governance and risk management practices.

Source: CPSS 2006

36. Bilateral donors have made direct interventions as well. Those related to Latin America have come from the United States, Spain, Japan and Portugal although countries such as Italy and Switzerland have likewise begun to receive more South American migrants and formulate policies accordingly. These efforts on the part of bilateral and multilateral donors, and the ever-multiplying array of new initiatives, have accomplished much in many Latin American corridors. Transparency regarding prices and services has improved with falling prices (by more than 50% in certain markets). Service options have begun to expand. The financial architecture used for money transfer is being adapted to allow increased access for a wider range of RSPs.

Box 2. Multilateral Investment Fund Remittances Principles

Core Principles for Remittance Institutions Improve Transparency Promote Fair Competition and Pricing Apply Appropriate Technology Seek Partnerships and Alliances Expand Financial Services Core Principles for Public Authorities Do No Harm Improve Data Encourage Financial Intermediation Promote Financial Literacy Core Principles for Civil Society Leverage Development Impact Support Social and Financial Inclusion

Source: Multilateral Investment Fund, Inter American Development Bank. For more information: **www.iadb.org/mif/remittances/mif/principles.cfm?language=EN&parid=2**

37. Although institutional capacity to address recommendations such as those espoused in the CPSS General Principles and the MIF's Core Remittance Principles has improved in sending countries, counterpart efforts in receiving countries are developing slowly and often with the donors' technical assistance. Mexico is an example in Latin America of a

government that has both worked independently, as well as with international partners, to define its ongoing programs in remittances. Other countries are working to develop procedures and resources and capacity to collect and disseminate data.[16] There are also examples of international cooperation to reform regulatory and supervisory frameworks, such as that between Guatemala and the United States.

Remittances markets in Latin America: major themes

Informal vs. formal money transfers

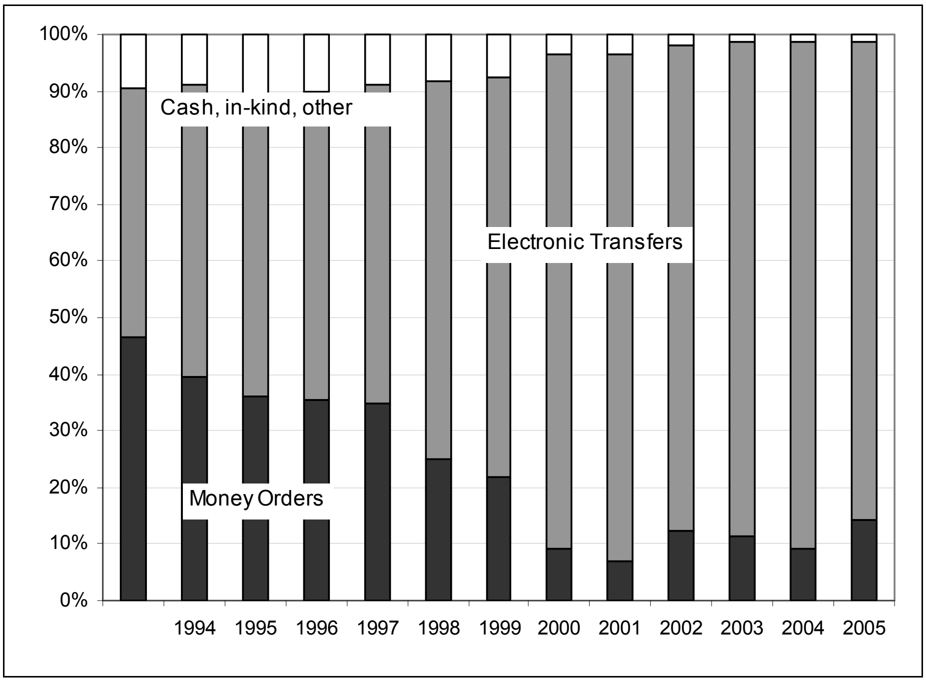
38. Remittance senders do not always use formal institutions and electronic methods (see Table 1). [17] In fact, the volume of informal transfers globally is such that including them may increase the total amount by 50% (World Bank 2005). Among all senders of remittances to Latin America in the United States, for instance, a Bendixen and Associates survey in 2004 found that on average 13% of senders use either people travelling or mail services to send their remittances (Bendixen 2004). The volume of Latin America's informal transfers has probably fallen substantially in recent years, if Mexico's experience and the entry of new RSPs aimed at Latin America is any indicator (see Graph 4).

Table 1.
Use of formal and informal transfer channels to Latin America

Sending country	Receiving country	Formal	Informal
United States	Mexico	90%	10%
	El Salvador	85%	15%
	Dominican Republic	86%	14%
	Guatemala	87%	13%
US/Spain	Ecuador	86%	14%
Japan	Brazil/Peru	93%	5%

Sources: Banco de Mexico, Remittances and Development: The Case of Mexico, June 2005. Receptores de Remesas en Centroamerica, Sept 2003. Remittance Recipients in the Dominican Republic and Remittance Senders from the United States. Receptores de Remesas en Ecuador: Una Investigacion del Mercado. Note: The World Bank's Global Economic Prospects 2006 *makes use of household survey data that indicates far lower levels of informal channel usage in Latin America – closer to 5% for Mexico, Dominican Republic and Guatemala but 15% for El Salvador. This may be a question of definition, but household surveys generally carry the caveat of underreporting.*

Graph 4. Mexico: Remittances and mode of transfer (as % of total)



Source: CONDUSEF, Banco de México.

39. Further price declines could encourage increased use of formal transfers. Although prices for money transfers have fallen globally, simulations indicate market sensitivity to price declines in formal sector money transfer offerings. World Bank (2005) estimates that the increase in formal sector remittances to Latin America would be in the range 50% - 100% if the cost of formal sector remittances converged to that of the informal sector range of 2%-5% and dual exchange rates were eliminated.

40. The persistence of informal transfers in certain markets has specific relevance for competition agencies. It may be worthwhile to determine what market conditions drive these informal flows. An analysis of informal flows may indicate problems of price and non-price competition, such as the existence of dual exchange rates, poor distribution networks (especially in rural areas) and high prices for remittance transactions (World Bank 2005). Financial literacy or low educational attainment in general, as well as discomfort or bad experiences with financial services, may also cause migrants to persist in using informal means. Such an inquiry would serve the double objective of governments wishing to encourage increased adoption of formal channels.

41. The incidence of informal transfers also relates to regulation and enforcement in that laws and regulations, or their uneven application across institutions, affects competition. Andreassen's survey of MTOs (2006) cites informal remittance providers who face no or very weak regulatory and supervisory attention as a major factor relating to competition. Because informal institutions do not face equivalent regulatory scrutiny, a disproportionate burden may be placed on firms of a size that does merit the attention of the authorities (Andreassen 2006). While the balance between cost of supervision and risk must always be considered, competition agencies may help to quantify the impact of informal transfers on competition in specific corridors.

Pricing and Price Competition

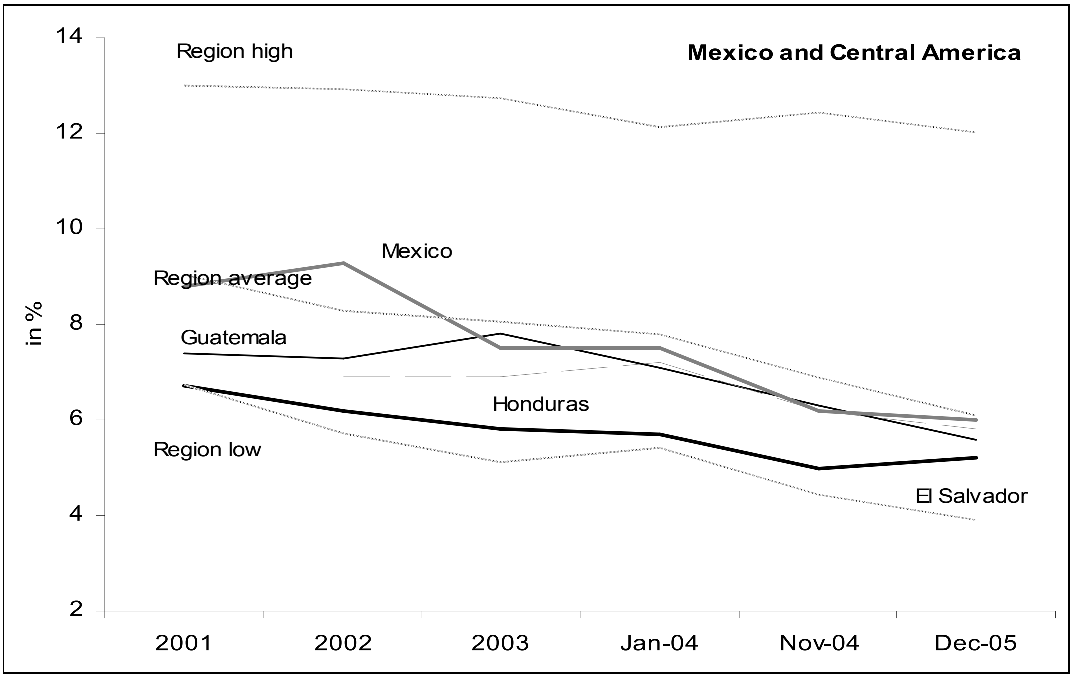
42. High prices for money transfer to Latin America in the 1990s – as well a marked lack of transparency - triggered the current elevated attention to remittances as a development issue due to their heavy burden on the poor. High prices are also associated with increased use of informal transfer channels, which are neither secure can easily estimated or monitored (World Bank 2005). If lower cost transactions can be combined with improved financial access, then remittances may be an effective tool for encouraging increased financial intermediation.

43. Although small payments continue to face high prices, one of the major developments in remittance markets in Latin America in recent years is a sharp decline in remittances fees in many markets, as illustrated in figures 4, 5 and 6.

44. One reason for high prices lies in the characteristics of demand for money transfer. Most services can be considered experience goods because their price/value characteristics are difficult to judge a priori without having executed a transaction. Risk aversion helped generate competitive inertia in the favour of MTOs, allowing them to exercise market power for many years, in the absence of the participation of other institutions such as other MTOs or banks. MTOs also offer superior customer attention and targeted marketing (Orozco 2006). Global firms such as Western Union, MoneyGram and DolEx also feature large sales and distribution networks in immigrant neighbourhoods. As a result, customers are highly satisfied (Orozco 2006, Bendixen 2005).

45. Over time, competition among MTOs has commoditized money transfer. In certain markets, remittances are now more like search goods such that consumers can easily compare services and prices. New entrants have increased contestability of major markets, contributing to falling prices. Orozco (2006) also finds that lower remittances costs are associated with higher volumes, lower foreign exchange spreads and a larger number of companies in the market.

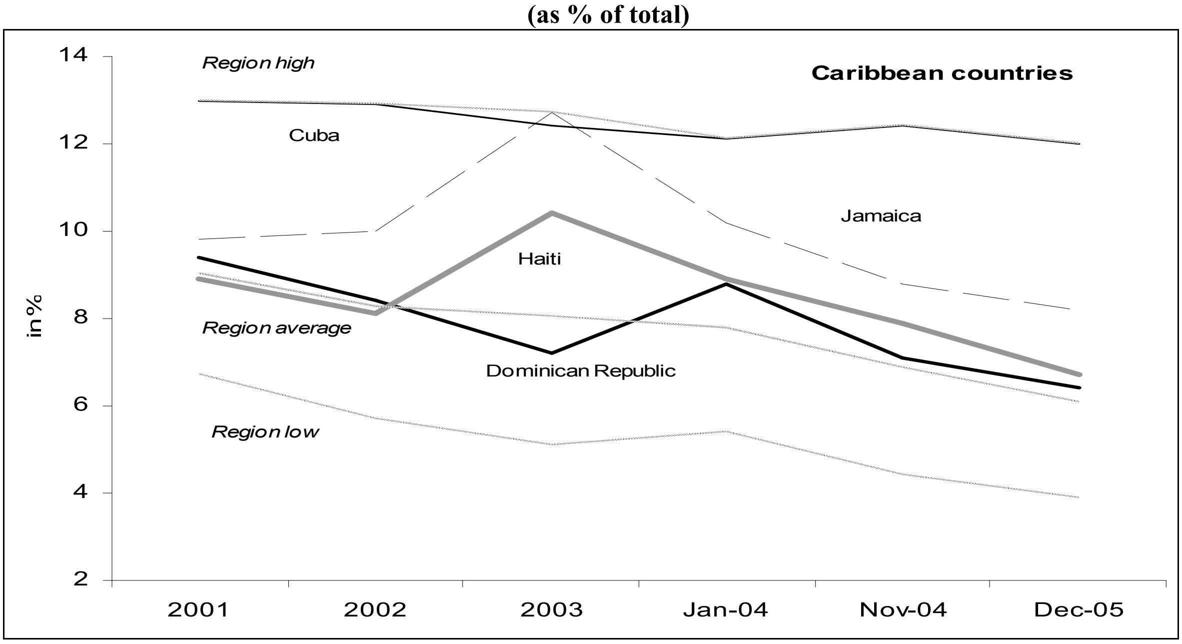
Graph 5. Average prices for remittances to Mexico and Central America from the United States (as % of total)



Source: Orozco 2006.

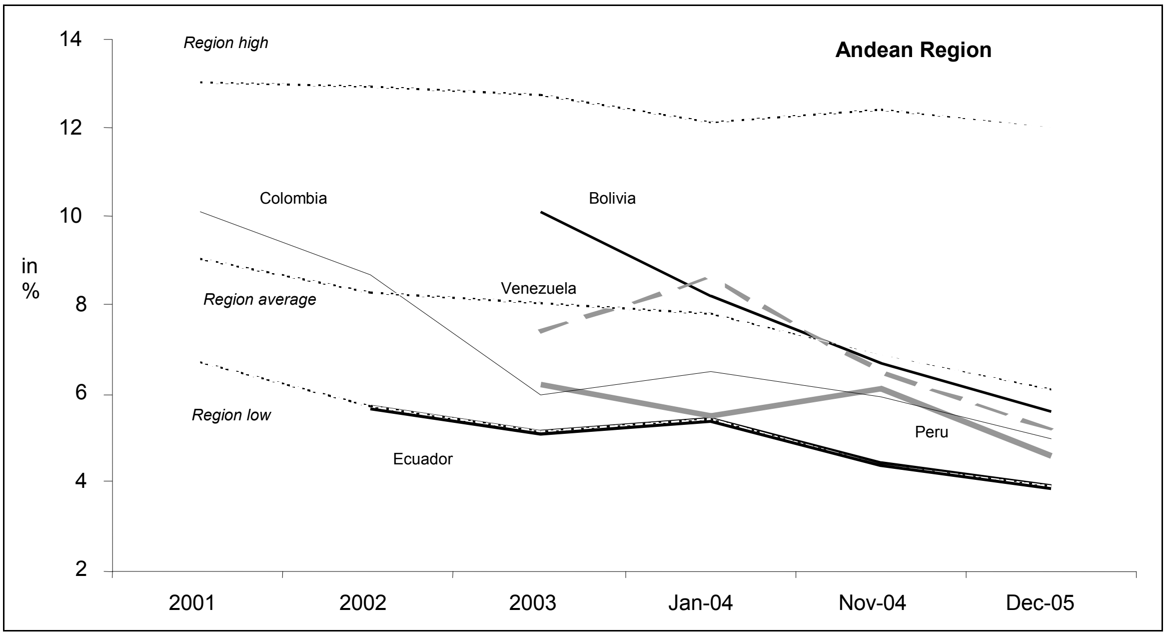
46. A wide range of prices is charged on average for remittances to the LAC region. Ecuador has typically has the lowest prices, while money transfers to Cuba are the most expensive in the region. Cuba has placed tight controls on foreign currency but also suffers from weak financial infrastructure and the US boycott on trade.[18] Prices to send money to Mexico and Central America are below the regional average while the Caribbean is higher (although Cuba skews the average). Prices in the Andean region are likewise below average. Each receiving market varies in its financial infrastructure, industry organization and regulatory and policy framework.

Graph 6. Average prices for remittances to the Caribbean from the United States (as % of total)



Source: Orozco 2006.

Graph 7. Average prices for remittances to Andean countries from the United States (as % of total)

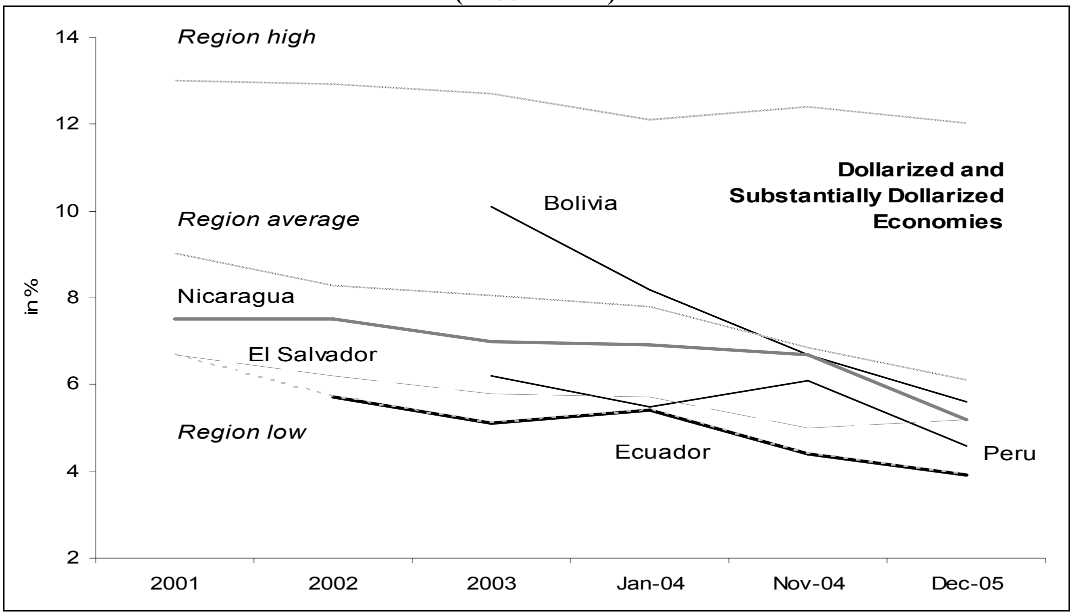


Source: Orozco 2006.

47. Fees for remittance services can be complicated for senders and receivers to understand. Pricing is sometimes based on a percentage and sometimes a flat fee, in both cases usually with a minimum floor fee to discourage small transactions. The fee structure tends to be regressive in that small transfers face proportionately higher fees (World Bank 2005). The transaction fee and the charge of a foreign exchange spread are the two most common components of the price of a remittance. Receiving institutions may occasionally charge an additional fee for home delivery or receipt in a remote area. It may also be difficult to know if a remittance transferred through correspondent banks will require an additional processing charge on the receiving side (CPSS 2006). The new money transfer service offered by certain banks also does not provide a fixed foreign exchange rate at the time of the transaction's origination, but rather only at settlement, worsening the lack of transparency to the customer.

48. There are few systematic efforts to educate remittance senders or receivers about prices at an accessible level.[19] RSPs do not always provide full information. Because fully dollarised economies can pay out remittances in U.S. dollars, eliminating the foreign exchange risk to institutions, some analysts have suggested that dollarised economies have experienced lower price declines and but enjoy lower prices in general (Orozco 2006, World Bank 2005, de Luna Martinez 2005). Although graph 8 indicates lower than average costs in dollarised and substantially dollarised economies, differences with other non-dollarised economies are not appreciable. In addition, because the foreign exchange spread is an important source of profit for RSPs, it might seem more likely that commissions would rise to compensate. This also does not seem to be the case.

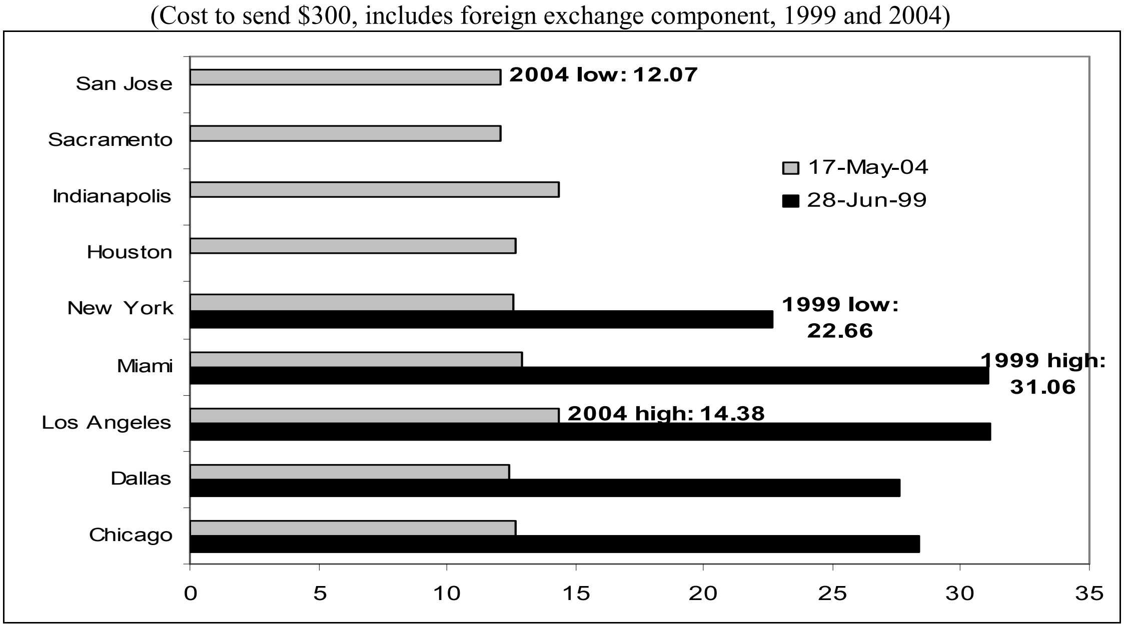
Graph 8. Average prices for remittances to dollarised countries from the United States (as % of total)



Source: Orozco 2006.

49. Costs to send money have been most thoroughly researched in Mexico by consumer protection authorities, Condusef and Profeco. Their studies reveal that substantial variation in prices has narrowed since 1999 but that a relatively wide range of prices for the same service is still charged across different cities. By mid-2005, the low of 2.5% and the high of 6% still represent a difference of $7.50 to $18.00, or $100-$200 per year. Among cities, the maximum average difference is approximately $3.00. RSPs explain that such differences are explained by the state of competition in individual markets. As illustrated in graph 9, Profeco found that the differential between maximum and minimum prices of money transfer among cities shrank from 1999 to 2004. Nonetheless, in 2004, there was still a difference of $2.21 in a selection of major sending cities for Mexico from the United States.

Graph 9. Total cost of money transfer from United States to Mexico
(Cost to send $300, includes foreign exchange component, 1999 and 2004)



Source: Profeco, Mexico.

50. Analysts disagree about whether migrants consider the price of a transfer service an important factor in determining demand, arguing that migrants are more concerned about convenience, speed, trust and security. The World Bank's Global Economic Prospects insists that prices can be brought down further, pointing out the gains that would come from formal prices converging to that of informal transfers, as highlighted in the discussion about informal transfers.

51. It has been suggested that one means of improving transparency and price competition in the market would be to allow disbursement of remittances in foreign currency so that all parties know exactly how much is being sent, received and paid for the commission. Also, in that way, recipients might seek better exchange rates away from the RSP (CPSS 2006).

52. In fact, migrants and their families are rarely offered the option of sending/receiving money in foreign currency (Orozco 2006). Some firms may indicate that they offer disbursement in US dollars, but in fact, they receive the money in local currency, with the foreign exchange spread already subtracted, and then charge an additional foreign exchange spread on top of that. Not surprisingly, this is not a popular option.

53. Nonetheless, especially the case during periods of high currency volatility or inflation, many migrants would prefer to receive foreign currency because of the disadvantageous foreign exchange spread charged on transfers received in local currency. As an example, firms in the Dominican Republic must by regulation disburse in the currency specified by the sender. When the currency depreciated rapidly during the most recent economic and financial crisis, the volume of transfers denominated in dollars grew rapidly. MTOs placed a large premium on transfers disbursed in US dollars (illustrated in table 2). Interestingly, the ability to receive remitted funds in dollars allowed commercial banks to offer remittance receivers a new promotion, in which dollars brought into the bank would be exchanged at a better rate than that given by the MTOs.

Table 2.
Commission for sending $150 from New York City to the Dominican Republic

	Pesos		Dollars	
Money Gram	12.5	8.33%	17.0	11.33%
Mateo Express	12.5	8.33%	17.0	11.33%
Pronto Envio	12.5	8.33%	17.0	11.33%
Cibao Express	12.0	8.00%	17.0	11.33%
Western Union	10.0	6.66%	22.0	14.67%
Quisqueyana	7.5	5.00%	12.0	8.00%
La Nacional	5.0	3.33%	12.5	8.33%
Pujol	5.0	3.33%	11.0	7.33%
Agil	4.5	3.00%	7.5	5.00%
RIA	3.0	2.00%	7.5	5.00%
BHD	3.0	2.00%	17.0	11.33%
CAM	2.0	1.33%	14.0	9.33%

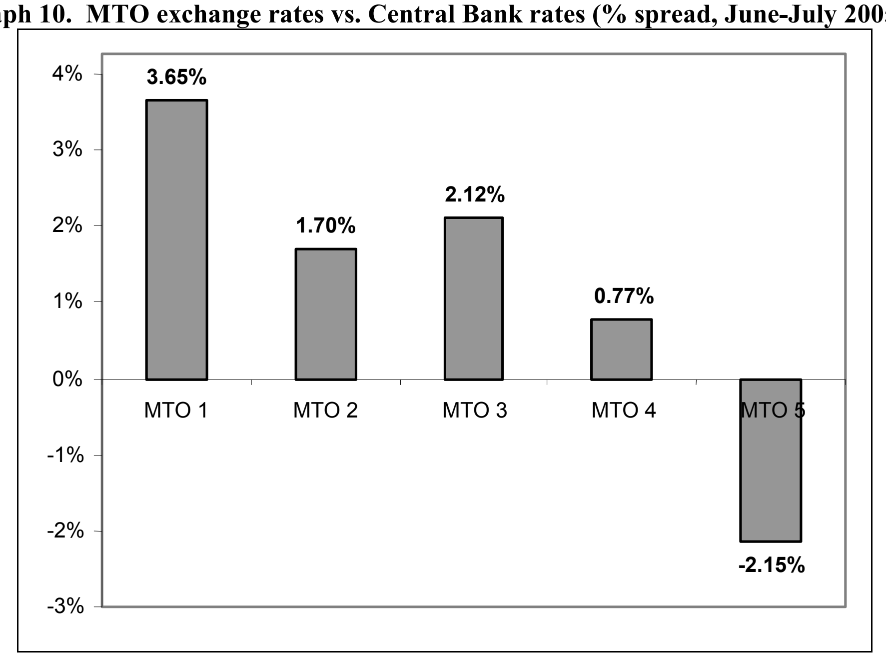
Source: Author's survey conducted November 12, 2004. All firms except one contracted to exchange funds into pesos at 25.75. The Central Bank's published rate to buy dollars on November 12 was 27.50

54. Modifying regulations to allow senders and receivers to specify foreign currency disbursement may promote new competition by forcing firms to calibrate their commissions and foreign exchange separately. This would have the effect of removing one profit source from MTOs. It may also affect competition in the sense that it would clearly favour firms with ready internal access to foreign exchange vs. incumbent firms (MTOs) who do not. In addition, managing foreign currency denominated liquidity creates new costs for MTOs versus commercial banks, who may already be accustomed to executing financial transactions in foreign currency. Regulatory constraints may make it difficult to manage such a change. Such adjustments would also have to be made consistent with the objectives of monetary policy authorities.

55. Certain firms have used the foreign exchange spread as a means of increasing market share. Commercial banks transacting foreign exchange in large amounts may have a natural advantage in this. Banks tend not to require a further intermediary in order to transact in foreign currency. Other intermediaries not authorized to trade foreign currency – credit unions, for example - would need to obtain that service from a bank. By contrast, most commercial banks have their own foreign currency trading desk. As a result, banks that trade foreign currency in large volumes for multiple business purposes may transact at better (smaller) spreads. Some banks may then pass this advantage onto the client by offering a more aggressive and lower foreign exchange spread than other RSPs (although this has not been systematically studied and proven).

56. The findings of the US GAO in Mexico (see graph 10) illustrate that MTOs charge a range of different exchange rates. In Guatemala, for instance, remittance recipients perceive that Banrural offers among the best foreign exchange rate of remittance payers. All things equal, recipients may prefer to receive their remittances in the institution that offers the best foreign exchange – therefore, the highest payout per amount sent – even if they subsequently take the funds to their depository institution.

Graph 10. MTO exchange rates vs. Central Bank rates (% spread, June-July 2005)



Source: GAO 2005.

57. In some countries, businesses are being permitted to share pricing information, thereby allowing them to maintain higher prices than would be expected in a competitive market. The Dominican Republic provides an example. MTOs have established an association for public advocacy purposes called ADEREDI (Asociación Dominicana de Empresas Remesadoras de Divisas). In addition to representing the industry in discussions with government and regulators, this organisation sets foreign exchange reference rates for the use of its members. The Dominican Republic seems to be the only country in which such an institution exercises such an impact on a major component of transfer pricing. This may be explained by the fact that Dominican corridors also feature Dominican-owned MTOs that have built out their own customer acquisition and distribution networks, rather than focusing solely on the receipt and distribution of funds.

Table 3.

Money transfer Chicago to Mexico			**Money transfer Los Angeles to Mexico**		
RSPs (banks in shading)	Total cost (USD)	Pesos received	RSPs (banks in shading)	Total cost (USD)	Pesos received
** CIME / Bancos Participantes	3	3,294	** Citibank Global Transfers. *Cuenta a Cuenta*	5	unknown
** Merchants and Manufacturers Bank. *Directo a Mexico/Fed ACH*	3.50	unknown	** US Bank. *L@Red de la Gente*	8.27	3,291
** Citibank Global Transfers. *Cuenta a Cuenta*	5	unknown	Order Express	8.82	3,285
Ria Envia	5.67	3,336	Majapara. *PagaDólar*	9	3,294
** US Bank. *L@Red de la Gente*	8.27	3,291	MoneyGram. *Cambio Plus*	10.26	3,291
Order Express	8.82	3,285	Majapara. *Maxipaga*	10.63	3,342
Majapara. *PagaDólar*	9	3,294	Western Union. *Giro Telegráfico*	10.81	3,285
MoneyGram. *Cambio Plus*	10.26	3,291	Western Union. *Dinero Día Siguiente*	11.63	3,276
Majapara. *Maxipaga*	10.63	3,342	Ria Envia	14.17	3,336
Western Union. *Giro Telegráfico*	10.81	3,285	Western Union. *Dinero en Minutos*	16.63	3,276
Western Union. *Dinero Día Siguiente*	11.63	3,276	** US Bank. *Tarjeta Secure Money Transfer*	17.65	3,210
Western Union. *Dinero en Minutos*	16.63	3,276			
** US Bank. *Tarjeta Secure Money Transfer*	17.65	3,210			
Delgado Travel	26.48	3,135			

*Source: Condusef, Mexico. ** denotes services offered by commercial and community banks acting as the RSP rather than agent for another MTO.*

58. Table 3 highlights that a range of prices that may exist in a given corridor, even in heavy flow corridors. Western Union's instant payment product, Dinero en Minutos, in many markets is the most expensive MTO. However, the entry of Delgado Travel (an Ecuador corridor specialist) has brought a new higher priced alternative. The new transfer products offered by banks (denoted with ** in the table above) are competitively priced in most cases but the service standard is slower delivery, though often not much longer than 1 day.

59. Tables 4 and 5 illustrate service to Ecuador from cities with large Ecuadorian communities in the US and Spain. The first table illustrates that money transfer from various cities may be priced differently despite money transfer being a homogeneous product in reflection of varying market conditions in different sending locations. It also shows that financial institutions have some offerings that are comparable to the market, but the second table, provided by a non-profit that tracks prices, indicates that some traditional bank money transfer services are the most expensive. Western Union and MoneyGram are the most expensive in almost every market, which highlights their market power and the ability to leverage their extensive distribution networks.

Table 4.
Money transfer to Ecuador (send USD 300 equivalent)

	USD	% of principal	Delivery time
New York			
Western Union	12	4%	Instant
Money Gram	9.99	3.33%	Instant
Delgado Travel	9	3%	Within hours or next day
Ria Envia	6	2%	Within hours or next day
Newark			
Western Union	15	5%	Instant
Money Gram	10	3.33%	Instant
Delgado Travel	9	3%	Within hours or next day
Dolex	8	2.67%	Within hours or next day
Ria Envia	6	2%	Within hours or next day
Chicago			
Western Union	11.99	4.00%	Instant
Money Gram	10	3.33%	Instant
Delgado Travel	9	3%	Within hours or next day
	7	2.33%	Within hours or next day
Ria Envia	6	2%	Within hours or next day
Dolex	6	2%	Within hours or next day
Barcelona	€		
Western Union	10.03	3.93%	Instant
La Caixa (no account)	9	-	Next day
Ria	6	2.40%	Within hours or next day
Dolex	3	1.20%	Within hours or next day
Dinero Express	3	1.20%	Unknown
La Caixa (with account)	3.9	-	Next day
Madrid	€		
Western Union	12.35	4.86%	Instant
Caja Madrid	9	-	Within hours or next day
Money Gram	8.9	3.53%	Instant
Banco Popular (no account)	7	-	Next day
Ria Envia	5	2.03%	Within hours or next day
Dolex	3	1.20%	Within hours or next day
Dinero Express	3	1.20%	Unknown
Banco Popular (with account)	4	-	Next day

Online	USD	
XOOM	29.9	9.67%
Western Union	15	5.00%
Money Gram	18	6.00%
Ikobo	14	4.67%
Cashpin	20	6.67%

Source: Author's inquiries conducted April 6, 2006. Where no total price is provided, the respondent could not give a foreign exchange reference rate.

Table 5.
Money transfer from Spain to Ecuador (March 2006)

Licencia Banco de España	Nombre de la empresa remesadora	¿Cuánto llega en US$?	¿Cuánto cuesta en %?
1725	LATINOENVIOS	173,6	3,79
1745	GIROEXPRESS	173,1	4,05
1744	UNIGIROS EXPRESS	172,8	4,21
1707	UNO MONEY TRANSFERS	172,3	4,47
1716	MACCORP EXACT CHANGE	171,6	4,86
1746	GEOMIL TRANSFER	171,5	4,93
1736	MASTER ENVIOS UNIDOS	171,4	4,96
1752	TRANS FAST FINANCIAL SERVICES	170,7	5,35
1730	CHANGEPOINT	170,2	5,63
1737	ENVIA TELECOMUNICACIONES	170,1	5,68
1706	R.D. MONEY TRANSFER	169,9	5,81
1717	Money Express (ex-Change Express)	169,9	5,83
1729	CAMBIOS SOL	169,9	5,83
1747	HISPANO WORLD TRANSFER	169,9	5,83
1718	SAFE MONEY TRANSFER SPAIN	169,7	5,94
1720	UNITED EUROPHIL	169,4	6,09
1741	INTERENVIOS MONEY TRANSFERS, S.A	169,4	6,09
1753	BBVA DINERO EXPRESS	169,4	6,11
1740	TELEGIROS	168,2	6,76
1756	TITANES TELECOMUNICACIONES	168,2	6,76
1713	FOREIGN EXCHANGE COMPANY	167,6	7,08
Transferencia	Cajamadrid-Transferencia a Produbanco	159,6	11,54
Transferencia	Caixa-Transferencia a Banco del Pichincha	159,3	11,69
Transferencia	Cajamadrid-Transferencia a Banco de Guayaquil	158,0	12,41
Transferencia	Caixa-Transferencia a Banco de Guayaquil	151,3	16,11
Transferencia	Caixa-Transferencia a Produbanco	149,0	17,40
Transferencia	BBVA-Transferencia a Produbanco	147,7	18,14
Transferencia	Cajamadrid-Transferencia a Banco del Pichinch	147,0	18,51
Transferencia	Santander-Transferencia a Banco del Pichincha	146,4	18,84
Transferencia	BBVA-Transferencia a Banco del Pichincha	145,1	19,55
Transferencia	Santander-Transferencia a Banco de Guayaquil	139,4	22,73
Transferencia	BBVA-Transferencia a Banco de Guayaquil	139,0	22,93

Source: Remesas.org.

60. Thus far, the author has found little systematic evidence of differentials in price depending on the receiving location, for instance to a more rural or remote area, but this has not been systematically explored. However, recipients in rural areas do face higher prices, often due to transportation to the nearest urban centre for pick-up. Alternatively, there may be a delivery fee. Finally, remote, rural microfinance institutions have been known to charge a small additional fee to compensate for the additional administrative cost of receiving transfers where telecommunications infrastructure and liquidity are lacking.

61. Product and service innovations new to the market, such as ATM and stored value cards, have failed to have much impact on consumer demand thus far (Suki 2004, Suki 2006, Orozco 2006). The prices for using these services can be non-transparent and, at times, more expensive than receiving the transfer. Cards, for instance, may entail an initiation fee, plus a fee to load up the card and a fee for transfer, as well as individual charges per transaction. In most markets, these products have very low market share of between 1% and 5%.

62. The foregoing discussion suggests that several areas of inquiry remain to be investigated in order to analyze more systematically the behaviour of remittance prices in Latin American markets, among which:
A comprehensive comparative price inquiry that takes into account different sending and receiving locations;

Analysis of foreign exchange spread charges to determine whether certain institutions compete more effectively by systematically offering smaller foreign exchange spreads;

An analysis of market shares obtained by major distributors of remittances in the recipient market;

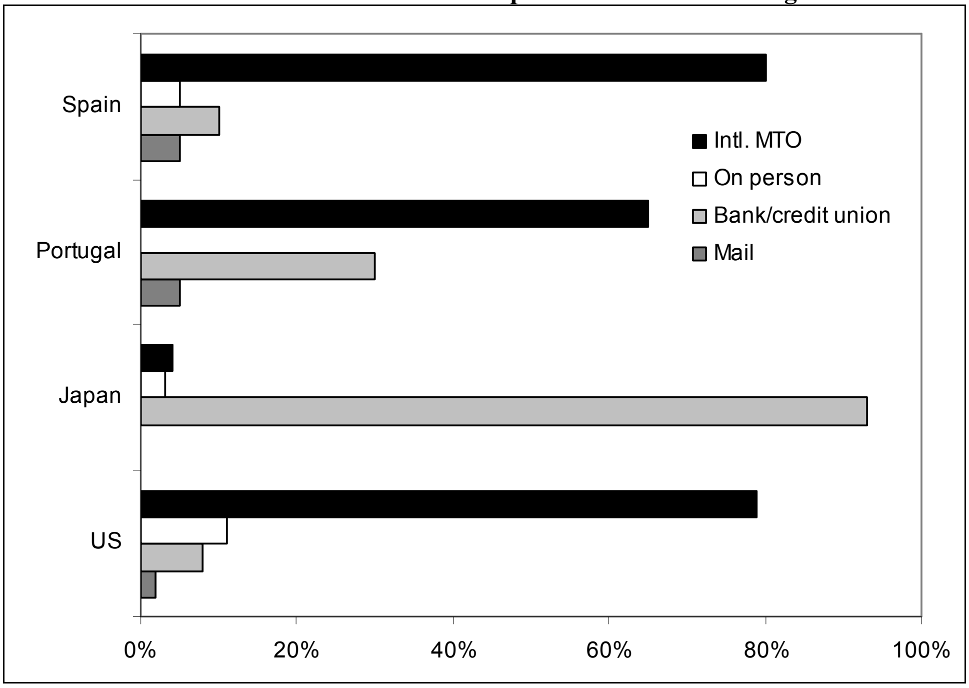
An evaluation of the pricing of new products beyond cash-to-cash transfers, such as dual ATM cards and account-to-account transfers.

A spatial analysis of remittance costs that highlights urban/rural disparities in access and integrates cost of transportation and expenses from high-migration areas.

Industry organisation: The dominance of money transfer companies and new entrants

63. This section highlights aspects of the remittance industry's organisation that have generated the current competitive landscape. It illustrates the dominance of money transfer companies in most remittance corridors to Latin America but also the increasing involvement of entrants among financial institutions. Business factors – revenue, cost and profitability drivers – are significant, especially due to high fixed set-up costs as well as ongoing costs of compliance and the risks entailed by the current regulatory environment. The importance of acquisition and distribution networks is related to exercise of market power.

Graph 11
Distribution of remittance service providers to the LAC region



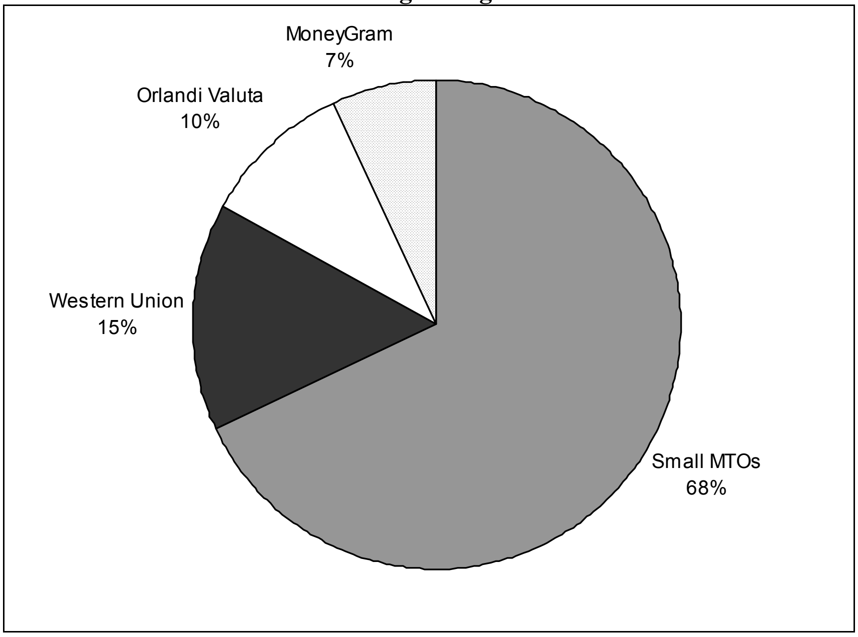
Source: Bendixen 2005.

64. The primary current market players in the remittances industry to the LAC region are MTOs, both small and very large, as illustrated in graph 11. In general, money transfer companies, firms that execute the money transfer, specialise in international remittances, offering few products or services in addition.[20] Large global multinational companies, such as Western Union, MoneyGram and DolEx, compete against medium-sized regional players, of which Delgado Travel or Vigo are good examples. Each country corridor also features a group of smaller corridor specialists.

65. The case of Mexico illustrated in graph 12 is typical of what exists in other countries in many ways. There are far more small companies than in other markets because of the fact that immigrants from Mexico are the most numerous foreign-born group in the United States and because there are so many more identifiable communities. Nonetheless, competition in most corridors features a similar industrial organisation with varying degrees of market power exercised by the main global players and multiple medium and small participants with smaller market shares.

66. Among other entrants, banks, credit unions and microfinance institutions have entered the market with the offer of new services at lower cost and sometimes bundled with other financial services. In Japan and Europe, depository institutions have entered the market more decisively with tailored products and marketing. In contrast with other sending countries, money transfer from Japan (primarily to Brazil and Peru) is dominated by depository financial institutions.[21] Nonetheless, the role of these institutions as RSPs, as distinct from distribution agents of MTOs in receiving countries, remains minor in the major markets, the US and Spain.

Graph 12.
Mexico – Market Share of Originating Institutions in June 2004



Source: Hernandez-Coss 2004

67. Postal networks have not been leveraged for remittances although new initiatives aim to change this, although these networks have developed more rapidly in parts of Asia and Africa.[22] Postal services have suffered from poor image and weak operational capacity. Therefore, they have not been exploited as a means of delivering financial services to rural populations in the LAC region.

68. Online services exist but are marginal players at the moment. They charge among the highest prices and tend to target Latin American and Asian migrants with credit, bank accounts and internet access – not a demographic that describes the majority of remittance senders from the LAC region.

69. Although MTOs are the primary intermediaries, these institutions do not act as market agents in a vacuum because of the importance of networks and alliances in the First and Last Miles, which will be discussed in an upcoming section. MTOs and many other RSPs, such as microfinance institutions, require bank accounts to operate.

70. Banks and credit unions have begun to offer a range of new products aimed at attracting remittance senders and receivers as new banking clients with lower costs and more value-added financial services. Banks' market share in the US remittance market lies in the range of 5% (GAO 2005, World Bank 2005). Banks promote low cost or free money transfers in all markets that include options such as account-to-account transfers, account-to-cash transfers or the use of dual ATM or stored value cards. Using financial institutions' services may be more cost effective in some cases but presents the challenge of encouraging migrants to open bank accounts.[23] Bank of America, Wells Fargo, Citibank, HSBC, US Bank, and many other community and regional banks have begun to offer low cost services of this nature in the United States, as have credit unions.

71. Credit unions have also made an important contribution as stakeholders. The establishment of the IRNet (or International Remittances Network) by WOCCU (the World Council of Credit Unions) with support from USAID.[24] Over $1 billion has been paid out since 2000 but, like banks, the experience has been difficult.

72. In relative terms, Spanish banks and credit unions – BBVA, Banco Popular, La Caixa and CECA - have all moved more aggressively to extend such services to migrants, also offering a range of additional financial services such as dual ATM cards, mortgage and personal credit and special savings accounts. La Caixa in Spain and Banco Solidario in Ecuador have developed the best known model, featuring a range of services that includes personal credit, mortgage financing in Ecuador, small business credit, account-to-account transfers, use of an ATM card in Spain and Ecuador and many other benefits. This has improved Banco Solidario's market share to nearly 10% - well above the banking average for the region.

73. Thousands of agents of MTOs help create the acquisition and distribution networks on which MTOs' competitiveness relies. These are the most salient First and Last Mile players in most LAC sending and receiving remittance markets. On the sending side, these agents are accessible to unbanked migrants and located in immigrant neighbourhoods in businesses with frequent foot traffic. Often immigrant-owned businesses, these businesses may be a hub of social interaction in an immigrant community, giving migrant senders an additional level of comfort in addition to the lower standard of identification than a bank. These agents may include small groceries, pharmacies, restaurants, beauty salons or other small business.

74. Alternative financial service providers are also natural partners as they provide a range of complementary services, such as check cashing, money order purchase, bill payment and payday loans - to the low income and unbanked. Package companies and tourism agencies are other examples. Likewise, agents may also be a bank or credit union branch acting as part of a system that is wholly or partially operated by the same financial institution acting as the RSP, as well as a post office, or the First Mile may be virtual for online services. None of these are as yet significant players with respect to the competitive landscape.

75. Agents fulfil the following needs: (1) convenience, security and accessibility; (2) professional management of financial services (especially for banks on the disbursement side); and (3) ability to manage disbursement liquidity.[25]

76. Agents also benefit from this relationship. Retail stores are common agents on both sending and receiving sides. Picking stores selling electronics and household appliances on credit as remittance partners with the implicit aim of selling goods is now common (in the case of Elektra in Mexico and many others). Informal remittances may also be received by check or money order (or in cash) to an agent with a bank account who can then disburse on the behalf of the sender.

77. Given that individual transactions are relatively small,[26] increasing volume and taking advantage of economies of scale is an important aim of those RSPs who specialise in providing only money transfer services. Revenues from remittance transactions are normally comprised of a fee for sending the money transfer (normally collected from the sender), a foreign exchange spread and occasionally a fee on the receiving side.[27] In theory, the foreign exchange spread allows the RSP a cushion against adverse currency movements between the time of transaction (and, therefore, commitment to a rate) and the time of settlement. However, in effect, it has become a source of profit and a fee in itself (World

Bank 2005). These firms focus on volume and standardisation of their product. Very few banks have pursued a similar strategy for many reasons.

78. Money transfer businesses face large up-front fixed costs related to establishing the business. The most important of these are licensing and bonding,[28] acquiring sales and distribution networks, investing in technology for transaction processing, compliance, reporting and record-keeping, meeting regulatory requirements and securing bank accounts (Andreassen 2006). World Bank (2005) suggests that the costs of running a remittance business are not very high, citing free or very inexpensive fees on remittances in some corridors and low fees for informal transfers and courier services. Even so, average business costs drop over time and only with scale when payments can be bundled, which drives the concentration of RSPs in densely populated immigrant communities. Some institutions (e.g. banks or alternative financial service providers) can spread costs over several business lines with complementary needs in terms of infrastructure, marketing, legal and compliance, etc. As Andreassen (2006) indicates that most RSPs are small- to medium-sized, many may not achieve sufficient returns to scale and, therefore, absorb higher average costs, which may be reflected in higher commissions, lower profits or constrained growth prospects.

79. Finally, MTOs face a cost that most other depository institutions do not; they require payments infrastructure through which to execute and settle transactions. The cost of maintaining bank accounts and transferring funds to disbursing agents via those institutions has become increasingly expensive and onerous in the United States and elsewhere due to stringent regulatory guidance from the FATF, the Patriot Act in the US and stringent domestic financial supervision (Andreassen 2006, Orozco 2006, Suki 2005).[29]

80. While depository institutions would seem to have certain cost advantages relative to other institutions based on these criteria, perceived operational risk has caused most to discount remittance services (see text box 3).[30] Also, their infrastructure for cross-border financial flows is primarily oriented towards large scale netting transactions rather than small, costly and personnel intensive retail payments.

The role of acquisition and distribution networks in competition

81. Acquisition and distribution networks are one of the core determinants of competition and market contestability in the remittance industry. Andreassen (2006) points out that successful MTOs tend to have large networks (see table 6). Franchised agents for RSPs,normally present on both sending and receiving sides, are the most common form of network building, but not all models make use of them. Many firms prefer full vertical integration, banks for instance, and, therefore, do not normally make use of agents but rather leverage their large branch networks. Other institutions may act as "gatekeepers" to regulate access to a network. Since no international money transfer platform exists that is open and freely available to all potential providers and bringing remittance operations to scale is important, networks play the important role of expanding the potential sales and distribution points to support large volumes of remittance transactions.

Box 3.
Commercial Banks in the US-Mexico Corridor

Mexico is an interesting case regarding competitive threat to incumbents posed by new entrants among the commercial banks. It differs from many countries in Latin America by the high proportion of banks that are foreign-owned following a spate of acquisitions triggered by the conclusion of NAFTA. Although many of these institutions have extensive retail distribution in the United States, where most Mexican migrants live, none of the recipient counterparts are sourcing important flows from their banking network in the United States. In fact, although Citibank and HSBC have their own money transfer products to Mexico from the United States, these have not as yet been actively promoted in the United States as part of a strategy to "bank the unbanked." On the receiving side, their counterparts, Banamex, HSBC-Mexico and Bancomer, all source the vast majority of their remittances from money transfer companies. In fact, Bancomer sources the majority of its transfers from its own MTO, Bancomer Transfer Services.

The Mexico case is instructive of the limited involvement of banks in channeling remittances. Many factors would suggest highly favorable conditions for their involvement, among which concentration of Mexicans in the United States, densely populated Mexican communities, management of the majority of foreign exchange flows between the two countries and retail banking networks on both sides of the border. Nonetheless, these institutions have made their most prominent contribution to remittances to Mexico either through MTO partners or by offering low cost financial services of restricted availability and access (to account holders). The other US commercial banks that have been more successful – Bank of America and Wells Fargo – have banking and retail partners in Mexico, which are not subsidiaries of those institutions.

Table 6.
Acquisition and distribution networks of major MTOs

	Points of service	Agents	Countries
Western Union	233,000	100,000	200
MoneyGram	80,000	39,000	150
Travelex Money Transfer	17,000		138

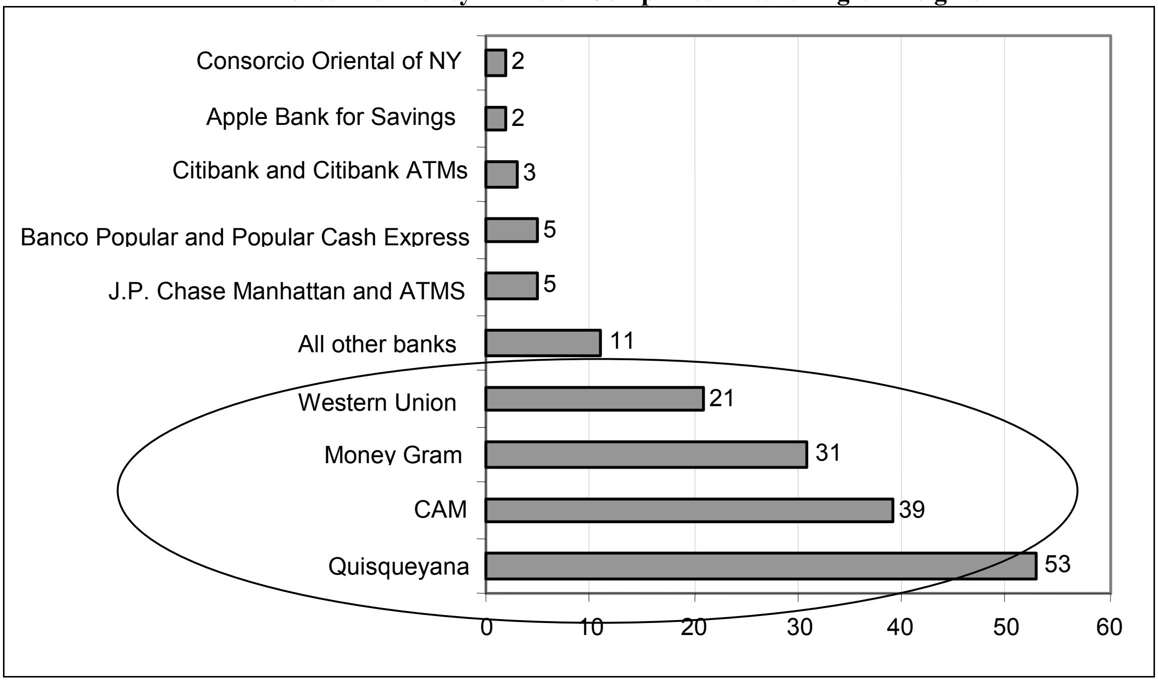
Source: Company press releases.

82. CPSS (2006) sets out four main network structures: (1) unilateral – same company at both sending and receiving side, such as MTOs or banks with branches on both the sending and receiving side; (2) negotiated – individually determined alliances with strategic partners or networks, such as Vigo's alliance with the World Council of Credit Unions and their affiliates in the IRNet; (3) franchised – generally the model used by large multinationals using agents to capture flows and distribute; and (4) open – no restrictions to anyone wishing to use the correspondent banking network (the only existing example of an open network). Because agents or strategic partners in a remittance network can exercise substantial negotiating power based on the characteristics of its network, especially the size, each of the above structures bear on the competitive landscape of the industry. On the sales and distribution side, the network's size, in particular, can generate substantial negotiating power that impacts final prices.

83. The "franchise" model has generated the most concern about the contestability of remittance markets. Large, global RSPs like Western Union, MoneyGram and DolEx, most commonly adopt this structure with diversified and extensive sales and distribution networks in a wide variety of businesses. Global RSPs and some corridor specialists gained a first mover advantage in this respect by adding remittances to existing platforms of

alternative financial services providers (check cashing, money orders, bill payment, payday loans, etc.) or by “franchising” to immigrant-owned businesses offering complementary services.[31] In immigrant neighbourhoods, the physical presence of RSPs and their agents overwhelms that of other financial service providers as graph 13 illustrates in the case of the major Dominican neighbourhood in New York. In fact, the MTOs below only represent a fraction of the total located in that neighbourhood. This is a common phenomenon in many markets.

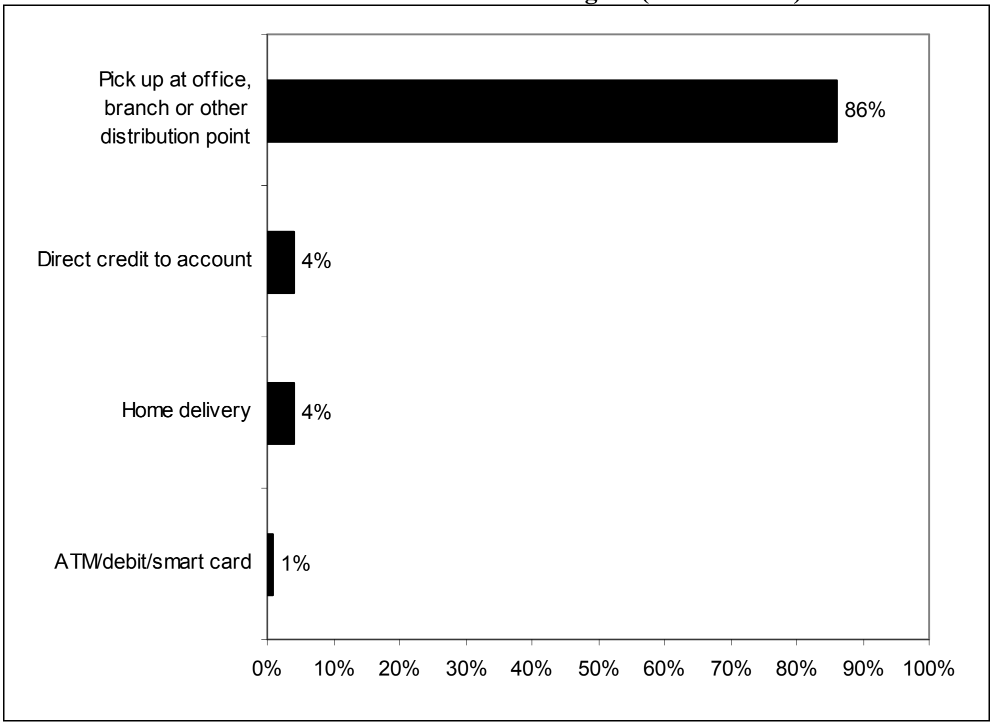
Graph 13.
Bank Branches and Money Transfer Companies in Washington Heights*



** New York City Zip codes 10031, 10032, 10033, 10039, 10040. Survey: November 2004.*

84. This same model is dominant in the Last Mile as graph 14 illustrates. About 80% of remittances are picked up in the offices of partners of an MTO. Banks and other financial institutions such as credit unions or non-bank financial institutions such as mortgage finance companies are important partners (Orozco 2006) for their branch networks, professional management, disbursement liquidity and ICT investments for their own businesses. Distributing institutions may also be retail stores, such as consumer electronics/domestics stores, pharmacies or supermarkets. Elektra in Mexico or La Curacao in Central America are examples of distributors hoping to attract business from customers with regular cash infusions from abroad.

Graph 14.
Remittances distribution in LAC region (as % of total)

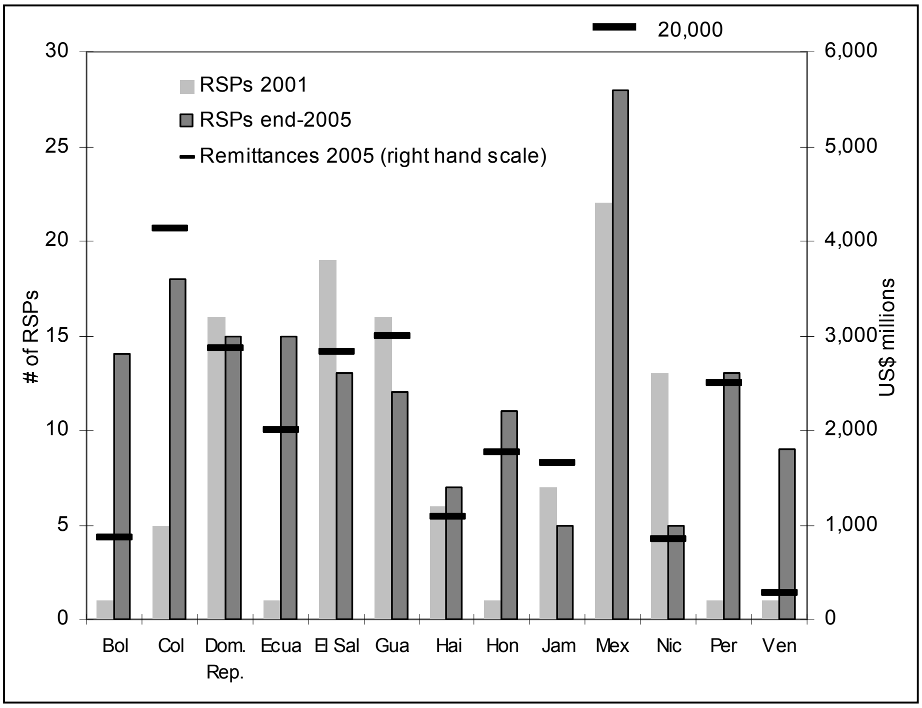


Source: Orozco 2005.

85. Early entrants have also exercised considerable market power by building dominant, sometimes exclusive, agent partnerships in remittance-receiving countries. World Bank (2005) illustrated that exclusive relationships have had a damaging effect on competition, resulting in higher prices on markets in which large distribution networks, such as postal networks, have been tied for long periods of time to one RSP. Exclusivity is increasingly rejected, except in special situations, in favour of multiple linkages with different types of acquisition and distribution partners across the three stages of the remittance transfer.[32] In certain markets, participants believe that the marketplace has reached saturation with most potential points of service already linked up to an RSP. As such, the nature of such partnerships can have an appreciable impact on the state of competition and the maturity of the market.

86. The growth of small and medium-sized specialist money transfer companies has increased the contestability of remittances markets, but their impact is concentrated in densely populated immigrant communities where customer acquisition efforts are more cost-effective.[33] These firms are unlikely to make a broader geographic impact because business costs for small and medium-sized firms are more burdensome (Andreassen 2006), especially if larger firms have already partnered with dominant distribution agents. In fact, for many later entrants to remittance markets, regardless of size, finding acquisition and distribution partners can be time-consuming and costly. Even if agents contract with multiple RSPs, those with longer relationships may benefit from better marketing or the agent's familiarity with the staff and products of its first partners. As a result, populous or high density sending or receiving locations may not fully reflect average prices and the competitive landscape of a given corridor.

Graph 15. Remittance service providers in the LAC region (by country)



Source: Orozco (2006).

87. Nonetheless, consolidation among existing market players has apparently stabilised the number of companies in most Latin American corridors (Orozco 2006 and graph 15). Mergers and acquisitions due to rising asset values as well as competitive and regulatory pressures, indicates rapid growth in the number of RSPs since 2001, but levelling off in many corridors. Merger and acquisition behaviour (see text box 4) has never been publicly evaluated for impact on competition.[34]

88. Because of the purported "stickiness" of people's choices in executing their remittances, MTO agents can exercise substantial negotiating power vis-à-vis their partner MTOs. Agents are compensated for their acquisition or distribution role by a formula that varies by their negotiating power. Some agents receive a percentage of the transaction fee; in others, effective agents capture the full commission (Suki 2004). The MTO shares the remaining transaction fee and foreign exchange spread with the distributing partner.

Box 4.
Selected investment activity in remittances

March 1999 First Data Corp. (Western Union parent company) purchases Orlandi Valuta (Mexico specialist with 2,000 points of service in five US states

March 2003 Vigo Remittance Corp. purchased by private equity firm, Great Hill Partners

November 2003 Global Payments Inc. purchases DolEx Dollar Express (DolEx) and enters retail money transfer industry

May 2005 First Data Corp. (Western Union parent company) purchases Vigo (LAC specialist with 3,700 agents and 47,000 service points)

January 2006 First Data Corp. announces spin-off of Western Union

April 2006 Mexican bank, Banorte, to acquire UniTeller Holdings, which operates in 41 states with half of its volume to Mexico

May 2006 Coinstar to acquire Travelex Money Transfer, the third largest money transfer company with 17,000 points of service in 138 countries

89. Alternatively, some MTOs set a reference foreign exchange rate to allow the agent to work within a range to offer better rates to customers, using that flexibility to maintain customer loyalty or extract additional rents. In fact, the New York City Department of Consumer Affairs drew attention to this phenomenon in 2003, advocating for more transparent pricing information and more consistent oversight after it found substantial variation among agents within and across immigrant neighbourhoods.[35] Such behaviour may be important in setting prices to end users if agent networks on the sending or receiving side have significant negotiating power. It also speaks to a possible lack of transparency in "real" prices as opposed to "headline" prices.

Box 5.
The Case of Correios in Brazil: Postal Distribution of Remittances

In 2000, Banco Postal emerged from the union of Correios, the public sector postal operator in Brazil, and Banco Bradesco – seven years after the initial feasibility studies were conducted. The strategy of using Correios to expand financial services into rural, largely unbanked areas received strong backing from the government. In Brazil, most bank branches are located in urban areas. This strategy would integrate microfinance, savings, giro, remittances, payments and other products and bring these services to low income individuals and small enterprises. With the designation of Banco Bradesco, one of Brazil's top commercial banks, as partner, the Central Bank gave its approval for regulatory adjustments that would allow Correios to become a correspondent of Bradesco.

Partially leveraging on the remittances product as well as other services, Banco Postal has opened more than 3 million accounts through 5,000 participating post offices, more than doubling the existing bank branch network. This required investments in human resources, information systems and regulatory reforms to allow Correios to operate as a banking institution.

Postal services in Latin America have suffered for decades from concerns about service, human resources, institutional capacity and outdated information systems and infrastructure. Although the process was long, Brazil's experience illustrates that postal networks may be one answer to the question of bringing cost-effective remittance services to rural populations. Ideally, such a strategy would integrate broader financial access objectives. Currently, the postal services of Spain are preparing to launch a new low cost remittance service to Latin America.

90. Financial institutions' unilateral or negotiated models of network-building have as yet made little impact on the competitive landscape. Citibank Global Transfers in the United States will distribute remittances into Banamex, their Mexican subsidiary's branches. The WOCCU scheme, IRNet, has pioneered the inclusion of credit unions in the remittances market by making alliances with Vigo Remittance Corp. and MoneyGram to originate transactions from 160 credit unions with 480 points of service in the US and over 800 points of service in eight countries in Latin America. Citibank's new partnership with Banco Solidario in Ecuador is a new example of a negotiated network. These networks are smaller but allow the principals to retain better control over business processes and the quality of the service.

91. Other network models have been modestly successful. Institutions from several migrant-sending countries have established "branches" in immigrant communities abroad. Central American institutions pioneered this practice, and others have followed. These firms have opened modest storefronts in the United States that offer mostly money transfer services while giving customers the ability to fill out paperwork to open a bi-national bank account. They are not banks, however, but rather money transfer companies.[36]

92. Although postal networks, especially postal savings institutions, have successfully distributed remittances in other regions, such as Asia, Latin American postal networks have yet to be deployed for this purpose, except in Brazil (see text box 5).

93. The foregoing discussion highlights areas that would benefit from additional investigation and analysis:

    The extent to which distribution networks in the receiving country contribute substantially to market power of individual competitors paying particular attention to the role of exclusivity arrangements with distributors;

    Comprehensive surveys of distribution networks in receiving country, categorized by type of partner (financial and non-financial), geographic distribution and concentration, existence of exclusivity arrangements, with an evaluation of the penetration of distribution partnerships relative to "potential" distribution;

    Identification of alternative networks, such as state-owned financial institutions or postal networks, that might serve as new distribution avenues to rural and remote high migration areas; and

    Determination of whether barriers prevent expansion of distribution networks in the receiving country or into "branches" abroad.

Services and Access

94. The various services and products offered within a market indicate the extent of formality and the nature of product market competition, as well as future trends. Most RSPs offer similar service – point-to-point cross-border money transfer, available instantly for the largest firms or within hours for others, both payable and disbursed in cash, with access to multiple points of service for both origination and distribution. The homogeneity of the dominant cash-to-cash service suggests contestability of markets and, possibly, substitutability of services. Money transfers to more remote areas may still face fewer options, long delivery times and higher prices or receiving fees.

95. Table 7 outlines service innovations related to payment instruments currently on offer in the market. This service differentiation relies on more intensive use of technology to ensure precision and speed in messaging and execution, as well as to connect banking networks across borders. European and Japanese financial institutions have made more progress with this, and it is common in these countries to find online transactions, ATM transfers and cellular phone transfer services, all of which are available in Spain, Portugal and Japan. These new methods have yet to take hold in the United States, which sends 80% of remittances to the LAC region.

96. Although cross-selling from remittances to other services and products is not new, recent market entrants are attempting to compete with incumbents by offering additional services, new payment instruments, technologies and linked financial services for remittance senders and receivers both. Official sector and government stakeholders have endorsed improved financial access to meet the special needs of migrants as a means of increasing competition. The following illustrate sending side examples:

Check-cashing, money order sales, bill payment, travel services and long distance phone cards have long been sold with remittances (Andreassen 2006).
In the United States, commercial banks such as Bank of America, Wells Fargo, Citibank and US Bank offer low cost or free (in the case of Bank of America) transfers from bank accounts into other bank accounts or into cash, primarily as a means of building a new bank account base. They have also diversified to offer dual ATM cards and stored value cards, as well as telephone money transfer.
In Spain, credit unions La Caixa and Caja Madrid (as well as federations like CECA) have developed financial services specifically for migrant senders and their families by developing partnerships in the origin countries.
Banks from the home country open offices abroad to facilitate opening bank accounts with binational access.
In New York, Mutualista Pichincha, the largest mortgage finance company in Ecuador, markets homes in Ecuador and Colombia, financing them in Ecuador.
Banco del Austro, the New York MTO branch of an Ecuadorian bank, offers video-conferencing and account-opening assistance in Queens, New York.

Table 7.
Remittance services offered to the LAC region

Transaction	Target client1/	Participants	Payment	Speed	Complexity
Cash-to-cash	Any (subject to normal verification)	MTOs, some credit unions on a limited basis 2/	Cash, money order, stored value debit card	Instant or within hours	Low
Credit card-to-cash	Clients with access to credit (subject to normal verification)	MTOs, including online MTOs 2/	Credit card	Instant or within hours	Low/ Medium
Cash-to-account	Banked recipients, also to build unbanked clients	Some MTOs, 3/ some credit unions on a limited basis 2/	Cash, receiving account credit	Normally next day; can be as long as 2-3 days	Low/ Medium
Account-to-cash	Banked senders, also to build unbanked clients	Banks and credit unions in US and Europe, esp. Spain; online MTO providers	Sending account debit; debit card sending side; cash, stored value card or ATM for recipient	Instant or within hours for MTOs; Hours, next day or longer for banks/credit unions	Medium/ High
Account-to-account	Banked on both sides, also to build unbanked clients	Banks and credit unions in US and Europe, esp. Spain	Sending account debit; debit card sending side; ATM card for recipient	Next day or longer for banks/credit unions; can be as long as 2-3 days	Medium/ High

1/ *All clients sending money transfers are subject to verification via electronic filters that check names against various lists to ensure no criminal behaviour.*
2/ *Credit unions in the United States may offer remittances to non-members on a limited basis with the sole aim of familiarizing remittance senders with the credit union in order to build new membership.*
3/ *MTOs will often offer this service without making an electronic transfer to a bank account but rather by receiving the cash and depositing it physically into the designated account.*

97. In receiving countries, although very few new services and products have had the appeal of cash-to-cash remittances in sufficient volume to impact the remittance market significantly, there are similar innovations:
Retail firms offer the opportunity to use remittances immediately to purchase goods, such as medicines or sundries in a pharmacy;
Home electronics stores are selling domestic durable goods on rent-to-own terms;[37]
In Mexico, Construmex, a division of Cemex, allows customers to buy construction materials and services; and Supermercados Wong in Peru allows customers abroad to buy items online for loved ones in the country to pick up or receive by delivery.

98. The main obstacles to further competition on the basis of product differentiation result from weak financial infrastructure, lack of financial access in sending and receiving countries, lack of investment in financial literacy and education, migrants' low confidence in institutions and poor information and communications technology infrastructure. ATM and point-of-sale (POS) equipment are often not available in areas where migrants normally work, shop and live, or they may not work consistently enough to stimulate trust (Suki 2004). They also require a consistently well-functioning communications and information technology infrastructure. Financial institutions find it overly costly to maintain liquidity in remote ATMs. Lack of financial access is a problem for banking schemes that require accounts. These require further investment in financial literacy. In no country is there a concerted and comprehensive effort to educate about the use of financial services. Initiatives tend to be more piecemeal, but the government of Mexico has promoted several policy responses already mentioned. Even when governments have created good resources, they may be on line and, therefore, not reaching their target audience.

99. Further areas of inquiry may merit additional attention in the future:
Differences in services used and survey recipients about preferences, needs and shortcomings of existing services;
Identification of growing service trends that may have an important impact on demand;
Evaluation of the potential for card-based options based on ICT infrastructure, existence of ATM and POS network in urban and rural areas.

Public sector role in remittance market competition

100. With the recognition of the importance of migration and remittances in development, LAC governments are becoming more engaged in the topic of remittances and have begun to involve a wider range of government agencies in policy-making. The government of Mexico has been the most activist with activities ranging from direct provision of financial services through Bansefi, the national savings bank, to collection and dissemination of institutional and pricing information to active consumer protection and service offerings to Mexicans abroad through consulates. This section highlights government interventions with specific relevance for competition. It also addresses lower priority themes and their significance for competition authorities.

101. A few examples highlight ongoing interventions of other governments in LAC:
In Colombia, the 2006 Census included questions on migration and remittances for the first time after the government worked with the International Organization for Migration to carry out extensive surveys of remittance receivers in 2004.
In Ecuador, the Central Bank is exploring the concept of providing a low cost payments infrastructure that would allow microfinance institutions to disburse remittances more efficiently and in a more cost effective manner.
The Guatemalan authorities have been working with the US Treasury Department to refine their legal and regulatory framework for remittances with respect to anti-money laundering provisions and countering terrorist finance. Guatemala has also introduced a sophisticated identification card to be used by Guatemalans abroad.
The Centro de Estudios Monetarios de Latinoamerica (CEMLA) is working with Latin American Central Banks to define standards for improving data quality.

102. Among others, public sector initiatives help to increase competition in remittance markets by improving information about senders and receivers; by opening up domestic payments infrastructure to allow small institutions to participate in a cost-effective manner; and by facilitating financial access and, therefore, improved options for senders and receivers.

Improve data quality and provide pricing and institutional information

103. Lack of data on remittances presents a serious challenge to both private sector actors and policymakers. Definitions of remittances vary among Central Banks and other institutions, and many institutions charged with collecting that information do not survey MTOs, which are the majority of the institutions that conduct those transactions (De Luna Martinez 2005). In addition, information about informal flows may not be collected at all.

104. For competition authorities in particular, historical high frequency pricing data and market share information is necessary to evaluate aspects of price and non-price competition, merger and acquisition behaviour, and the implications of exclusivity, among other themes.

105. Governments may also wish to understand the macroeconomic impact of remittances on the economy or to design and implement projects related to migration and remittances. Such interventions also rely on data, but the types of data needed may be different. For example, extension of payment systems infrastructure should be based on estimates of flows and potential usage. Private sector institutions likewise need data to evaluate entry strategy. As

a result, collecting and providing data and market information can be key part of the strategy to ensure competitive conditions in the remittances market.

Expansion of access to financial infrastructure

106. Improvements in electronic payments system infrastructure in LAC in recent years has dramatically improved the accessibility of electronic payments instruments in both the retail and corporate sectors. These changes have made possible the introduction of card-based remittance services while developing retail systems that allow cards to be used both for ATM and point of sale functionality, both of which have important implications for the development of remittance-based services and financial products.

107. Cross-border payment and settlement of remittances crosses both domestic and international payment systems. As a result, access to payment systems infrastructure plays a role in the contestability of the market. CPSS (2006) highlights disparities in access that may complicate the messaging function or domestic settlement of remittances. These include weak financial infrastructure, limited geographic accessibility in certain regions (especially for non-cash payment instruments and in receiving countries) and payments systems with little interoperability. Settlement systems with low automation and substantial manual procedures add both cost and time while increasing the probability of mistakes. Increased automation, openness of systems and standardisation of messaging protocols, as well as new investments in domestic payments infrastructure, are recommended to address domestic shortfalls.

108. International settlement creates some similar and other distinct challenges, especially in the realm of interoperability. The cross-border nature of these flows suggests a need for coordination between sending and receiving countries at a minimum and, at the most interventionist, a potential role in provision of infrastructure or creation of direct linkages between sending and receiving countries among governments with large remittance flows.

109. Accessibility to payment and settlement systems has been raised by a number of actors as a stumbling block to competition. Among these, MTOs in the United States and other countries have pointed out that the lack of direct access to the payments system forces these RSPs to bank with institutions that have responded with great caution (by closing MTO bank accounts or raising the cost of maintaining the accounts) to supervisory guidance with respect to maintaining MTOs as customers. Two other financial service providers – credit unions and microfinance institutions – likewise have been restricted from direct access to payments systems in many countries.[38]

110. Private messaging and payments systems are also developing their own responses to these challenges. SWIFT[39] has recently launched a long-term initiative to develop its strategy toward remittances. Credit card companies like Visa International are also leveraging their existing payments infrastructure in domestic and international spheres for remittances. Public systems may also be put in place by Central Banks to bridge domestic and international systems. Another primary example is that of Visa International, which is working with its member banks to develop card products and service support options to promote the use of cards for remittances.

111. Another dimension of expanding the financial infrastructure might include consideration of postal networks. In contrast with Asia and Africa, postal networks in LAC have not been

mobilized as financial service providers. Brazil is the major exception to this. These networks have not been developed as financial service providers due to historical concerns about reliability, weak image, lack of institutional capacity and the state of infrastructure. Even so, Brazil's experience of ECT (Empresa de Correios e Telegrafos), or Correios, partnering with Banco Bradesco (mentioned below) provides an example of how postal networks might be leveraged to provide financial services, among which remittances. World Bank (2005) cautions, however, that prices for remittances are higher in countries where postal networks have exclusive arrangements with major global RSPs such as Western Union or MoneyGram because these partnerships absorbed such a large percentage of the available distribution points, especially in rural areas.

112. Examples from Latin American countries illuminate the role of the public sector (domestic and international) in furthering the goal of increasing access to payments and settlement infrastructure:

The U.S. Federal Reserve Bank established an Automated Clearing House (ACH) connection with the Central Bank of Mexico called Directo a Mexico illustrates a direct intervention to promote the sending of very low cost remittances through American banks for distribution to Mexican banks. The Directo a Mexico program allows banks in the United States to use a Federal Reserve Bank platform to send very low cost remittances into the banking system in Mexico. Thus far, there has been little uptake by banks in the United States due to shortcomings in the time-to-delivery relative to the market, marketing and communication to member banks, concerns about documentation and legal status, and uncertainty about supervisory guidance with respect to the AML/CFT implications of money transfer services.

The government of Brazil has actively supported initiatives to leverage public infrastructure to improve accessibility of remittance services. For instance, the state-owned Caixa Economica Federal has alliances where Brazilians live abroad to allow them to send money via a Visa card or a bank transfer to a beneficiary with or without an account, as well as to manage savings accounts and payments. Brazil's National Monetary Council also supported the joint venture of Banco Bradesco and Correios, the national postal network to expand points of financial access in underserved areas, especially rural areas. With its membership in the Eurogiro network, the postal network of Brazil added 18,000 points of service for distribution of remittances, approximately doubling distribution points and substantially expanding access outside of major urban areas.

Mexico's national savings bank, Bansefi, has constructed a domestic network called La Red de la Gente, in which credit unions in Mexico who have met guidelines for institutional development and prudential regulation may become a member. This network is intended to connect a large network of capture points in the US in banks, MTOs and Mexican consulates to a range of financial services, including a future plan to provide accounts in Mexico senders and receivers. Bansefi has created a unified platform to give increased negotiating power to small institutions in Mexico and bring easy access to multiple MTOs to more remote receiving areas of Mexico.

The Ecuadorian Central Bank is currently working to construct a secondary payments infrastructure for microfinance institutions and other financial entities in rural areas with limited access to payment systems in order to give them access to Central Bank payments infrastructure.

WOCCU, with the support of USAID, has helped to build a payments infrastructure called IRNet for the benefit confederations of credit unions in Mexico, Ecuador, Guatemala and several other countries. This arose as a solution to the challenge posed by regulatory authorities in countries in which credit unions are not granted access to payment systems despite being regulated and supervised institutions. This infrastructure is being used to transmit remittances through partnership via WOCCU with Vigo and MoneyGram.

113. These interventions vary in the directness of the intervention but illustrate that public sector authorities on both sides have worked to facilitate access to payment systems as a response to the question of competition and access to acquisition and distribution networks.

Ensure a fair and non-discriminatory legal and regulatory framework

114. Regulatory authorities exercise different degrees of control over the remittances industry from minimal regulation to highly interventionist behaviour. Disproportionate burdens should not be placed on any institutions as a result of uneven application of laws and regulations (CPSS 2006). Particular institutions or types of institutions should not enjoy advantages with respect to the remittances' industry. Poor regulation can have negative effects on the formalisation of remittance flows, maintaining demand for less transparent informal providers and undercutting other important goals.

115. Regulation of remittances can define the following elements of remittance transactions, among others:
Access to market participants;
Licensing or registration regime;
Reporting and customer identification requirements;
Risk management procedures and governance guidelines;
Consumer protection and grievance procedures; and
Institutions responsible for oversight. (Lee 2005)

116. Although the legal and regulatory framework for remittances is increasingly better understood as distinct from other types of financial sector regulation, authorities must take care to ensure that the legal and regulatory framework do not become a barrier to entry. Several institutions, including the World Bank, the Inter American Development Bank, UK's DFID and the Committee on Payment and Settlement Systems, urge a legal framework that is "sound, predictable, non-discriminatory and proportionate" (CPSS 2006). These needs must be balanced against the recommendations of the Financial Action Task Force (FATF) on money transfer to ensure that remittance systems are not being used for money-laundering or terrorist financing.[40] These require that participating countries must license or register RSPs and put in place procedures to prevent transfer systems from being used for money laundering (see table 8).

Table. 8.
Registration compared with licensing

	Registration	Licensing
Supervisory requirements:		
Background checks	To identify providers, no consequences attached	Full fit-and-proper test
Internal procedures	Basic AML/CFT preventive measures	Detailed business plan, including AML/CFT procedures

Monitoring	Basic reporting requirements and risk-based inspections'	Basic reporting requirements and onsite inspections
Sanctions	Ranging from informal warnings to fines	Ranging from warnings to withdrawal of license
AML/CFT requirements:		
Customer identification	Required	Required
Record keeping	Required	Required
Suspicious transactions reporting	Required	Required

Source: Lee 2005.

117. While regulation can address diverse issues as outlined above, the regulatory framework should not discriminate among institutions offering remittances such that regulations become a barrier to entry in themselves (CPSS 2006). Their assessment of risk should reflect only the money transfer business of the institutions involved, rather than any other business lines, as well as the remittance flow of the institution. In other words, credit unions offering remittances should face the same remittance regulations as a bank offering remittances, but the risk assessment should take into account the smaller flows and diminished likelihood of money-laundering or terrorist-financing behaviour.

118. The cross-border nature of remittances again creates special challenges. The involvement of sending and receiving countries calls for coordination and dialogue among legal jurisdictions. Foreign exchange regulations may also affect the cost and complexity of remittance transactions.

119. Other industry regulation – both financial and commercial - may impact the competitive landscape for remittances. The most important of these is in the areas of foreign exchange, establishment of banks abroad, microfinance and telecommunications.

120. Although sending and receiving side regulations will often address similar themes, they will usually come from different legal traditions and institutional landscapes. In the United States, for instance, regulations have increased costs to MTOs and other RSPs. Redundant and unclear supervisory responsibilities, as well as overlapping mandates at the state and federal level, have diminished the access of MTOs to the banking system. On the receiving side, another example relates to credit unions. In many countries, such as the Dominican Republic, credit unions as yet have no formal ability to participate in the remittances market although they are deposit-taking institutions.

121. Regulatory frameworks can be refined in order to improve the efficiency of remittance markets in some of the following ways:
Identification of companies involved in money transfer for a national registry, which would facilitate analysis of market shares, service provision and pricing;
Examination of existing and proposed regulations to determine whether any represent barriers to entry or measures that may drive formal remittances toward informality, such as:
Limits on the participation of certain kinds of institutions in remittances
Different requirements across types of institutions
Imposition of prudential requirements relative to systemic risk of remittance institutions
The magnitude of licensing or registration fees

Demands for identification not easily accessible by migrants
Active dialogue between government and private sector stakeholders to ensure that proposed regulation is oriented toward a competitive market
Regulatory assessment with the aim of ensuring non-discriminatory and proportionate prescriptions relative to risk posed by RSPs.

Other areas of public sector involvement in remittances

122. Public sector agencies may also influence remittance markets beyond data, infrastructure and remittance market regulation. In the most common areas of further engagement, governments may be regulating foreign currency, working to ensure that consumers receive adequate protection, improving financial literacy and access and sponsoring dialogue among remittance stakeholders.

123. Foreign exchange regulations may place limits on firms ability to transact in foreign currency. Most importantly, monetary policy authorities place controls on what institutions may deal in foreign currency. Governments may also influence the choice of disbursement currency or control foreign exchange operations.

124. Consumer protection has become a key issue for government as well. Ensuring that disputes and conflicts can be resolved may have a beneficial impact on competition by generating confidence in a wider range of instruments and channels. Mexico has two agencies that fulfil such a role. Profeco (Procuraduria Federal del Consumidor www.profeco.gob.mx) promotes awareness of consumer rights and carries out price comparisons of remittances. Condusef (Comision Nacional para la Proteccion y Defensa de los Usuarios de Servicios Financieros www.condusef.gob.mx) focuses on the financial services industry.

125. Improving financial literacy and access may also have a positive impact on competition. Increasing the proportion of remittances sent through formal channels should improve opportunities for new entrants, such as banks, credit unions and microfinance institutions, to link financial services and the financial needs of migrants.

126. Governments can also help to guide the public and internal dialogue on remittances, addressing the interests of all parties. This would make alternative options to incumbent services more visible to the general public. It may also orient governments toward more consistent application of principles in remittances markets. It is worth making particular note of the incipient dialogues and collaborations between governments and civil society organisations, such as migrants' associations. These associations can assist with inquiries into remittance markets, dissemination of market information and improving financial literacy in their communities.

127. Some governments have attempted to make remittances another lever for fiscal policy by taxing it. Although there is no consensus as to the impact of taxation on remittance flows, a tax would be an additional cost and unlikely to improve the competitiveness of the market as it is.

Areas for further study

128. The study of remittances and the competition landscape of this industry is still in its infancy. The issues posed by these developing markets for cross-border financial services suggest several avenues for future inquiry.

129. The following areas should be promising directions for additional activity within receiving countries:

    Improved estimation of informal transfers and their impact on competition in specific corridors;

    Detailed analysis of prices with increased attention related to sending and receiving locations and a range of money transfer and related products and services;

    Evaluation of foreign exchange spreads and their role in price competition;

    Quantification of market shares of major distributors of remittances;

    Spatial market analysis of urban/rural differentials in access and cost;

    Survey and assessment of receiving country distribution networks with particular attention to the role of exclusivity arrangements, barriers to widening distribution networks and obstacles to domestic institutions expanding abroad;

    Survey of services used, preferences, needs and shortcomings of existing services, as well as the potential for the entry of alternatives;

    Determination of information-related avenues for improving the competitive landscape;

    Assessment of payments systems and their impact on access, pricing and efficiency;

    Examination of existing and proposed regulations to determine whether any represent barriers to entry or measures that may drive formal remittances toward informality

    Regulatory assessment with the aim of ensuring non-discriminatory and proportionate prescriptions relative to risk posed by RSPs.

130. An expansion of the area of inquiry may require additional data that is not easily accessible at the moment, but the results of such investigations would surely add much to the rapidly evolving dialogue regarding efforts to make remittances cheaper, more efficient and more effective in delivering benefits to consumers in both sending and receiving countries.

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Notes

1 Remittances are generally thought to be underestimated by at least half because of weak data collection procedures in sending and receiving countries, inaccurate estimates of informal flows and incomplete coverage of RSPs by statistical agencies. The cited estimates for remittance flows to Latin America in 2005 can be found on the Inter American Development Bank's (IDB) Multilateral Investment Fund (MIF) website for remittances (www.iadb.org/mif/). The MIF estimates are derived from surveys conducted in most Latin American countries since approximately 2000 by Sergio Bendixen and Associates. In some cases, these data differ from those published by Central Banks in the region.

2 The states where the largest Latino populations in the United States reside are California, New York, Texas, Florida, Illinois, and New Jersey. The mid-Atlantic region (Washington, D.C. to Connecticut) and New England all have large or growing Latino populations, as do many western states such as Arizona and Colorado. The Pew Hispanic Center has focused its attention on changing patterns of Latino population growth different parts of the United States and in particular the emergence of new settlement areas (see http://pewhispanic.org/topics/index.php?TopicID=1).

3 See Bendixen's surveys for various estimates of the percentage of Latin American adults abroad who remit. Bendixen's 2005 survey of remittance senders by US state found a range of 60%-70% in the number of adults of Latin American origin who remit.

4 Indeed as all official and scholarly analyses report, remittances can also be domestic in nature, but due to the particular challenges of ensuring payments across borders, this report and many others focus on international remittances.

5 Remittances may also be made in-kind (food, domestic appliances, construction materials, etc.), but at this point, these flows have not been well quantified nor do they likely form a very substantial proportion of the total of the flows to Latin America. In other regions or within regions, when travel between host and home countries is easier,

6 CPSS (2006), World Bank (2006), Hernandez-Coss (2004), Orozco a, b and c (2005) and Sander (2003) all provide exceptional detail on trends, determinants, economic impacts, institutional intermediaries, financial access issues, public policy, regulatory frameworks and multilateral and bilateral cooperation.

7 The Dominican Republic – New York corridor is a good example. Most operators offer a service that the majority of senders request – cash-to-cash with home delivery – and customer satisfaction is high across the board (Bendixen 2004).

8 The pioneers in this area have been Wells Fargo with its *Intercuenta Express* service and Bank of America with its *SafeSend* service in the United States. In Spain, the other main destination for LAC migrants, major credit unions, such as La Caixa and Caja Madrid, have offered below market remittances.

9 In response to mounting concern over money laundering, the Financial Action Task Force on Money Laundering (FATF) was established by the G-7 Summit that was held in Paris in 1989. During 1991 and 1992, the FATF expanded its membership from the original 16 to 28 members. In 2001, the development of standards in the fight against terrorist financing was added to the mission of the FATF. The work of the FATF focuses on three principal areas: (1) Setting standards for national anti-money laundering and counter terrorist financing programmes; (2) evaluating the degree to which countries have implemented measures that meet those standards; and (3) identifying and studying money laundering and terrorist financing methods and trends. The FATF Standards are comprised of the Forty Recommendations on Money Laundering and the Nine Special Recommendations on Terrorist Financing. (www.fatf-gafi-org)

10 There are reportedly new preliminary service partnerships being set up between Spain and postal services in several South American countries.

11 A class-action lawsuit seeking $100 million was filed in December 1999 against Western Union, MoneyGram and Orlandi Valuta. The companies were charged with deceiving customers, mostly immigrants who sent money to Mexico, about the costs of sending money. Under the proposed settlement, persons who could prove that they sent money to Mexico via Western Union, MoneyGram and Orlandi Valuta would get discount coupons worth $4 on future transactions. In addition, the money transfer companies would give $5 million to Latino community organizations. According to the suit, a person sending the typical $300 remittance was charged $30. In addition, the money transfer companies usually convert dollars to pesos at a rate about 10 percent below the interbank rate, which was 9.4 pesos per dollar in December 1999. The suit required the money transfer companies to fully disclose transfer costs and to contribute funds to foundations for support of Mexican immigrants in the United States.

12 The CPSS report (2006) likewise regularly refers to the need to ensure that markets are contestable.

13 One example would be the US-Mexico corridor between New York and the states of Puebla and Guerrero, the originating region of the majority of the Mexicans in New York. Likewise, New York or Barcelona and Ecuador are corridors of substantial volume. A more specific corridor would include Los Angeles-Zacatecas

state in Mexico, northern Virginia/Washington, DC - El Salvador, Miami – Colombia, etc. For a thorough enumeration of the various US-Mexico corridors, see Hernandez Coss (2004).

14 Many of these firms may also offer non-financial services such as international package delivery and tourism services.

15 In the case of Mexico, the state-owned savings bank, Bansefi, has an initiative called *La Red de la Gente,* which unites its own branches and credit unions into a large distribution network. In Guatemala, the formerly state-owned Banrural channels a large percentage of remittances. In Brazil, the Caixa Economica Federal delivers both money transfer and pro-poor financial services. In Ecuador, the state-owned development bank distributes remittances as well.

16 In Latin America, this is being led by the Centro de Estudios Latinoamericanos (CEMLA) which is advising central banks in the region to improve their data collection procedures and standards.

17 This report defines informal transfer as those transfers carried and delivered physically by family, friends or unregulated money transfer services (such as *hawala* or *hundi* services in the Middle East and Asia or the use of *cambistas* in Latin America). This includes delivery by post or package service. We recognize that there is some controversy as to the use for formal vs. informal or regulated vs. unregulated as explained in CPSS (2006). However, this report solely uses the term "informal" for the sake of distinguishing characteristics of competition. We acknowledge that regulated institutions may likewise face competitive barriers to which unregulated institutions who *are* legally permitted to transact money transfers may not be subject.

18 All agents in the United States that wish to provide remittance services to Cuba now need to be licensed by the Office of Foreign Assets Control (OFAC) in order to become a remittance-forwarding service provider. As of this report's writing, OFAC was responsible for regulating nearly 200 licensed remittance-forwarding service providers. A handful of major MTOs are included among these, as well as many travel service companies. See treas.gov/offices/enforcement/ofac/programs/cuba/cuba_tsp.pdf.

19 Mexico's consumer protection agency (Profeco) and financial sector consumer rights' (Condusef) have published prices. Remesas.org in Spain has published online updates of prices for various institutions. None of these has managed to disseminate its information to local migrant communities. Profeco (Procuraduría Federal del Consumidor) and Condusef (Comisión Nacional para la Protección y Defensa de los Usuarios de Servicios Financieros) have undertaken responsibility for collecting and disseminating data on various RSPs providing money transfer services to Mexico from the United States.

20 MTOs may partner with institutions or franchise their services to other institutions that offer other services. Remittances may also be domestic rather than international. The LAC corridor specialists do not offer domestic remittances, but the global MTOs like Western Union, MoneyGram and DolEx do offer service within the sending countries they serve.

21 Remittance senders from Japan also tend to send more money per transaction (approximately $600) (Bendixen 2005).

22 Postal money transfer schemes between Spain and several Andean countries are being launched currently.

23 In general, banks will only offer money transfer services to clients with bank accounts in order to meet required monitoring and reporting demands.

24 WOCCU itself has played an important role in advocacy to governments highlighting the importance of granting access to credit unions to payment systems to facilitate their ability to extend financial services to low income clientele. They have worked to address obstacles to credit union engagement in the Dominican Republic, Brazil and the United States.

25 This is particularly important because remittance clients often complain of arriving to pick up their money only to be told that there is no more. Such problems, if consistent, can erode customer loyalty.

26 The average sent from the US is approximately $300 and from Japan, $600. (Bendixen 2005)

27 Fees for receipt of remittances in Latin American markets are very rarely charged except when the transfer is executed through a correspondent banking network, is delivered at home or is disbursed in a very rural location with little technology infrastructure.

28 In the United States, regulations vary widely from state to state. RSPs must meet an individual state's requirements for licensing and bonding in each state in which they plan to do business. Hernandez-Coss (2004) addresses this in detail.

29 In the United States, MTO bank account closures have become one of the most daunting challenges to RSPs. Banks indicate that the Department of the Treasury gives guidance that discourages taking RSPs as clients, primarily as a result of the interpretation of Know Your Customer rules as requiring banks to effectively know their customers' customers to minimize risk of money laundering and terrorist finance in their customers' business lines. MTOs whose accounts have been closed point to unfair competition from banks wishing to enter the remittances business and prejudice against immigrant-owned businesses. In the Dominican Republic, this situation was seen as sufficiently acute as to merit the current President highlighting the plight of Dominican MTOs to US authorities and in public speeches.

30 Management of both commercial and retail financial institutions indicate concerns about the damage and reputation risk that might be caused by any incidence – or even the suggestion - of their institution being used as a vehicle for money laundering or terrorist finance. Smaller institutions mention concerns about not having the capacity to exercise sufficient oversight of banking clients' transactions.

31 An important distinction is that MTOs very rarely originate business in a regulated depository institution. On a few occasions, community banks in the US have leased space within specific branches to MTOs to bring new clients in the door and ensure that these clients have access to reliable and convenient money transfer services. Two interesting examples are located in the midwestern United States: both US Bank and Marquette Bank (Chicago) have alliances with MoneyGram.

32 Alliances that are still characterized by exclusivity include Western Union's partnership with Banamex in Mexico and Banco Vimenca in the Dominican Republic, MoneyGram's partnership with Bancafe in Guatemala, the relationship between WOCCU and disbursing credit unions in the *IRNet* system and credit unions involved in Bansefi's *La Red de la Gente.* In the last two cases, however, the sponsoring institutions, WOCCU and Bansefi, have gained access to multiple RSPs on the sending side, diminishing the impact of the exclusivity of the contract. Exclusive arrangements may also exist between small RSPs with small distributors when the RSP provides disbursement capital from which to pay remittances. These situations do not pose a threat to competitiveness.

33 See paragraphs 73 through 76 for more detail.

34 US anti-trust officials in the Deparment of Justice have evaluated the most important mergers. Given that these acquisitions were executed, one can assume that at least government officials felt that the impact on prices would not be prohibitive.

35 The New York City Department of Consumer Affairs sent a research field team to visit nearly 90 money transfer agent locations in three New York City communities - Washington Heights, Sunset Park, and Jackson Heights. The varied costs of sending $500 to the Dominican Republic were documented with prices ranging from $5 - $38 and transmission time ranging from "a couple of hours" to "not more than 24 hours." Further, the report shows that many local agents often develop prices "on the spot." (http://www.nyc.gov/html/dca/html/news/pr_remittances.shtml)

36 Some examples include: Bancomercio, BancoSal and Banagricola of El Salvador; Banco del Austro of Ecuador; Banco Cuscatlan from Central America; and Banco del Occidente and Banco GyT of Guatemala.

37 It is worth noting that rent-to-own electronics and domestics retailers often charge very high finance fees to purchase these goods, which is often not in the interest of the financial health of the buyer.

38 In Brazil, the Dominican Republic and the United States, credit unions have faced difficulty in offering remittances products and other services to unbanked clients for various reasons, primarily relating to their non- or quasi-regulated status. In the United States, these institutions must illustrate that such services are being offered to non-members for a limited time solely for the purpose of building membership.

39 SWIFT is a financial industry-owned cooperative supplying secure, standardized messaging services and interface software to 7,800 financial institutions in more than 200 countries. SWIFT's worldwide community includes banks, broker/dealers and investment managers, as well as their market infrastructures in payments, securities, treasury and trade.

40 FATF recommendations related to remittances require that money service businesses be either licensed or registered and subject to AML/CFT measures. Financial institutions are also expected to perform due diligence related to identification of customers and verification of identification, to correspondent banking relationships that involve cross-border transactional flow, and to technologies or relationships that allow increased anonymity of transactions or non-face-to-face relationships. When engaging in these relationships, the FATF recommendations indicate that correspondent banks should assess the AML/TF controls of the counterparty. See www.fatf-gati.org for more information.