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## CRAFTING A MONEY TRANSFERS STRATEGY: GUIDANCE FOR PRO-POOR FINANCIAL SERVICE PROVIDERS



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CGAP, the Consultative Group to Assist the Poor, is a consortium of 29 development agencies that support microfinance. More information is available on the CGAP web site: [www.cgap.org](http://www.cgap.org).

### Introduction

As more data becomes available on cross-border remittances, these financial flows are attracting greater attention from the private sector, governments, and development agencies alike.<sup>1</sup> Although not all money transfers are captured in official statistics, formal remittances nevertheless constitute the second largest source of external funding for developing countries, ahead of both capital market flows and official development assistance. Remittances are qualitatively different from other sources of development finance in that they are both relatively stable and counter-cyclical in nature, since migrants tend to remit more during periods of economic downturn in their home countries.<sup>2</sup> Because remittances represent private money sent person-to-person, they benefit the poor directly and as poor people determine they need it—on demand.

From the viewpoint of financial service providers (FSPs), transferring remittances can be a lucrative business. Western Union's dominance in this market has earned the company hefty profit margins, estimated to be 150 percent higher than those of the average US commercial bank.<sup>3</sup> Attracted by this profit potential, smaller providers have begun to explore market segments not yet penetrated by the global giants, often by targeting particular diaspora communities and/or by improving domestic transfer services in developing countries.

Financial service providers that cater to the poor have been drawn to the money transfer market because it offers them the opportunity to fulfill their financial goals as well as their social objectives.<sup>4</sup> As a fee-based product, money transfers can generate revenues and bolster an FSP's bottom line. From a social perspective, money transfers allow FSPs to deliver an additional service demanded by poor customers, at a cost potentially lower than that of mainstream providers.<sup>5</sup>

Although much has been written about the benefits that money transfers could bring to pro-poor FSPs and their clients, relatively little information is available on *how* they might enter the money transfer market. This paper explores the operational and strategic considerations involved in launching a money transfer product. The first section begins with an overview of global money transfers, including the overall size and structure of the industry and the differences between its different segments—



cross-border and domestic, formal and informal, retail and wholesale. The second section describes the main types of transmission channels used to transfer funds, the types of providers traditionally associated with these channels, partnerships between these providers, and new customer interfaces being used to make money transfers cheaper and more convenient for clients. Finally, the third section explores how a pro-poor FSP might begin to build a money transfers strategy, considering factors such as client preferences, regulation, competition, institutional capacity, financial analysis, and marketing.

### The Money Transfer Market

The money transfer industry is highly complex, comprising a vast array of formal and informal players that use rapidly changing technologies and institutional infrastructure to effect transactions for diverse clients. The market can be segmented in various ways, for example, by type of customer (governments, businesses, individuals), origination and end points (cross-border or domestic), and type of transmission channel (formal or informal).

This section describes why person-to-person remittances may be the most relevant type of transfer for FSPs that cater to poor customers and explains what FSPs can learn from informal money transfer providers. It then examines the market opportunity presented by the best-documented type of person-to-person transfer: cross-border remittances. Lastly, it examines domestic and

regional money transfers, which may offer FSPs an equal or greater opportunity than North-South transfers, although they tend to be much less well known.

### Types of Money Transfers

In addition to person-to-person remittances, FSPs can process many other types of money transfers, including business-to-business transactions (e.g., invoice payments), business-to-person flows (e.g., salary payments), and government-to-person transfers (e.g., pension and welfare payments). Consumer-initiated payments are sometimes known as “retail” payments, while those initiated by institutions are known as “wholesale” payments. The Boston Consulting Group (BCG) estimates that cross-border retail and wholesale payments will grow considerably in both value and volume between 2001 and 2011 (see table 1).<sup>6</sup>

Although they make up a tiny fraction of worldwide payments, person-to-person money transfers may be the most important type for the majority of poor people in developing countries. Business-to-business and business-to-person transfers are currently beyond the capacity of most informal-sector enterprises, which employ many of the world’s poor. Additionally, few governments of developing countries have implemented significant programs involving government-to-person transfers to the poor.<sup>7</sup> Therefore, for this paper, the term “money transfers” refers to person-to-person transfers.

**Table 1 Cross-Border Payments by Type**

	2001*		2011	
	Value (US\$ billions)	Volume (millions)	Value (US\$ billions)	Volume (millions)
Retail	300	1,977	748	5,176
Wholesale	329,517	536	602,914	980
<b>Total</b>	<b>329,817</b>	<b>2,513</b>	<b>603,662</b>	<b>6,156</b>

\* The most recent year for which comprehensive data was available

Source: Boston Consulting Group (BCG), *Preparing for the Endgame*. Figures for 2011 are projections. BCG defines payments as non-cash transactions, i.e., payments not involving a face-to-face exchange of cash.

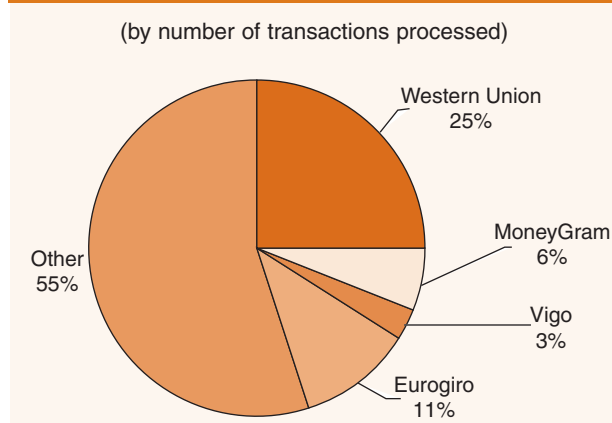
## Size and Structure of the Formal Cross-Border Money Transfer Market

The volume of formal remittance transfers within and between specific countries is only beginning to be documented.<sup>8</sup> Based on IMF data, the World Bank estimated the global volume of formal cross-border remittance transfers to be US \$88.1 billion in 2002 and US \$93 billion in 2003.<sup>9</sup> These figures reflect startling market growth since 1970, when the total volume of international transfers was estimated at US \$2 billion.<sup>10</sup> According to the World Bank, Latin America and the Caribbean received the most international transfers in 2003, with 30 percent of global flows, followed by South Asia (18 percent), the Middle East and North Africa (13 percent), Europe and Central Asia (10 percent), and sub-Saharan Africa (4 percent).<sup>11</sup> India and Mexico rank among the top recipient countries of international transfers, while the United States and Saudi Arabia currently are the principal sending countries.<sup>12</sup>

The sizeable market for person-to-person transfers is dominated by large, specialized money transfer companies (MTCs), including Western Union, MoneyGram, and Vigo. The rest of the formal money transfer market is fragmented among commercial banks, post offices, foreign exchange bureaus, credit unions, and niche money-transfer companies, with different players dominating specific markets.<sup>13</sup> For example, while 70 percent of Latin American immigrants in the United States use MTCs to transfer money home, banks process a relatively larger share of formal money transfers to Turkey, India, and the Philippines.<sup>14</sup> On the other hand, 90 percent of remittances from Russia to Ukraine and from the United Arab Emirates to India are transferred in cash.<sup>15</sup>

Total industry revenues in 2003 can be estimated at approximately US \$18 billion, with an estimated 320 million transactions processed.<sup>16</sup> Given that many market actors report the value of transfers, not the number of transactions, it is dif-

**Figure 1 Estimated Market Share of International Person-to-Person Transfer Providers, 2003**



Sources: Ratha, "Workers' Remittances," First Data, SEC Form 10-K; MoneyGram, SEC Form 10; Bezard, *Global Money Transfers*; Great Hill Partners, "Great Hill Partners Form GMT Group;" private estimates of Gera Voorrips and Hans Boon, ING Postbank; authors' estimates.

ficult to estimate the total number of formal transfers made in a given year. Western Union, the largest money-transfer company in the market, reported that it processed approximately 81 million transfers in 2003,<sup>17</sup> which Bezard estimates to represent roughly 25 percent of the total market.<sup>18</sup> Market shares of the other major international transfer providers, shown in figure 1, are estimated, using the average figure of US \$300 per international transfer cited by MoneyGram.<sup>19</sup> These percentages are, however, indicative at best, since average transfer amounts vary widely by region, as table 2 illustrates.

Much clearer are the significant profits earned by the leading players in the industry. Western Union, for example, reported US \$3.3 billion in revenues and \$1.23 billion in operating profits for 2003.<sup>20</sup> Bezard considers this figure to represent 18.5 percent of total formal market revenues.<sup>21</sup> MoneyGram is a distant second player in the market, reporting only US \$737 million in revenues and \$112 million in operating profits in 2003.<sup>22</sup> Although other money transfer companies are not believed to earn the same margins as Western Union and MoneyGram, the market is clearly profitable.

**Table 2 Average Annual Value of Transfers to Selected Countries by Immigrants in the USA**

Country	Amount (US\$)
India	1,104
Pakistan	790
Bangladesh	562
Philippines	397
Mexico	385
Egypt	307
El Salvador	280
Dominican Republic	203

Source: Orozco, "Worker Remittances."

Fees and foreign exchange commissions contribute the bulk of income earned by these companies. Boston Consulting Group data for retail payments in 2001 indicate that fees make up about two-thirds of total revenue, while foreign exchange income makes up about one-third. (See appendix 1 for detailed figures.)<sup>23</sup> Float income is largely insignificant.<sup>24</sup>

Another interesting trend emerging from the BCG data is that total retail-payments revenue is anticipated to increase as per-payment revenue decreases. This suggests that capturing significant volumes of money transfers will become increasingly important to the profitability of the business. Fortunately for money transfer providers, this growth in total demand is expected to be significant. Bezard expects that formal and informal retail transfers together will grow to US \$177 billion by 2006, and that recent anti-money laundering efforts will reduce the share of worldwide transfers channeled by informal providers from 50 percent in 1996 to 34 percent in 2006. At present, formal money-transfer companies are concentrating their expansion efforts in those countries likely to be most affected by the switch to formal providers, such as India and China.<sup>25</sup>

### Regional and Domestic Money Transfers

Although research at present focuses on transfers from developed to developing countries, migra-

tion often occurs within the same continent: close to half of all reported migrants live in developing countries.<sup>26</sup> Refugee movements are even more localized, with the majority of refugees moving to a neighboring country.<sup>27</sup> BCG estimates that the total value of intra-regional transfers in Asia, Europe, and the Americas in 2000 was US \$168 billion, corresponding to 1.85 trillion payments (see table 3).<sup>28</sup> Money transfers between developing countries represent a significant market opportunity, although appropriate transfer infrastructure may have to be refined or developed, depending on the country.

Transfers within individual developing countries represent a similar promising market (and similar infrastructure constraints). Evidence indicates that poorer and more rural migrants tend to move to destinations closer to home—often urban centers within the same country. They also earn and remit less money than do wealthier international migrants.<sup>29</sup> The amounts of domestic transactions thus tend to be smaller than international transfers, but these transfers are more numerous and flow to many more households.<sup>30</sup> In China alone, domestic migrants sent US \$45 billion via formal transfer providers in 2003.<sup>31</sup> Table 4 provides estimates of total domestic retail and wholesale payments in selected countries for 2000, the most recent year for which comprehensive data was available. (See appendix 1 for total and per-payment revenues generated by domestic retail payments.) As with cross-border payments, forecasts indicate that future profitability of domestic

**Table 3 Intra-regional Transfers by Region, 2001**

	Value (US\$ trillions)	Volume (millions)	Revenues (US\$ billions)
Americas	17	296	2.9
Europe	121	1,249	11.2
Asia Pacific	30	308	3.6

Source: Boston Consulting Group, *Preparing for the Endgame*. Figures combine retail and wholesale transfers. No data was available for Africa or the Middle East.

**Table 4 Domestic Payments in Selected Countries, 2001**

	Value (US\$ trillions)	Volume (millions)
USA	741.2	82,594
EU 15 *	371.9	51,542
Canada	20.1	6,159
Brazil	12.7	21,693
Mexico	6.9	7,476
China	7.7	6,731
Poland	4.0	598
India	4.0	4,242
Czech Republic	2	910
Indonesia	2	9,698
Thailand	1.6	1,150
Malaysia	1.2	944
Philippines	1.1	3,466
Russia	2.9	622
Hungary	0.6	218
<b>Total (World)</b>	<b>1446.1</b>	<b>220,457</b>

\* The EU-15 includes countries that were members of the European Union prior to 2004: Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, the Netherlands, Portugal, Spain, Sweden, and the United Kingdom.

Source: Boston Consulting Group, *Preparing for the Endgame*.

transfers will depend on capturing an increased volume of transfers.

Safe, affordable money-transfer mechanisms are critical for processing both domestic and international transfers. Domestic transfer services are the final link—the “last mile”—of the international transfer process, so domestic markets must operate efficiently for international transfers to reach intended recipients. However, money transfer networks within developing countries are often more limited than international networks due to undeveloped infrastructure, lack of FSPs that provide transfer services, or both. This reality represents an opportunity for FSPs that serve poor customers, especially in remote or rural areas where transfer options may be especially scarce. Box 1 describes how an FSP in Ghana filled such a gap in the domestic transfer market.

### Informal Channels

While formal money transfers are recorded in the accounts of a business entity that reports to

### Box 1 Apex Link: Going the Last Mile

Apex Bank is a central treasury for the rural banks of Ghana, a network of more than 100 banks representing over 400 points of service, some in villages as small as 500 people. Market studies in the rural areas served by these banks revealed that clients were having difficulty accessing transfers from urban areas in Ghana. Crime made it especially difficult for traders, who carried large sums of cash on their person for business. At the same time, the rural banks were looking for new revenue sources and ways to attract more customers.

In response to this dual need, Apex Bank developed the “Apex Link” domestic money-transfer system. The service uses proprietary software to manage money transfers between rural banks using coded messages sent by phone, fax, or express mail. Turnaround time is between 15 minutes and 24 hours, and transfers can be made from an account or in cash, making the service accessible to customers and non-customers alike.

If recipients lack the government-issued identification card or passport normally required for identification purposes, they may come to the bank accompanied by a “locally known person” to act as a witness to the transfer. Transfer fees are paid by the senders on a sliding scale, depending on the amount transferred (usually 0.5 percent of the transfer amount for customers, and 0.75 percent for non-customers). These fees are shared between Apex Bank and the sending and receiving rural banks.

Apex Link can also be used as the “last mile” in an international funds transfer because Apex Bank has a partnership with a local commercial bank that is licensed to handle foreign exchange. The local bank deposits funds from abroad into Apex Bank’s central account in local currency. Apex Link then transfers the funds to a rural bank for final payment to the receiving client.

From the launch in June 2003 to May 2004, the system has made 24,000 transfers totaling over US \$27 million. Management reports that the system is now running well, despite initial operational challenges that included staff training and marketing. Expanding awareness of the product throughout Ghana will be key to the project’s success, as Apex Link was designed not only to generate revenue, but also to attract more clients to the rural banks.

Source: Interview with Emmanuel Yaw Sarpong, Apex Link manager, Apex Bank, June 21, 2004.



government authorities, and are thus included in national economic statistics, informal transfers are not. Experts estimate the total value of monetary transfers made through informal channels (e.g., transfers conducted through family, friends, or undocumented transfer channels) is somewhere between 40 and 100 percent of the volume of global formal transfers.<sup>32</sup> Recent studies estimate, for example, that over half of the money transfers from France to Mali and Sénégal are made via informal channels, as are 85 percent of total transfers made to Sudan. Informal channels are also estimated to process six times the volume of formal transfers sent to Nepal and three-quarters of all transfers made to India and China.<sup>33</sup> Bezaud estimates that informal money-transfer systems in Asia and the Middle East may manage two-and-a-half times the value of transfers processed by formal systems in these regions.<sup>34</sup>

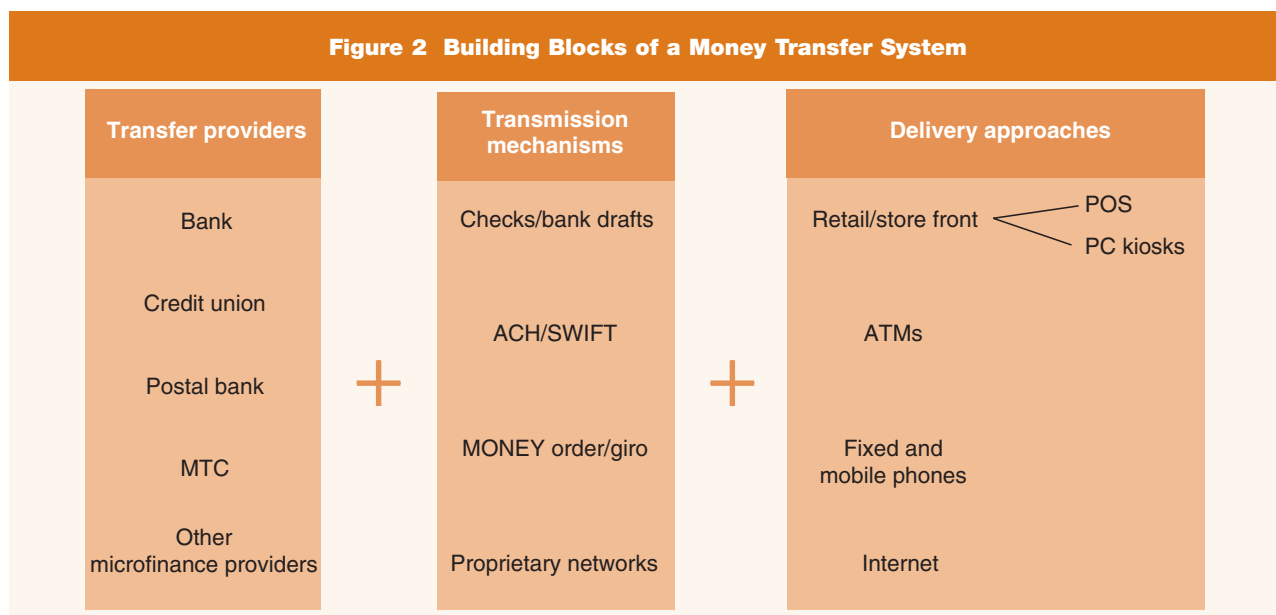
Such evidence indicates that informal systems are competing successfully with even the largest players in the formal money transfers market. In large part, their popularity is due to certain client-friendly features. Regardless of the actual mechanism employed, informal transfer systems are usually fast, discreet, and involve a minimum of paperwork. They are also generally less expensive

than formal transfer mechanisms which are subject to regulation and taxation, and they are often available in areas where no formal sector providers exist.

From a client perspective, informal systems may be more familiar and therefore more trusted than formal money transfer services, despite the risk of possible theft. For clients who lack identity or residence documentation, these systems may also be easier to use. Such client-friendly features could serve as a model for FSPs, which may want to incorporate certain aspects of informal systems into their own money transfer offerings. (See appendix 2 for a more detailed description of various informal money-transfer systems that operate around the world.)

### The Building Blocks of a Money Transfer System

Money transfer systems can be thought of as having three main elements: (i) the institutions that provide the transfer; (ii) the mechanism that carries a transfer from point A to point B; and (iii) the customer interface through which cash is collected from senders and/or disbursed to recipients. As illustrated in figure 2, possible combinations of



these three elements are virtually limitless, and as the money transfer industry evolves, new combinations are constantly being invented. However, these combinations may require partnerships between providers, as certain types of FSPs are often restricted by law from using certain types of transfer mechanisms. This section briefly addresses the following topics:

- Common transfer mechanisms
- Limitations that prevent FSPs from using these mechanisms
- Types of institutional partnerships forged by FSPs to access an expanded range of transfer mechanisms
- The growing number of customer interfaces that are being used to make money transfers more accessible to poor clients

### Transmission Mechanisms

The main types of money transfer mechanisms in use today fall into two broad categories. Paper-based systems include instruments such as bank checks and money orders. Increasingly, these instruments are being replaced by electronic systems, such as real-time gross settlement systems,<sup>35</sup> networks operated by money transfer companies (MTCs), and internal bank branch networks. As illustrated in table 5, these mechanisms can be further divided into different categories, depending

on whether clients are required to have an account at a financial institution in order to either send or receive a money transfer. (This requirement is an important consideration for poor clients, many of whom do not have bank accounts.)

There are five major instruments used to transfer money in the formal market, and different types of FSPs have access to different instruments.

### Checks and Bank Drafts

Paper checks and bank drafts were among the original forms of documented money transfers and are still a major form of person-to-person money transfers in certain industrialized countries. Issuing checks and bank drafts is generally limited by law to regulated financial institutions, such as banks and credit unions. Where these institutions are readily accessible by the majority of the population, the system is easy to use. However, the mechanism depends on postal reliability, which is often lacking in developing countries, so clients risk losing checks and drafts in the mail. Even in the best cases, the recipient must wait for a check to arrive and then for the funds to clear the banking system. The physical processing of paper-based instruments also incurs costs for a bank, especially in countries where labor is expensive. For these reasons, paper checks are increasingly being replaced by electronic payments.

**Table 5 Main Money Transfer Mechanisms by Type**

		Transmission Mechanism	
		Paper-based	Electronic
Sending-Client Requirement	Cash	Money orders	Money-transfer proprietary networks
	Bank account	Checks, bank drafts	Giro, ACH, SWIFT

## Money Orders

Money orders have also traditionally been paper-based instruments, but unlike checks, they can be issued by and redeemed at a variety of FSPs. Major issuers of money orders include postal financial institutions and MTCs, such as Western Union and MoneyGram. Money orders do not require a bank account; a recipient receives cash upon presenting the money order to an authorized paying agent (a post office, MTC agent, etc.). This process also reduces the time a recipient must wait to access the transferred funds, compared to checks or bank drafts. However, given the need for money orders to be physically delivered to a recipient, they are subject to some of the same risks of delay and theft.

Postal money orders are now estimated to provide 1 percent of formal international money transfers. In contrast, postal networks play a very important role in domestic transfer markets in many countries. The National Post in China, for example, manages 90 percent of cash-based transfers within the country. In Bulgaria, the post office processes three times more cash payments than do all commercial banks together. While the volume of these transactions is large, their value is estimated as only 2 percent of the value of cash payments processed by banks—a trend visible in the majority of countries of Eastern Europe and Central Asia.<sup>36</sup>

## Electronic Transfers<sup>37</sup>

At the domestic level, the most common types of electronic funds-transfer systems are the automated clearinghouse (ACH) and the real-time gross settlement system.<sup>38</sup> Both mechanisms allow member financial institutions to exchange payment instructions and settle obligations electronically. ACHs can accept payment instructions from a financial institution or directly from clients, who can link into these systems using their bank-issued debit or credit cards. These networks are often owned and operated by central banks, although

private players such as Visa also operate ACH systems in certain countries.

At the international level, the most commonly used system for facilitating electronic fund transfers is operated by the Society for Worldwide Interbank Financial Telecommunication (SWIFT), an industry-owned cooperative that provides real-time payment messaging services to member institutions.<sup>39</sup> SWIFT is often the cheapest option for high-value transactions between financial institutions, but can be expensive for small transfers. For this reason, most payments processed by SWIFT are not individual person-to-person transfers, but larger payments between businesses or between businesses and consumers, such as university tuition.<sup>40</sup>

Most transfers referred to as “wires” are routed over SWIFT or a national ACH. Transfers over such electronic networks are quite reliable, but non-bank FSPs may not have access. Although some credit unions have access to such systems through a national federation, most non-bank FSPs are restricted by law from becoming part of a domestic payment system.

The technical capacity of FSPs can represent another hurdle to accessing payment networks. The cost, information technology, and staff capacity required to connect with SWIFT systems, for example, can be significant obstacles to becoming a member of the industry cooperative.<sup>41</sup> Although FSPs can often link to SWIFT through a member bank, the resulting transaction entails a certain loss of competitive privacy, as the intermediary bank necessarily obtains information about the FSP’s money transfer business. Transfers over these networks can also be slow, and lost or delayed funds can be difficult to track.<sup>42</sup>

## Giro

“Giro” is the term used for the electronic cross-border payments offered by post offices in more than 40 countries. This system enables holders of a postal bank account to send money—



**Table 6 Advantages and Disadvantages of Money Transfer Mechanisms for Customers and Financial Service Providers**

	<b>Customers</b>	<b>Financial Service Providers (FSPs)</b>	<b>Restrictions to Access by FSPs</b>
<b>Checks</b>	Slow; subject to loss/theft; must be physically delivered; require bank accounts to send (not necessarily to receive)	Incur relatively high processing costs	Depends on local regulation; access often limited to regulated financial institutions only
<b>Money Orders</b>	Slow; subject to loss/theft; must be physically delivered; do not require bank accounts to send or receive	Incur relatively high processing costs	Postal money orders for postal FSPs only; others can be issued/paid at variety of FSPs
<b>Electronic Funds Transfer (EFT)</b>	Faster than paper-based instruments; requires bank accounts to send and receive; cheaper than MTC transfers	Lower labor costs than checks, but requires link to network and infrastructure; fees lower than for MTC transfers	Can be accessed by many FSPs through financial institutions with which they conduct business
<b>Giro</b>	Requires a postal account for sending, but generally cheaper and more accessible than bank-based EFTs	Lower labor costs than checks, but requires link to network and infrastructure	Only postal FSPs can originate transactions; both postal and other FSPs can receive
<b>MTCs</b>	Real-time delivery possible; no bank accounts required; numerous access points; higher price	Infrastructure requirements and costs can vary depending on agency relationship; generally more lucrative than other transfer mechanisms	Depends on local regulation; agents sometimes restricted to banks, with fewer restrictions on sub-agents

domestically or overseas—to another postal account, a bank account, or to a post office for cash payment. It generally takes two to four days to receive a giro transfer. The international service is often used by small entrepreneurs for import and export payments.

Although sending a giro requires a postal bank account, these banks tend to have more widespread locations than commercial banks. Postal giros also tend to be cheaper than bank transfers for small amounts. Barriers to access for poor clients, therefore, tend to be lower than for checks or commercial bank transfers. To cite a regional example, postal networks in North Africa provide account-based giro services that are highly popular with students and low- and middle-income groups who find it difficult to open checking accounts at commercial banks.<sup>43</sup>

### Money Transfer Proprietary Networks

This type of payment system is restricted to agents of the organization or association that owns the network. However, many types of institutions can become agents, including banks, non-bank financial institutions, post offices, and retail businesses of all stripes.

MTC services tend to be extremely customer-friendly, requiring neither the sender nor the receiver to hold an account or complete extensive paperwork. Such services are also known for their speed: many MTCs offer a “real-time” service that allows a recipient to collect transferred funds almost instantaneously. They also have a reputation for reliability, which the dominant industry players take care to reinforce through extensive advertising.

In return for their simplicity, speed, and reliability—and in part, to finance large marketing

budgets—MTCs are typically the most expensive of the transfer mechanisms (when prices are expressed as a percentage of the funds transferred) discussed in this section. Although seemingly disadvantageous for the customer, the revenues earned by leading players indicate that this type of service has tapped enormous customer demand. The significant per-payment fees charged by MTCs also represent an attractive source of income for FSPs that join these networks.

### **FSP Partnerships and Other Institutional Arrangements**

FSPs that serve the poor have forged a number of creative partnerships with other institutions to provide money transfer services. Alliances with banks, credit unions, postal networks, international money-transfer companies, and retail outlets allow them to leverage their strengths (proximity to clients and established quality services) and overcome their weaknesses (limited transfer expertise, restrictions on foreign exchange dealings, access to a payment system). This section describes FSP alliances with MTCs, international correspondent banks, and non-bank institutions.

Agency relationships and business partnerships require trust and transparency. FSPs must select partners carefully, especially as more operators enter the money transfer market. When receiving institutions deliver a transfer payment to a client, they assume credit risk, as they often have not yet received the actual funds from their international partner and need to know that the funds will soon arrive. Sending FSPs rely on receiving partners in other countries to make sure that transfers are delivered to recipients. Information on both sending and receiving FSPs can be difficult to obtain. Receiving institutions may not be able to easily compare different money-transfer partners. Likewise, send-side FSPs often don't know which partners are reliable and offer good client service in a specific country. Thorough due diligence on potential partners, including reference checks, legal status, and financial statements, is crucial.

### **Money Transfer Company Partnerships**

A growing number of FSPs have established alliances with MTCs, such as Western Union, MoneyGram, and Vigo. Part of the attraction is due to simplicity: MTCs often offer a turn-key solution for providing money transfer services to agents and sub-agents, which basically is a complete package of software and training. Agents may also benefit from existing marketing programs and an established agent network, which can generate transfer volume. MTC relationships may even become a competitive necessity for pro-poor FSPs—as they did for XAC Bank in Mongolia, when it needed to offer the same convenient transfer services its competitors had in order to retain clients.

The most important factor in an MTC's choice of agent is often regulatory. In some countries, access to MTC networks is limited by law to banks and occasionally credit unions and foreign exchange bureaus. A second crucial factor is the extent of an agent's branch network, which can be its most valuable bargaining chip when negotiating for MTC agent or sub-agent status. MTCs are often attracted by the proximity of microfinance institutions to poor clients, whom they consider one of their most important target markets.

Additional criteria that figure in agent selection are operating hours, financial soundness, and sufficient liquidity to advance customer payments prior to reimbursement. Because verifying these criteria for large numbers of agents can be cumbersome, MTCs usually sign a few primary agents in each country, often banks. Depending on local regulations, the banks may then sign sub-agent relationships with a variety of different FSPs. In this case, the MTC's relationship is really with the primary agent, while the primary agent is responsible for due diligence on its sub-agents.

The paying agent's portion of the money transfer fee is then divided between the agent and sub-agent. In order to avoid fee sharing, smaller financial institutions could potentially form a consortium to become the primary agent of an MTC, assuming that consortium members had a

minimum level of systems integration and/or a common IT platform. This approach has been used by a number of FSP federations, including the Jamaica Cooperative Credit Union League (JCCUL), which has partnered with a local money transfer company to bundle four foreign MTCs into a money transfer service under its own proprietary brand.<sup>44</sup> In Mexico, La Red de la Gente links several hundred savings and credit cooperatives along these lines in order to form a distribution network for remittances and other financial services.<sup>45</sup> IRnet, a money transfer service created by the World Council of Credit Unions, bundles transactions from multiple credit unions in order to obtain discounted service from established MTCs.

MTC partnerships also entail a number of risks that need to be managed. For example, the larger the MTC, the more likely that it will attempt to impose exclusive relationships on its agents. Yet even large MTCs cannot always generate adequate transaction volumes for institutions in receiving countries, particularly if they have not sufficiently penetrated the relevant immigrant communities in sending countries. For example, one of the first

foreign MTCs that JCCUL partnered with was hardly used by Jamaicans in the United States—even though it is widely used by Latin American immigrants. Because it had refused to become an exclusive agent, JCCUL was able to bolster disappointing transfer volumes by adding other MTC partners.<sup>46</sup> Box 2 describes other risks entailed by MTC relationships and how pro-poor FSPs have dealt with them.

### Partnerships with Financial Institutions

Financial institutions with bank licenses can provide money transfer services via an electronic payment network by setting up correspondence relationships with banks in other countries or regions. The relationships between FONKOZE in Haiti and City National Bank of New Jersey in the United States, and between Spanish savings banks and Banco Solidario in Ecuador, are two such examples. In both cases, money transfers are bundled by the sending institution and transmitted to an account at the recipient institution that unbundles the payments for distribution to receiving clients. NGOs like the one described in box 3 may also set up partnerships with banks to provide their clients with money transfers.

## Box 2 Managing Risk in MTC Relationships

Partnering with an MTC can offer FSPs a complete package of services and infrastructure necessary to process money transfers. However, entering into an agency agreement with an MTC does not fit the needs of all pro-poor FSPs. One MFI with rural branches in the Philippines found that the domestic long-distance charges for dialing into the servers of its MTC partner rendered the entire relationship unprofitable, even though initial training and software had been free of charge. In addition to dial-up charges, transfers incur other costs, such as cashier services, management attention, and office space. FSPs must therefore be particularly careful in assessing the full cost of an agent or sub-agent arrangement.

One way to manage the risk of launching money transfer services is to phase the introduction of such services. Such phasing can be done geographically, for example, by initially rolling out MTC services only in certain branches. This approach was taken by XAC Bank in Mongolia, which for the first few months limited its international MTC service to the head office. As volume builds, branches must be able to process transfer clients quickly and smoothly, a lesson XAC Bank had already learned from its domestic transfer products. Phasing the introduction of international MTC transfers in its branches allowed the bank to learn how to minimize operational costs before opening up the network to larger volumes of transfers.

Phasing the intensity of the relationship with an MTC is another way to manage risk. XAC Bank chose to become a sub-agent, that is, its MTC transfers are routed through another commercial bank that acts as the MTC's primary agent in Mongolia. Although this arrangement requires XAC to share over half of the revenue from each transfer with the primary agent, it avoids paying the cash security deposit that full agency status requires. If transfer volumes generate sufficient revenue to justify becoming a full agent, XAC has the option to upgrade its relationship with the MTC.

*Sources:* Interviews with Jim Anderson and G. Tuul, XAC Bank, June 7, 2004; and Chairman, Philippine MFI (name withheld), June 23, 2004.

### Box 3 Partnering with a Commercial Bank to Provide Domestic Remittances

In India, the NGO Adhikar is piloting a domestic money transfer service for the large number of migrants who travel from the eastern state of Orissa to work in the western state of Gujarat. Adhikar's comparative advantage in money transfer services is knowledge of customer needs and preferences, as well as the ability to service clients in remote locations. When designing its transfer system, Adhikar decided to leave the actual transmission of funds to Corporation Bank, which has branches in both Orissa and Gujarat and the infrastructure to make timely, secure transfers.

Although bank transfers take place regularly between Orissa and Gujarat, most migrants do not have bank accounts and find it costly to visit a bank branch. Adhikar centralizes the collection and dissemination of these small transfers and routes them through one account at the bank. This process spreads transaction costs over a larger number of transfers, bringing down the per-transaction fee. Adhikar is now looking to leverage the system by involving NGOs that serve other districts in Orissa as distribution agents, lowering per-transaction fees even further while enabling the NGOs to earn a new source of revenue to support their work.

#### Other Partnerships

FSPs also partner with other non-bank institutions, such as credit unions. In Nicaragua, for example, FAMA (a microfinance institution) partnered with a network of rural credit unions to distribute transfers. The rural credit unions can receive overseas transfers, but have no presence in urban areas. FAMA, on the other hand, lacks access to a payments system, but offers the credit unions a complementary urban distribution network.<sup>47</sup>

Even if they enjoy access to one type of transfer mechanism, FSPs may establish links with other providers so that they can offer customers a more comprehensive range of transfer options. Post offices, for example, often offer postal money orders as well as MTC services, enabling them to process both domestic and international transfers. Credit unions may subscribe to both an ACH network and an MTC service, giving transfer customers a choice in terms of speed, reliability, and cost.

### Box 4 Mobile Phones Bring Money Transfers Closer

In the Philippines, a novel combination of traditional MTCs, non-financial retail establishments, and a wireless communications company are using text messages to make money transfers, including cross-border remittances and business payments, such as salaries and commissions. The transmission mechanism is the mobile phone network of SMART Communications, whose subscribers can activate a virtual wallet service called Smart Money.\* Smart Money can function as a purely virtual wallet or be linked customers' bank accounts and a MasterCard-enabled debit card. In both cases, the service is controlled via the customer's mobile phone.

To make an international transfer, a sender gives cash to a SMART-affiliated MTC in his/her own country. The MTC uses its mobile phone to instruct SMART to transfer funds from the MTC's virtual wallet to the recipient's. A text message to the recipient's mobile phone advises of the successful transfer.

Depending on whether recipients use Smart Money with a debit card or as a virtual wallet, they can withdraw transferred funds from ATMs run by Smart partner banks or collect cash at a network of paying agents. This network currently includes fast-food restaurants, gas stations, pawnshops, major shopping malls, and SMART's own encashment centers.

While these agents provide wide coverage in urban areas, in rural areas coverage is sparser, presenting a potential opportunity for microfinance providers to become paying agents in underserved regions. Ongoing negotiations between SMART and financial institutions for the poor have shown the paramount importance of the number of points of service that a paying agent brings to the relationship.

A money transfer sent through SMART system incurs three separate fees charged by (i) the international agent that initiates a transfer; (ii) SMART (for transmitting the message), and (iii) domestic paying agents that turn a transfer into cash. Despite the number of actors, their combined fees are often lower than those charged by either traditional banks or MTCs.

\* Virtual wallets are accounts or stores of monetary value held in electronic form on behalf of the customer, often by companies that facilitate payments but may not offer other financial services

Sources: Conde, "Phoning Home Pesos"; interview with Ramon Isberto, group head, Public Affairs, SMART Communications, January 16, 2005; interview with John Owens, manager, MABS/DAI, September 27, 2004.

## Customer Interfaces

Money transfer operators have traditionally expected customers to come to them, typically delivering transfers to customers in cash at a bank branch, post office, or MTC agent location, such as a retail outlet. More recently, the spread of new technologies in developing countries is enabling clients to send and receive transfers in a wider variety of forms and locations.<sup>48</sup> Solutions such as these can eliminate service constraints related to branch locations and operating hours, while potentially also lowering the cost of service delivery, especially in remote locations. For example, in South Africa, Cameroon, and the Philippines, systems combining mobile phones and point-of-sale (POS) terminals<sup>49</sup> at retail outlets are being developed to allow clients to move and access transfer funds (see box 4). Box 5 describes how an Indian bank uses computer kiosks to deliver such services outside their branch network.

Debit and stored-value cards, in combination with POS devices, can transmit transfers in secure electronic form, enabling clients to access transfers in multiple locations. Magnetic-strip cards, typically used as debit or credit cards, retrieve a user's account information from an online network. "Smart" cards have an embedded computer chip that stores account data on the card itself. While magnetic-strip cards require POS terminals to connect to a financial institution's computer server to process every transaction, smart cards can process payments without connecting as often. This often makes smart cards more suitable for environments where telecommunications infrastructure is expensive or absent.

Many money transfer systems based on card technologies are currently in use or being developed. For example, one organization in Tanzania is installing POS terminals in savings and credit cooperatives (SACCOs), which are present even in

### Box 5 ICICI Bank: Money Transfers and Rural Outreach

ICICI Bank, a private Indian commercial bank that evolved out of a national development bank, offers a wide range of financial services, including money transfers sent to India by non-resident Indians. In 2004, the bank's "Money2India" service had over 670 agent locations in India and recently extended its outreach to remote village centers via computer kiosks.

The computer kiosk system work as follows: a sender remits a money transfer to the recipient's ICICI account, either through an ICICI branch office or a Money2India agent. As soon as the transaction has taken place, the Money2India agent informs the kiosk operator, who in turn informs the recipient. The recipient can then either collect the remittance at ICICI or the kiosk, which is equipped with a low-cost ATM. ICICI estimates that kiosks can be profitably placed in villages as small as 2,000 residents. This option is very attractive for rural recipients because it eliminates transaction costs involved in traveling to a larger town to visit a bank branch.

Kiosks used by ICICI bank offer a combination of telephone, financial, educational, and other services. Kiosk operators are independent business people, remunerated through commissions paid by service providers and user fees paid by customers. They pay for set-up costs themselves, for which they typically obtain a partial loan from ICICI Bank. Since ICICI Bank does not incur any fixed costs, the system has proven a cost-effective way for the bank to extend its outreach to rural areas. In mid-2004, approximately 150 kiosk operators offered ICICI services and the bank hoped to increase that number to over 2,000 in approximately 12 months. From an operator's perspective, the business model is only viable if multiple services are routed through a single kiosk. However, experience indicates that the kiosks can become profitable even without the money transfer service, which can easily be added at a later date.

ICICI Bank was able to offer its Money2India service due to a confluence of circumstances: (1) the inventors of the kiosk system were seeking appropriate business applications for it, (2) the technology suited the needs of ICICI, and (3) other non-financial service providers, such as companies that offer educational and health information/diagnostic services, also opted to use the kiosks, creating multi-service businesses that ensured operator profits. These circumstances, and therefore the transmission system for Money2India, may be somewhat difficult to replicate in other countries. However, the example of computer kiosks with low-cost ATMs may represent a cost-effective way for FSPs to expand the outreach of money transfers, as well as other services.

Source: Interview with Bindu Ananth, social initiatives manager, ICICI Bank, June 15, 2004.



remote areas of the country. Travelers are thus able to load their debit cards with cash at a bank in the capital, and then withdraw the cash at their hometown SACCO to avoid the risk of traveling with large sums of money. Although the service appears promising, the experiment has encountered a significant challenge in getting SACCO members to buy the debit cards.<sup>50</sup> This experience underlines the importance of educating customers about the benefits and use of new technologies.

In North America, many banks have taken advantage of debit card technology to design accounts specifically for transfers to Latin America. Such accounts often come with two (or more) debit cards: one for the sender to deposit cash into the account at an automatic teller machine (ATM), and one for the receiver abroad to withdraw the cash at a compatible ATM. A variation on this scheme is the VisaGiro product, which enables the sender to transfer funds to a reloadable prepaid card delivered to the receiver, who can then withdraw cash at ATMs or a Visa merchant.<sup>51</sup> New models like these illustrate one reason why Bezdard forecasts that the growth of card-based payments will become the single biggest threat to MTC dominance of the money transfer business.<sup>52</sup> A recent study of the remittances in Latin America found that debit card withdrawals were the least expensive of any transfer method in the market.<sup>53</sup>

However, the relatively low fees normally charged for card-based transactions also mean that these types of transactions are less lucrative for FSPs than transfers through other mechanisms, such as SWIFT or an MTC. In some markets, customers have also been slower than expected to embrace new technology. Another obstacle to the spread of debit card-based transfers is the standardization of ATM and POS networks, which must be harmonized nationally and globally to allow such transfers to function smoothly.

Another emerging customer interface takes advantage of the growing availability of the Internet. Many MTCs have established service

options that allow senders to initiate a transfer through the Internet and use their credit or debit cards to fund the transfer. Receivers then pick up cash at an agent location. Transfer providers specializing in web-based transfers have also come into existence. Using what are sometimes called “online or virtual wallets,” companies such as PayPal allow senders to load funds from a bank account or credit card into a PayPal account, then transfer the funds to a receiver’s PayPal account. The receiver can then withdraw cash at an ATM.

A third model combines elements of both the cash-to-cash and online wallet systems. Companies such as Xoom, for example, allow senders to initiate transfers on a web site, and partner with financial institutions in destination countries so that receivers can access cash without either a bank account or Internet access.

### **Determinants of a Money Transfers Strategy**

FSPs face a problem that seems deceptively simple: how to move funds from a sender to a recipient and make a profit. Yet the choice of partners, transmission mechanisms, and customer interfaces involves a complex set of strategic considerations. These include market factors, the regulatory environment, and the institution’s own internal capacity. Market considerations are particularly important for pro-poor FSPs that enter the money transfer business, since they must typically compete with established—and often specialized—money transfer companies. FSPs need to find a market niche and craft their money transfers strategy accordingly.

To identify an appropriate market niche, FSPs must assess the potential value of offering money transfer services by conducting a thorough market study. This study should analyze questions, such as to what extent is the market governed by regulation; how fierce is the competition; whether client needs are being addressed by current money

transfer operators; or whether there is a better way to meet those needs. This section explores how FSPs can analyze client preferences, competition, institutional issues, and market and environmental factors to craft a robust money transfers strategy.

## **Client Needs and Preferences**

### **Who Are the Clients?**

FSPs should study both sending and receiving clients, as the characteristics of these clients have consequences for product design and marketing. Financial institutions should identify, for example, the age, socioeconomic background, and interpersonal relationships of senders and recipients. Are migrant young men remitting to their parents, wives, or children? Are older women remitting to sustain their children? Are younger women sending to their parents or siblings? Understanding client profiles strongly influences an institution's ability to cross-sell existing products to both senders and receivers. Such linked products include savings accounts, loans, mortgages, credit cards, and insurance. Client literacy, educational levels, and occupational data are also crucial to the design of appropriate products, systems, and marketing strategies.

In addition to demographic information, poorer FSPs should study whether target clients currently have access to financial services: are potential transfer clients already customers of the institution, another FSP, or are they unbanked? Are they senders or receivers? Using this information, an FSP can identify product features that will attract target customers. For example, if a market study reveals that many people in the area receive money transfers but do not have accounts, the FSP may want to introduce a service that does not require an account, while offering clients incentives to open one.

### **Where Are the Clients?**

Potential market entrants must map the geographic patterns of the transfer flows of interest to them. Where do these flows originate and where

are they delivered? If sending clients work or live in concentrated areas, or participate in hometown or community associations, targeted marketing and clustered points of service will be more feasible. If sending clients are dispersed, marketing will be more challenging, and the number of transactions per branch office may be lower, reducing economies of scale. If receiving clients are dispersed, the FSP must tackle the challenges of infrastructure, client outreach, cash management, and security. These factors may vary between urban or rural areas.

### **What Are the Existing Transfer Patterns of Potential Clients?**

Potential providers should gauge the size and characteristics of money transfers from both international and domestic sources. How often do clients typically send or receive transfers? How large are these transfers? It is important to note the difference between average and modal transfer amounts, as averages can be skewed upward by a few large transfers, while the most frequent transfer amounts may be much smaller. This information is vital for pricing and revenue projections because fees usually depend on the amount transferred.

Patterns of seasonality in remittances can also influence marketing efforts, financial projections, and the design of complementary financial products. An FSP must consider the likelihood that migration patterns might be disrupted or changed by political or natural events. Finally, FSPs should consider how transfer patterns have evolved over time and the effects of long-term changes in the volume or frequency of transactions. In the case of remittances, research indicates that migrants take some time after immigration to establish regular money transfer patterns, and that remittances may taper off after immigrants have spent significant time in the host country. The effect of current labor movements on money transfers may thus not be felt for several years.<sup>54</sup>

### What Product Features Do Clients Prefer?

Table 7 shows generally observed customer preferences vis-à-vis money transfer services. The attributes considered in the table form the core of money transfer product design and can guide a pro-poor FSP to identify its market niche.

### What Other Financial Services Do Clients Want?

Services linked to transfers can attract clients, keep them loyal, and generate additional revenue. Access to other financial services may also deepen the developmental impact of transfers. Initially, recipients may not trust an FSP to hold their money, preferring instead to receive cash immediately. Over time, however, a client may consider banking some of the transferred funds in a linked savings or checking account, if such options are available.

The same possibility exists on the sending end: migrants may gradually begin to use other financial services if an FSP offers them. Banco Solidario in Ecuador, for example, has developed products in conjunction with banks in Spain that allow Ecuadoran migrants working in Spain to access and repay short-term credit, save for their return home, buy real estate in Ecuador, or create savings accounts in Ecuador to which they can control access by family members.

### Competition

Along with regulation, competition is one of the most important external considerations of an FSP money transfers strategy. A pro-poor FSP should identify which formal and informal money transfer agents operate in its region, the transfer

**Table 7 Client Preferences in Money Transfer Services**

Attributes Sought	Key Issues
Accessibility	Many migrants, especially undocumented workers, prefer few or no <b>identity requirements</b> , but most formal money transfer operators must comply with some type of identity stipulation. Financial institutions can also set other requirements (e.g., opening a bank account or maintaining a minimum balance) that impede the access of poor people to transfer services.
Confidentiality	Some clients prefer to keep their receipt of money transfers <b>confidential</b> (either to reduce claims within the family, or to minimize the risk of theft) and may favor using providers like specialized money transfer companies, that may have less stringent identity documentation requirements than multi-service financial institutions.
Cost and transparency	Most people seek transfer services that offer <ul style="list-style-type: none"> <li>• low <b>fees</b>;</li> <li>• attractive <b>exchange rates</b>; and</li> <li>• <b>transparency</b> on fees and exchange rates at both the sending and receiving ends.</li> </ul>
Ease of use	People prefer <b>limited paperwork</b> to send or collect funds, especially if they are not literate. Some people prefer <b>interacting</b> with a sales agent for reasons of ease and personal service. Others prefer the <b>convenience</b> and <b>anonymity</b> of ATMs or POS devices.
Safety	Transfer operators must earn the trust of migrants and their families. <ul style="list-style-type: none"> <li>• Clients may be reluctant to seek services from banks or formal financial institutions, due to mistrust or <b>past experiences</b> in their home or adopted country.</li> <li>• Many people prefer to send money transfers through institutions that have a <b>track record</b> in handling transfers and other financial services, and/or belong to a larger, well-known international network.</li> </ul>
Speed	Many people prefer <b>“real-time”</b> transfers, regardless of the cost or urgency of the transfer.
Transaction convenience and cost	Both senders and recipients want to transfer funds at <b>nearby locations</b> and <b>reduce other transaction costs</b> , such as travel time, travel expenses, and bribes paid for better service.

Sources: ACCIÓN, *Leveraging the Impact of Remittances*; Barro and Sander, “Étude sur le transfert d’argent”; Cross, “Migrant Workers’ Remittances”; ILO, “Making the Best of Globalisation”; Marx, “Remittances and Microfinance”; Siddiqui and Abrar, “Migrant Worker Remittances”; Thieme, “Savings and Credit Associations.”

mechanisms they use, and the volume of transfers that they process. Key formal actors can include commercial banks, money transfer operators, foreign exchange bureaus, post offices, credit unions, and microfinance institutions. Informal actors typically include informal transfer operators, travel agents, couriers, bus drivers, shop owners, business people, family, friends, and migrants themselves (via personal delivery).

An FSP should assess competitors' strengths and weaknesses in addressing client preferences, including both formal and informal operators. A competitive analysis should enable FSPs to determine whether they can offer customers a better product and thus identify their comparative advantage as a provider. Can the FSP compete in terms of cost, speed, transaction security, location, client-friendly service, and/or linked financial products?

Current formal transfer providers may offer safe and fast services, but these services may be expensive or accessible only in urban centers. Alternatively, existing services may require clients to open a bank account with an unaffordable minimum balance. Informal transfer providers tend to be particularly strong on customer service, so poorer FSPs must offer similar, or better, service to compete effectively.

## Regulation

The regulatory environment determines many of the options available to an FSP seeking to enter the money transfer market, including whether the service provider will have

- direct access to foreign exchange;
- the legal right to become an agent or sub-agent of an MTC (or face other licensing and operating requirements, such as being a licensed bank);
- access to the national payments system;
- to comply with anti-money laundering regulations;
- to pay government taxes on transfers.

Due to common restrictions on the type of institutions that can deal in foreign exchange or process payments, few non-bank FSPs are likely to be licensed to handle international money transfers on their own.<sup>55</sup> However, those that are regulated as banks or as part of a credit union federation may qualify for a license, depending on the national regulatory environment.<sup>56</sup>

Regulatory issues are, moreover, not limited to the receiving country. Licensing regulations can have an adverse effect on money transfer operators on the send side and limit the scope for international commercial alliances. For example, new "Know Your Customer" regulations promulgated in South Africa have made banks reluctant to

### Box 6 "Know Your Customer" Regulations in South Africa

In South Africa, the Financial Intelligence Centre Act of 2001 created stringent "Know Your Customer" requirements. Banks, insurance companies, money remitters, casinos, attorneys, and foreign exchange bureaus are required to identify and verify the identities of their customers, keep relevant records, report suspicious and unusual transactions, and establish necessary compliance procedures.

Financial institutions are required to obtain clients' full name, date of birth, identity number, and residential address. They must then verify this information by comparing it with an identification document. When necessary, these particulars must also be compared with information obtained from an independent source. In the event that a bank does not receive the necessary information from customers, the law stipulates that it must freeze "questionable" accounts until it can verify an account holder's identity.

These requirements have generated considerable protests from South African banks, which find it difficult to obtain the required proofs of identification and residence from their poorest clients. The new requirements also increase the cost of money transfer services for this target group. Institutions were originally given until June 30, 2004, to implement identification and verification procedures. In response to bank protests, the minister of finance pushed back the compliance deadlines to December 31, 2004, for high-risk clients and to September 30, 2006, for low-risk clients.

Sources: Genesis Analytics, "African Families" and "Access to Finance"; Lee, "KYC Deadline."

partner with MTCs. South Africa attracts many labor migrants from neighboring countries, and they represent a huge market for transfers. However, banks and other FSPs report concerns about complying with tightened security precautions required by the “Know Your Customer” law.<sup>57</sup>

This is true not only in South Africa but around the world, as governments attempt to comply with recommendations on anti-money laundering and combating the financing of terrorism by imposing increasingly strict requirements on cross-border money transfer providers.<sup>58</sup> Country implementation of international recommendations varies, although common elements include more requirements for customer identification (i.e., “know your customer”), responsibility to alert officials about suspicious patterns or individual transfers, and increased reporting requirements. Regulations affecting domestic transfers are presently not as extensive.

### **Infrastructure**

The physical and financial infrastructure of a given country will greatly affect an FSP’s choice of money transfer mechanism, if not the viability of the potential service. The geographic coverage of the power grid and telecommunications network in part will determine whether an FSP can offer real-time transfers to remote areas, although alternative arrangements and new technologies are beginning to overcome these obstacles. Financial infrastructure such as widespread POS networks, an automated clearinghouse, or other payment system (and the institution’s access to it) will also shape an institution’s choice of transmission mechanism(s).

### **Institutional Capacity**

Internal considerations are as important as market factors in the money transfers strategy of a pro-poor FSP.<sup>59</sup> Institutions must evaluate themselves before deciding whether to launch any new service. Money transfer operations require a significant

investment in skilled human capital, which adds to the cost of the service. New operators need to train staff and/or hire specialized staff for customer relations and back-office functions. Information systems must be capable of managing the volume of anticipated transfers, ensuring transaction security, possibly interfacing with other transfer operators, and generating reports to comply with regulations (e.g., anti-money laundering legislation).

Transfer operators must also have the capacity to carefully manage liquidity and, if they receive cross-border transfers directly, foreign exchange risk. The ability to analyze and change prices rapidly is important, as FSPs must consider the competition when setting fees, commissions, and foreign exchange rates to convert payments to local currency.

As described earlier, alliances can help FSPs launch remittance services with lower initial investments *and* avoid barriers to entry. This arrangement leaves the FSP to concentrate on functions such as customer service, where it may have a strong comparative advantage.

### **Financial Analysis**

Because launching a money transfer service can require significant investment and is expected to generate profits, initial financial projections and ongoing financial analysis are critical. Financial projections must begin with a demand forecast based on informed estimates of long-term transfer trends among the potential client base. Although a region may generate large amounts of transfers at a given point in time, flows can fluctuate or dry up if migration is not sustained.<sup>60</sup> Money transfers are essentially a volume business, so confidence about future volume is crucial, especially if the method chosen requires a large initial investment.

The profitability of the money transfer service itself is not, however, the only argument for pro-poor FSPs to enter the money transfer business. As



a relationship product, money transfers give FSPs the opportunity to acquire new and retain existing customers. In their financial analysis, therefore, FSPs should estimate projected revenues from cross-selling other financial services, as well as savings generated by increased customer retention.

## Marketing

In markets where many transfer options are available, marketing information is often superficial, making it difficult to understand or compare prices, speed of delivery, and other aspects of the service. In environments with few transfer services, however, marketing is instrumental for introducing the new service to clients. In all cases, continuous targeted marketing is the key to attracting clients.

Many recipient institutions overlook the crucial role that send-side marketing plays in generating

transfers. One of the chief ways that leading MTCs maintain their dominant market share is through well-funded media campaigns. FSPs that partner with such companies will benefit from their marketing efforts. FSPs that choose other options, however, must compensate for the lack of an established marketing machine. One of the most promising strategies available to such institutions is marketing targeted at specific ethnic communities (see box 7).

## Conclusion

Because many people who send and receive money transfers are poor and do not patronize mainstream banks, they are a natural target market for pro-poor FSPs. These businesses have a social interest in providing poor clients a crucial financial service at low cost. They also have a potential

### Box 7 Send-Side Marketing by FONKOZE in Haiti

Send-side marketing is crucial to the success of money transfer services in recipient countries, but can be easily overlooked. The Haitian MFI FONKOZE learned this lesson when it launched its own, low-cost money transfer service in cooperation with a commercial bank in the United States. Although it negotiated attractive terms with the bank and generated a break-even transaction volume, the new transfer product did not produce sufficient profits to invest in improving the service.

FONKOZE consequently formulated a send-side marketing campaign targeted at the Haitian community living in the United States. At first, FONKOZE planned to produce public service announcements, purchase targeted radio and print advertisements, and conduct radio interviews in US cities with large Haitian populations. However, the MFI quickly realized that this type of expensive marketing was better at producing market awareness than changing client behavior.

Since FONKOZE's money transfer service works quite differently than a typical MTC (a customer mails a check to the US bank partner of FONKOZE, which then sends the funds to the Haitian MFI), it needed a marketing campaign that could convince potential clients to do things differently, rather than simply change service providers. The MFI also needed to overcome an image of unreliability that small institutions offering low-cost services have among many Haitians abroad.

The result was an innovative campaign of "family days" at FONKOZE branches in Haiti, during which the institution rented out cyber-café and gave customers a free five-minute phone call to the United States. FONKOZE also gave non-clients free phone calls, provided they took the money they would have spent on a call and opened an account with the microfinance institution. Using this technique, the first event generated 100 new accounts in a single day. Costs were controlled because the MFI did not pay for individual calls, but purchased them in bulk at a deep discount by paying the cyber-café a daily rate.

During the calls, grateful clients almost invariably mentioned FONKOZE to their relatives, producing a referral from a trusted source—the best kind of publicity the institution could generate. The calls also produced a targeted list of clients who already send money to FONKOZE clients on a regular basis, representing an ideal market for its money transfer service. FONKOZE is currently developing a brochure and educational video on the service for these potential clients. The MFI is betting that this focused strategy will yield better customer conversion rates than the expensive, untargeted media placements used in the past.

Source: Author interview with Anne Hastings, director, July 1, 2004.

financial interest in money transfers because the service may enable them to increase revenues, attract new clients, cross-sell existing services, and develop new linked products.

Although a great deal of research remains to be done—particularly on transfer flows within developing countries and regions<sup>61</sup>—it is clear that there is a growing, multibillion-dollar market for money transfers. This market is evolving quickly given changing technology, new market players, and increasing competition. As transfer volumes, profits, and operators continue to increase, greater transparency on the costs and services of money transfer operators will be required.<sup>62</sup>

Given the lack of data on money transfers in poor countries, this paper has provided a high-level overview of the global money transfer market. Specific FSPs must compare this overview against the realities of their own markets to determine client demand and desired product features in their respective regions. Before launching any new product, but especially a highly complex one like money transfers, FSPs must give careful consideration to the internal and external factors that shape a viable market entry. These factors include client preferences, competition, and regulation. Regulation is particularly relevant to money transfers because national laws may prohibit certain types of institutions from accessing specific transfer mechanisms (for example, non-bank financial institutions may not be allowed to conduct foreign exchange transactions, issue checks, or link into payment networks).

Alliances that allow FSPs to offer money transfer services may be the best approach for new market entrants. The customer base, location, and existing distribution infrastructure of pro-poor FSPs can make them attractive partners for existing money transfer operators. The international

payment networks, foreign exchange access, and risk management expertise of specialized money transfer companies and commercial banks can, in turn, reduce both the cost and risk of a pro-poor FSP's entry into the market.

In addition, new customer interfaces that reduce the cost of providing access to far-flung clients are multiplying the possibilities for offering money transfer services to poor clients. Policymakers and donors can play a role in eliminating the bottlenecks in regulations, information, infrastructure, and existing services that currently prevent poor clients from deriving the maximum benefit from money transfers.

Although the money transfer market offers tantalizing opportunities for pro-poor FSPs, the risks can be high. FSPs should proceed with caution in evaluating the potential for such services and learn from the experience of pro-poor institutions that have already launched them. Money transfers providers must also carefully weigh the competition from informal operators and mimic certain product characteristics that give these services their competitive edge. A viable money transfers strategy must be underpinned by a keen understanding of institutional capacity, the ability to launch a new product, thorough financial analysis, and a robust plan for marketing the service to current and new clients.

The considerations discussed in this paper are not meant to discourage pro-poor FSPs from entering the transfer market. On the contrary, the paper is intended to help FSPs undertake the serious analysis needed to decide whether and how to introduce a money transfer product. As more poor households in developing countries come to rely on income earned elsewhere, demand for these products will continue to increase. Satisfying this demand for diverse financial services is crucial to building financial systems that truly serve the poor.



## Appendix 1 Estimates of Money Transfer Revenues\*

**Table 8 Total Revenue from Cross-Border Retail Payments, by Source**

	2001		2011		Compound annual growth rate (CAGR)
	US\$ billions	% of total	US\$ billions	% of total	
Fees	6.9	66%	9.1	63%	2.8%
Foreign exchange	3.4	33%	5.3	36%	3.4%
Float	0.1	1%	0.1	1%	-0.1%
<b>Total</b>	<b>10.4</b>		<b>14.5</b>		<b>2.90%</b>

Note: 2011 figures are projections.

**Table 9 Average Revenue per Cross-Border Retail Payment, by Source**

	2001		2011		Compound annual growth rate (CAGR)
	US\$	% of total	US\$	% of total	
Fees	3.5	66%	1.8	59%	-6.60%
Foreign exchange	1.7	34%	1.0	37%	-5.0%
Float	0.1	0%	0.0	0%	-9.3%
<b>Total</b>	<b>5.3</b>		<b>2.8</b>		<b>-6.10%</b>

Note: 2011 figures are projections.

**Table 10 Total Revenue from Domestic Retail Payments, by Region (US\$ billions)**

	2001	2011	CAGR
Asia	33	66	7.1%
Americas	102	143	3.5%
Europe	42	67	4.7%

Note: 2011 figures are projections.

**Table 11 Average Revenue per Domestic Retail Payment, by Region (US\$)**

	2001	2011	CAGR
Asia	1.33	0.94	-3.4%
Americas	1.42	1.17	-1.9%
Europe	1.09	0.86	-2.4%

Note: 2011 figures are projections.

\* Adapted from and reprinted with permission of Boston Consulting Group, *Preparing for the Endgame: Global Payments 2004* (London: Boston Consulting Group, 2004). BCG defines payment revenues as derived from five sources: sale of non-cash transactional products (checks, credit cards, ACH payments, current accounts, debit cards), float revenues on payments, all interchange revenues except from ATMs, and direct interest revenues (revenues from current accounts and credit cards directly related to their use as payment instruments).

## Appendix 2 Informal Money Transfer Systems

Informal funds transfer systems vary tremendously in structure and complexity.<sup>A1</sup> Hand carrying cash, usually by migrants themselves or by family and friends, is the most basic system and is especially common in situations of seasonal or circular migration, where migrants frequently return to their place of origin.<sup>A2</sup> In some countries, the physical transfer of cash is also done by couriers (internationally) or bus companies and taxi drivers (domestically).

Other systems involve only the virtual movement of funds. A basic two-way system is common between West Africa and France, where two people (one in the home country and one overseas) collect and distribute money transfers in their respective communities, settling periodically through their respective individual bank accounts. These transfer providers can move sums significant enough to meet the needs of traveling business people, who often do not hold credit cards and prefer to transfer cash via informal channels rather than face the safety, customs, and foreign exchange issues involved in carrying large amounts of cash.<sup>A3</sup>

More sophisticated informal systems exist under different names around the world, including *hundi* (South Asia), *fei-chen* (China), *hui kwan*

(Hong Kong), *padala* (Philippines), *phei kwan* (Thailand), and *hawala* (Middle East).<sup>A4</sup> Many of these systems, such as those common in African mineral-exporting countries like Angola, evolved as mechanisms for trade financing and net funds transfers against the movement of goods.<sup>A5</sup>

The hawala system used in the greater Middle East is representative of how such systems work. Typically, a migrant makes a payment to an agent (*hawaladar*) in the country where he works and lives, and the hawaladar gives him a code to authenticate the transaction. The hawaladar requests his counterpart at the receiving end to make the payment to a beneficiary upon submission of the code.

After the transfer, hawaladars settle accounts through payment in cash or in goods and services. They are remunerated by senders through a fee or an exchange rate spread. Hawaladars often exploit fluctuations in demand for different currencies, which enables them to offer customers better rates than those offered by banks (most of which will only conduct transactions at authorized rates of exchange). Since many hawaladars are also involved in businesses where money transfers are necessary, such as commodity trading, remittance services fit well into their existing activities. Remittances and business transfers are processed through the same bank accounts and few, if any, additional operational costs are incurred.<sup>A6</sup>

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<sup>A1</sup> For descriptions of particular systems, see Kabbucho, Sander, and Mukwana, “Passing the Buck”; Jaramillo, *Leveraging the Impact of Remittances*; Mellyn, “Worker Remittances as a Development Tool”; and Genesis Analytics, “African Families.”

<sup>A2</sup> Fagen and Bump, “Remittances between Developing Neighbors.”

<sup>A3</sup> Blion, *Les revenus de la migration*.

<sup>A4</sup> For more information on the *hawala* system, see El Qorchi, “Hawala.”

<sup>A5</sup> Barro and Sander, “Étude sur le transfert d’argent.”

<sup>A6</sup> See Jost and Sandhu, *Hawala Alternative Remittance System*.



## Endnotes

- 1 See, for example, Interamerican Dialogue, "All in the Family"; IDB, "Remittances as a Development Tool"; World Bank and DFID, "International Conference on Migrant Remittances"; ILO, *World Migration Report 2000*; Group of Eight, "G8 Action Plan." Remittances are defined as the portion of migrant-worker earnings sent to family members or other individuals in their place of origin.
- 2 Ratha, "Worker's Remittances," 157.
- 3 Bezard, *Global Money Transfers*, 20.
- 4 FSPs that cater to the poor include financial institutions of all kinds, as well as non-financial institutions, such as retailers, that provide financial services as part of larger product mix. In this paper, the term "FSPs" is used to indicate financial service providers that deliberately offer products and services to clients below the socioeconomic level normally served by mainstream commercial banks.
- 5 Many of the resources listed in the bibliography contain more information on the potential benefits and developmental impact of secure, convenient, low-cost money transfer services in the lives of clients and their families. See for example Interamerican Dialogue, "All in the Family"; ILO, "Making the Best of Globalisation"; IMP, "Migrant Remittances"; and Van Doorn, "Migration, Remittances, and Development." As this paper takes a more institutional perspective, discussion of clients is therefore limited mainly to their preferences as money transfer consumers.
- 6 Boston Consulting Group, *Preparing for the Endgame*.
- 7 One notable exception is South Africa, where Absa Bank is issuing Visa cards that enable citizens to collect pensions and child and disability benefits. See Rodrigues, "Payment Solutions for Economic Growth." In other countries, salaries and pension payments to formal-sector employees are also sometimes transmitted through the banking or postal system.
- 8 The best data currently available on worldwide money transfers is compiled by the International Monetary Fund (IMF). This data provides the foundation for estimates developed by other institutions and researchers in the field. The Inter-American Development Bank (IDB) has conducted a number of studies on money transfers, although these studies focus exclusively on countries in Latin America. The International Organization for Migration (IOM) has also sponsored a growing number of remittance studies in individual countries around the world. Additional studies are presently being conducted by the World Bank, the UK Department for International Development (DFID), and CGAP. Unfortunately, comprehensive studies of domestic, intra-, and inter-regional remittances do not exist for all regions of the world. (In some cases, such transfers are not even officially tracked.) This paper relies on three sources that the authors consider to offer the most reliable and comprehensive data available: World Bank, *Global Development Finance*; Bezard, *Global Money Transfers*; and Boston Consulting Group, *Preparing for the Endgame*.
- 9 World Bank, *Global Development Finance*. The World Bank remittance figures are calculated on the basis of the IMF *Balance of Payments Yearbook* of 2001. The US \$93 billion figure includes worker remittances, employee compensation, and migrant transfers.
- 10 IMP, "Global Migration Challenges," 3.
- 11 World Bank, *Global Development Finance*. It must be noted, however, that severe underreporting of remittances data is common in sub-Saharan Africa.
- 12 Ratha, "Workers' Remittances."
- 13 Bezard, *Global Money Transfers*, 20.
- 14 IDB, *Sending Money Home*; Orozco, "Worker Remittances"; interview with Jan Riedberg, September 21, 2004; Mellyn, "Worker Remittances."
- 15 Brocklehurst, "Remittances and Development."
- 16 Industry revenues were calculated on the basis of Western Union's 2003 revenues and 2002 industry revenue share, cited in Bezard. Almost the identical number can be calculated by dividing the World Bank estimate of the value of total formal transfers made in 2003 by the MoneyGram estimate of the average money transfer (US \$93 billion divided by \$300), yielding approximately 310 million total transfers. However, these numbers produce an average of \$56 in revenue per transaction processed, suggesting that figures on the money transfers industry may be most indicative of order of magnitude.
- 17 First Data Corporation, SEC Form 10-K. The US \$3.3 billion in revenues earned by First Data Corporation in 2003 (parent company of Western Union) on \$24.3 billion in transfers (equivalent to 81 million transfers of approximately \$300 each) represented 13.6 percent of the total value of transfers processed by Western Union. This percentage corresponds to Ratha's estimate that financial institutions worldwide charge an average of 13 percent of the value of a money transfer as a processing fee.
- 18 Bezard, *Global Money Transfers*, 14.
- 19 MoneyGram, SEC Form 10. Other sources estimate a slightly lower average: Ratha, "Workers' Remittances"; Jamaica Cooperative Credit Union League, "People2People Money Transfers." Averages may also be skewed by a small number of large transfers. Modal transfer amounts—the amounts most frequently sent—are often smaller. In general, regional transfer averages probably have more relevance to analysis of the transfer market than do worldwide averages, as transfer amounts vary widely by both region and transmission channel.
- 20 See First Data Corporation, SEC Form 10-K. Return on equity for First Data as a whole was 25.33 percent in 2003. Return on equity for MoneyGram could not yet be calculated when this paper went to press because of the July 2004 spin-off from its former parent Viad Corporation; results of its first quarter of operations had not yet been released.
- 21 Bezard, *Global Money Transfers*.
- 22 MoneyGram, SEC Form 10. The omnipresence of Western Union agents in countries around the world explains a large part of the company's market dominance. While MoneyGram has some 63,000 transfer agents in 160 countries, Western Union has 182,000 agents in 192 countries. See First Data Corporation, SEC Form 10-K.
- 23 Boston Consulting Group, *Preparing for the Endgame*.
- 24 Income derived from the investment of third-party funds during the time between the deposit and payment of those funds.



## Endnotes *continued*

- 25 Bezard, *Global Money Transfers*; First Data Corporation, SEC Form 10-K.
- 26 ILO, "Migrant Worker Remittances."
- 27 IOM and United Nations, *World Migration Report*.
- 28 Boston Consulting Group, *Preparing for the Endgame*. No data was available for Africa and the Middle East.
- 29 See Fagen and Bump, "Remittances between Developing Neighbors"; Cross, "Migrant Workers' Remittances and Microfinance in South Africa"; and Sander, "Capturing a Market Share?"
- 30 See Sander, "Capturing a Market Share?" In the author's words, "for instance, a study on Vietnam showed that 7 out of 8 transactions received were domestic remittances, but they constituted only 50 percent of the value."
- 31 Kyngé, "China's Urban Workforce."
- 32 Ratha and Bezard both estimate the size of the informal market to be approximately 40 percent of the formal market, but some private industry actors interviewed by the authors estimate it to be as large as the formal market.
- 33 Blion, *Les revenus de la migration* (Mali/Senegal); Sander, "Capturing a Market Share?" (Sudan); Thieme, "Savings and Credit Associations" (Nepal); Bezard, *Global Money Transfers* (Asia/Middle East).
- 34 Bezard, *Global Money Transfers*, 10.
- 35 Systems that allow individual payment orders to be settled one by one rather than by periodically netting debits and credits between two parties.
- 36 Boon and Greathouse, "Role of Postal Networks."
- 37 Information for this section is drawn from the Bank for International Settlements and an interview with Andre Boico, marketing director, SWIFT, June 23, 2004.
- 38 ACH is a batch-process settlement system, where transactions are typically settled overnight, which incurs lower costs than a real-time gross settlement system.
- 39 Messages routed over SWIFT are simply instructions to transfer funds; the actual exchange or settlement of the funds takes place subsequently through a payment system or correspondent banking relationships.
- 40 Banks may also bundle and send a batch of person-to-person transfers via SWIFT.
- 41 The cost of joining SWIFT is also a major obstacle for smaller institutions. In addition to buying shares, SWIFT members pay a one-time membership fee of several thousand euros, plus a yearly fee of over €1,000 per routing code. The number of codes an institution buys usually depends on the number of its branches or divisions that are linked to SWIFT.
- 42 Sander, "Capturing a Market Share?"
- 43 Boon and Greathouse, "Role of Postal Networks."
- 44 Interview with the special projects manager (name withheld), Jamaica Cooperative Credit Union League, September 2003.
- 45 Taber, "Integrating the Poor."
- 46 Interview with the special projects manager (name withheld), Jamaica Cooperative Credit Union League, September 2003.
- 47 WOCCU, *Technical Guide to Remittances*.
- 48 The multiplicity of customer interface technologies has important implications for increasing the access of poor clients to financial services because these technologies enable providers to reach more clients without incurring the cost of additional physical infrastructure. The costs and benefits of various cash access technologies are discussed at length in the CGAP IT Innovations Series, [www.cgap.org/publications/microfinance\\_technology.html](http://www.cgap.org/publications/microfinance_technology.html).
- 49 Electronic device capable of reading a magnetic strip and/or smart card, such as a credit or debit card.
- 50 CGAP interview with Sam Kamiti, director of operations, CRDB Bank Limited, May 3, 2004.
- 51 Rodrigues, "Payment Solutions for Economic Growth."
- 52 Bezard, *Global Money Transfers*.
- 53 Orozco, *The Remittance Marketplace*, 1.
- 54 Frumkin, "Remittances: A Gateway to Banking."
- 55 Sander, "Capturing a Market Share?" 30.
- 56 In general, regulation needs to balance the goals of minimizing illegal activities and promoting cost-efficient, transparent, and accessible transfer services. Several donor agencies have begun to promote dialogue among regulators, money transfer providers, and financial institutions to ensure that transparency does not come at the cost of reduced access and increased cost for poor clients. In June 2004, for example, the World Bank and the organization for Asia Pacific Economic Cooperation (APEC) sponsored a conference on how money transfers could be transitioned from the informal to the formal sector. Presentations and case studies from the conference are available at [www.amlcft.org](http://www.amlcft.org).
- 57 Genesis Analytics, "Access to Finance."
- 58 Many such recommendations are made by the Financial Action Task Force (FATF), an international grouping of nations that fight money laundering and the financing of terrorism. FATF currently has 33 individual country members and 25 observer bodies and institutions. Further information can be found on the FATF website, [www.fatf-gafi.org](http://www.fatf-gafi.org). FATF has developed 40 recommendations and interpretive notes for financial service providers. These recommendations are available online at [www.fatf-gafi.org/40Recs\\_en.htm](http://www.fatf-gafi.org/40Recs_en.htm). CGAP and the World Bank are also developing an overview of AML/CFT issues that will be available in mid-2005.
- 59 See WOCCU, *Technical Guide for Remittances*, 10–12.
- 60 See, for example, Blion, *Les revenus de la migration*; and Ratha, "Workers' Remittances."
- 61 The Group of Eight (G8) countries committed to improving their data on transfers, especially on the send side, at the Sea Island Summit in Georgia, USA, June 9–10, 2004. A similar effort is needed on the part of receiving countries. At the global level, institutions such as the World Bank and the International Monetary Fund, are already working to improve data on worldwide transfer volumes. At the regional level, however, much less is known about international transfer flows outside of Latin America. Even less data is available on domestic payments within developing countries, which poorer clients are likely to use much more frequently than international transfers.

62 The Inter-American Development Bank led a taskforce in 2003 to develop goals and recommendations for public and private entities to improve money transfer services in

the Latin American transfers market. See IDB, *Sending Money Home*.



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