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Arab Financing for Development Scorecard

International private finance: remittances

Summary

International migrant remittances, a major source of international private finance, amounted to $831 billion in 2022, of which the Arab region received $69.2 billion, outpacing foreign direct investment and official development assistance inflows received by the region since 2013. However, in 2022, the region received less than its share of remittances, be it in terms of the volume of migrants it hosted or the value of remittances it generated. By 2030, it is anticipated that migrants will remit over $5 trillion, of which $450–$636 billion is projected to be channelled to the Arab region, prompting the need to establish necessary channels to transform these flows into sustainable productive investments. Nonetheless, for every $1 received in remittances on average between 2008–2022, the region correspondingly repatriated $2.82 to other regions/countries owing to political and labour market factors, skill mismatches, and a growing reliance on foreign workers. On average, each Arab migrant remitted in 2022 roughly $2,321 per year, or a third less than the average for other international migrants.

Since 2011, correspondent banking relationships (CBR) declined by 22 per cent worldwide, which has contributed to a relative decline in the Arab region's remittance inflows; but both the value and volume of CBR has increased, suggesting higher market concentration. In the Arab region, however, CBR declined and so have the values and volumes of cross-border payments. The remittance value chain remains highly fragmented, driving up costs. Had remittance transfer costs been reduced to 3 per cent, as prescribed by Sustainable Development Goals 10.c, the Arab region could have gained $14 billion between 2015 and 2022, representing a hefty opportunity lost to finance sustainable development and support essential household expenditures. Equally, digitization has been changing the way remittances are transferred, leveraging mobile applications, online platforms, and digital wallets. The development of next generation digital infrastructure (networks, devices and applications) is an integral part of the discourse over how international private finance could be incentivized and harnessed for productive purposes to achieve sustainable development.

The Committee on Financing for Development in the States Members of the Economic and Social Commission for Western Asia is invited to consider the global trend and regional realities set out in the present document, and comment on the recommendations for Arab collective action needed to harness the expected increase in remittances.

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Introduction

1. Remittances are an important source of cross-border international finance that cannot be equated to other international private flows, owing to the social contract that binds migrants to their families. As a result, remittances are often relatively resilient to external shocks, as evidenced in the 2008 financial crisis and during the COVID-19 pandemic. On average, 75 per cent of remittances are used to alleviate poverty (Sustainable Development Goal (SDG) 1), reduce inequality (SDG 10), and cover essential needs such as food (SDG 2), education (SDG 4), health (SDG 3) and housing (SDG.11). More recently, they have also provided support for communities to adapt to changing climate conditions (SDG 13). All these factors remain at the core of the 2030 Agenda for Sustainable Development, and contribute to human capital development. Notably, in low-income and middle-income countries, remittances exceeded three times the amount of official development assistance (ODA) and foreign direct investments (FDI) that they received in 2022.

2. Remittances play a crucial role as a source of foreign exchange, and have significant implications for the overall economy, influencing both production and consumption patterns. In the current era of polycrisis, the United Nations has urged all stakeholders in both origin and recipient countries to maximize the socioeconomic benefits of remittances. This includes reducing transfer costs, promoting access to digital solutions for faster, safer and more affordable transfers, and ensuring the financial and digital inclusion of all migrants and their families.

I. Global versus regional realities

Trends in migration

3. Remittances serve as a lifeline for the families of 34.2 million Arab migrants,[1] an indispensable support that has become even more crucial amid the cost-of-living crisis underpinned by increasing inflation. As conscious agents, migrant remittances can be driven by altruism (1 in 10 people in the region wholly rely on remittances to meet basic needs),[2] or by economic motives to take advantage of investment opportunities or interest rate differentials, and to support social aims (remittance inflows to Morocco, for example, are associated with school attainment).[3] ESCWA studies indicate that remittances to the region are predominantly driven by altruism, and are directed to non-productive investments and consumption.[4]

4. In 2021, the total number of international migrants reached 282 million, of which 10.6 per cent were of Arab origin.[5] The six Gulf Cooperation Council (GCC) countries alone hosted 30 million international migrants (75 per cent of total international migrants in the region), of which 6.47 million migrants were from the Arab region. While the exodus from conflict-ridden countries such as the Syrian Arab Republic and Yemen contributed to this trend, Egypt observed the highest rates of migration at 41 per cent in 2021.[6]

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[1] ESCWA, Situation Report on International Migration 2021: Building Forward Better for Migrants and Refugees in the Arab Region, 2022.

[2] Impacts on Migrants and Remittances. https://www.undp.org/sites/g/files/zskgke326/files/migration/arabstates/Compounding_Crisis_UNDP_Feb07-2021_Combined_v3-68-79.pdf.

[3] Ibid.

[4] ESCWA, International migration and development in the ESCWA region: challenges and opportunities, 2011.

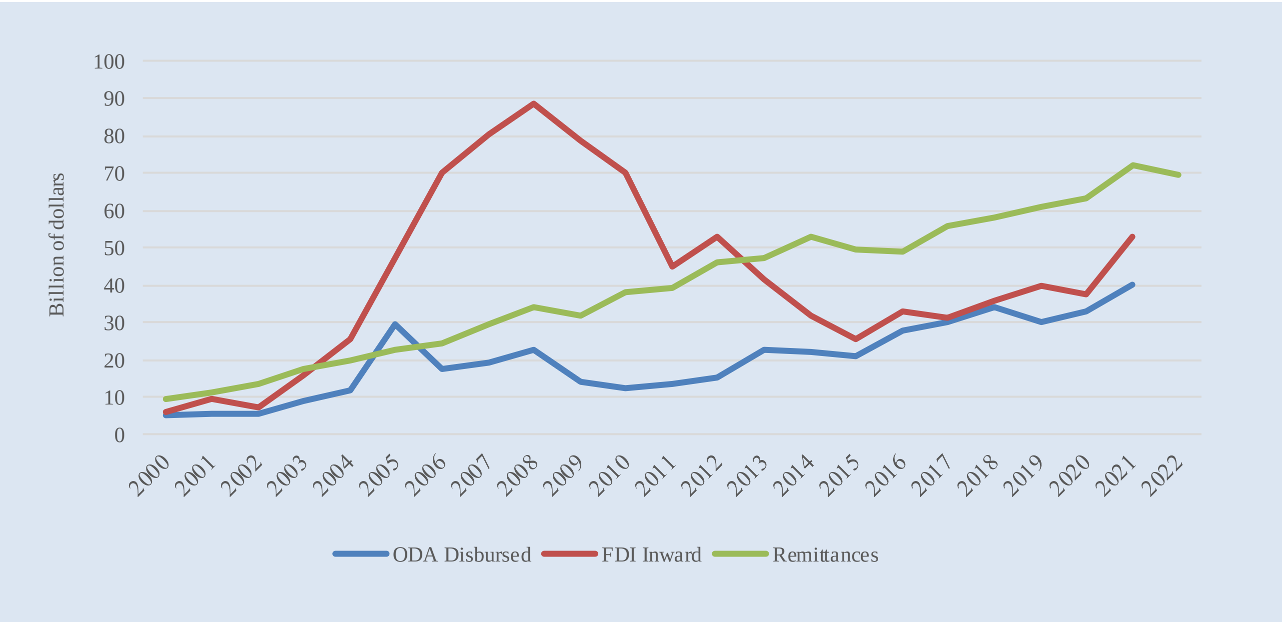
[5] Data on migration are based on KNOMAD/World Bank Bilateral Migration Matrix 2021, December 2022.

[6] ESCWA calculations based on KNOMAD/World Bank Bilateral Migration Matrix 2021, December 2022.

II. Scale of remittance inflows and outflows

5. International migrant remittances increased by 5 per cent to reach $831 billion in 2022. However, the Arab region witnessed a drop of 3.8 per cent as remittances declined to $69.2 billion, constituting 8 per cent of total migrant remittances (compared with a record high of 9.3 per cent in 2003). In other words, Arab migrants remitted less than their share in international migration, at roughly $2,321 per migrant. Nonetheless, despite the fallout from the COVID-19 pandemic, remittances (which constitute a prime component of international private financial flows for many low-income and middle-income Arab countries) have been on a sharply rising trend. In the Arab region, remittances witnessed a robust compound aggregate growth rate (CAGR) of 4.9 over the 2011–2022 period (figure 1). These flows represent the single largest source of international private capital inflows for Algeria, the Comoros, Egypt, Jordan, Lebanon, Morocco and the State of Palestine, and their scale has outpaced the values of FDI and ODA received by the region since 2013.[7]

Figure 1. ODA, FDI and remittance flows to Arab countries, 2000–2022



Source: Data for ODA is based on the OECD creditor reporting system, FDI from UNCTAD, and remittances from the Global Knowledge Partnership on Migration and Development.

6. Remittance outflows from the region, mainly propelled by high-income GCC countries, reached $132 billion in 2021, representing nearly 16 per cent of worldwide remittances. Kuwait, Qatar, Saudi Arabia and the United Arab Emirates are among the world's top 10 countries in terms of both the value of remittance outflows and their share of gross domestic product (GDP). GCC countries average remittance outflows amount to 7.2 per cent as a share of their collective GDP. These outflows have been largely fuelled by a surging influx of foreign workers. Top recipients from GCC countries were Egypt, Lebanon and Morocco. Remittance inflows to Lebanon represented the highest at 35.7 per cent as a share of the country's GDP in 2022 (figure 2). ESCWA estimates that on average, for every $1 the Arab region receives in remittances, it correspondingly repatriates $2.82 to other regions/countries.[8]

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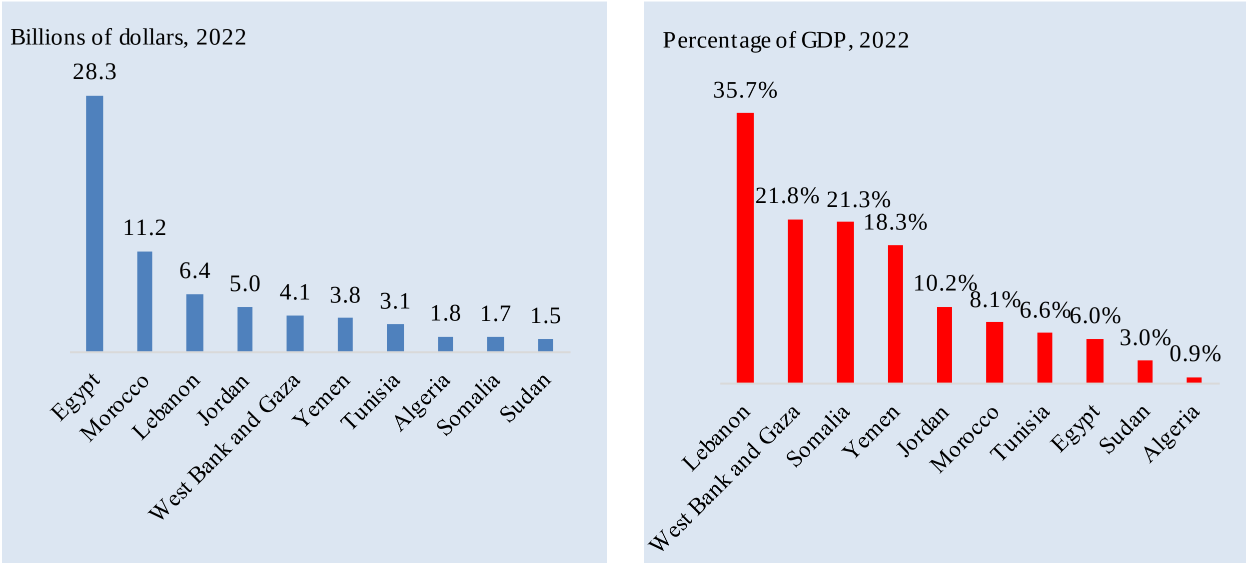
7 Excluding intra-Arab development assistance and regional concessional lending from within the region.

8 KNOMAD/World Bank Bilateral Remittance Matrix 2021, December 2022.

Figure 2. Top remittance recipients in the Arab region, 2022



Source: ESCWA calculations based on: Remittances – KNOMAD; GDP: IMF, World Economic Outlook Database, April 2023.

7. Remittances can be procyclical, countercyclical or acyclical to economic conditions in the recipient country. Empirical evidence shows a correlation between remittance outflows from GCC countries and oil price fluctuations. In the case of Arab recipients, the correlation between inflows of remittances and the recipient country's GDP is a dominant factor driving such inflows. For example, in the case of Egypt, ESCWA empirical findings indicate that in the long run, remittance inflows to Egypt are pro-cyclical. This behaviour can be seen by comparing the rate of change in the GDP of Egypt with the change in remittance inflows, which have followed each other neatly in the past decades with two interval exceptions (following the liberalization of the Egyptian pound in 2016, and the release of the International Monetary Fund (IMF) tranche from the Extended Fund Facility in the fourth quarter of 2017). IMF supports these findings, as the marginal propensity to remit is found to respond to conditions in the home country (Egypt), indicating that as Saudi Arabia real GDP increases by 1 per cent following a 1.3 per cent increase in Saudi oil supply, remittance outflows fall by 2.6 per cent on average.

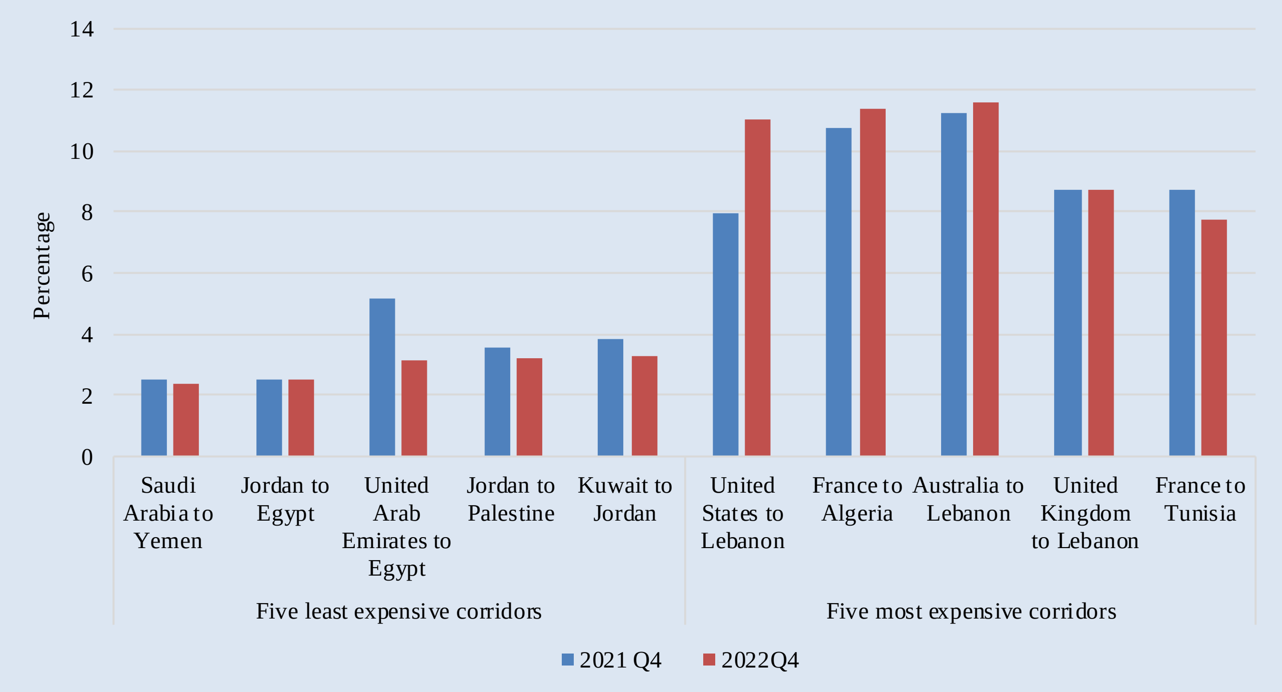
8. Globally, remittance growth is expected to moderate owing to slowing economic growth in major source countries. Growth of remittance flows is expected to rise by a modest 1.7 per cent in the Middle East and North Africa (MENA) in 2023, but estimates are being revised as these flows are expected to recede in the current global context. Downward pressures are not ruled out owing to de-risking practices and losses in correspondent banking relations associated with the cost of anti-money laundering/countering the financing of terrorism (AML/CFT) regulations. These costs will need to be revised as the relevance of AML/CFT is re-examined.[9]

III. Cost of remittances

9. The cost of transferring remittances varies widely across country corridors and types of remittance service providers. The global average cost of sending $200 in remittances remains double the target of 3 per cent set out in SDG10.c. While there has been a decline in costs due to the use of digital remittances, the cost of sending cash has remained at 6.2 per cent. Banks were the most expensive channel in 2022, with an average of 11 per cent, while mobile channels were the cheapest at 3.56 per cent. Moreover, there is a high degree of heterogeneity across individual remittance corridors, with costs above 10 per cent in many African corridors and for Pacific Island nations, and 42 per cent of corridors still have costs above 5 per cent.

[9] United Nations, Department of Economic and Social Affairs, Financing for Sustainable Development Report, 2023.

Figure 3. Remittances sent across the MENA region are lower than those sent from outside the region, 2021 and 2022



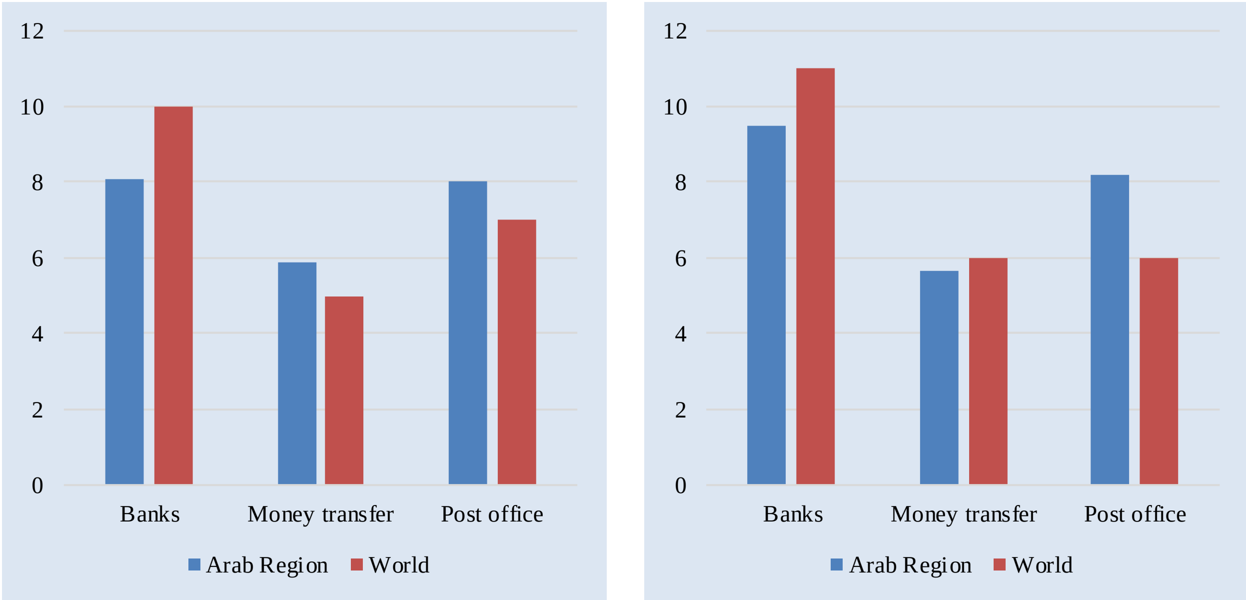
Source: ESCWA calculations based on Remittance Prices Worldwide.

10. The cost of sending $200 in remittances to the MENA region amounted to 6.2 per cent by year-end 2022. The cost of sending remittances from high-income countries of the Organisation for Economic Co-operation and Development (OECD) to the region remains in high double-digit ranges (figure 3), as opposed to the cost of sending money from GCC, countries which remains low at below 3 per cent in some corridors. In terms of service providers, banks continue to account for the highest costs associated with the transfer of remittances (figure 4).[10] According to ESCWA calculations, had remittance transfer costs been reduced to 3 per cent, the region would have gained a total of $14 billion between 2015 and 2022, representing a hefty opportunity lost in SDG financing, and a concern as these costs may drive some payments underground, with potential adverse consequences on economic growth, financial integrity and international trade. Currency conversion charges by money transfer operators can add other costs as they are even less transparent than remittance fees. Equally, greater credit risk reduces the willingness of agents to provide remittance services.

11. Reducing the cost of remittance transfers represents an important policy intervention. First, it will reduce the drain on the resources of poor migrants and their families, increasing the disposable income of poor migrants and incentives to remit. Second, it will increase flows through formal channels, especially banks. Third, it will improve financial access for the poor in developing countries. Weak competitive environment in the remittance market, lack of access to technology and supporting payment and settlement systems, and regulatory and compliance requirements tend to keep fees high.

[10] The World Bank claims that competition in the remittance market could be increased by lowering capital requirements on remittance services and opening up postal, banking and retail networks to nonexclusive partnerships with remittance agencies .

Figure 4. Comparative Cost of remittances (Percentage) by Service provider: Arab countries versus the world, 2021 and 2022



Source: ESCWA calculations based on Remittance Prices Worldwide.

IV. Changing remittance landscape and modes of transfer

12. Between 2011 and 2022, the Arab region witnessed significant declines in correspondent banking relations. The Syrian Arab Republic, for example, lost nearly 86 per cent, followed by Yemen at 62 per cent, Lebanon at 55 per cent, and Morocco at 50 per cent, with the number of correspondent banks dropping by 36 per cent on average for the entire region (figure 5). The reduction in the number of correspondent banks can be attributed to advancements in financial technology and payment systems, which have revolutionized the efficiency of transaction processing and settlement. Furthermore, banks are strategically consolidating their correspondent relationships by opting to collaborate with a smaller number of larger correspondent banks. According to IMF, multiple interrelated factors are leading to a decline in CBRs, and they generally reflect correspondent banks' assessment of the profitability and risk of relationships. In particular, decisions to terminate CBRs often relate to the correspondent bank's lack of confidence in the respondent bank's capacity to effectively manage risk.

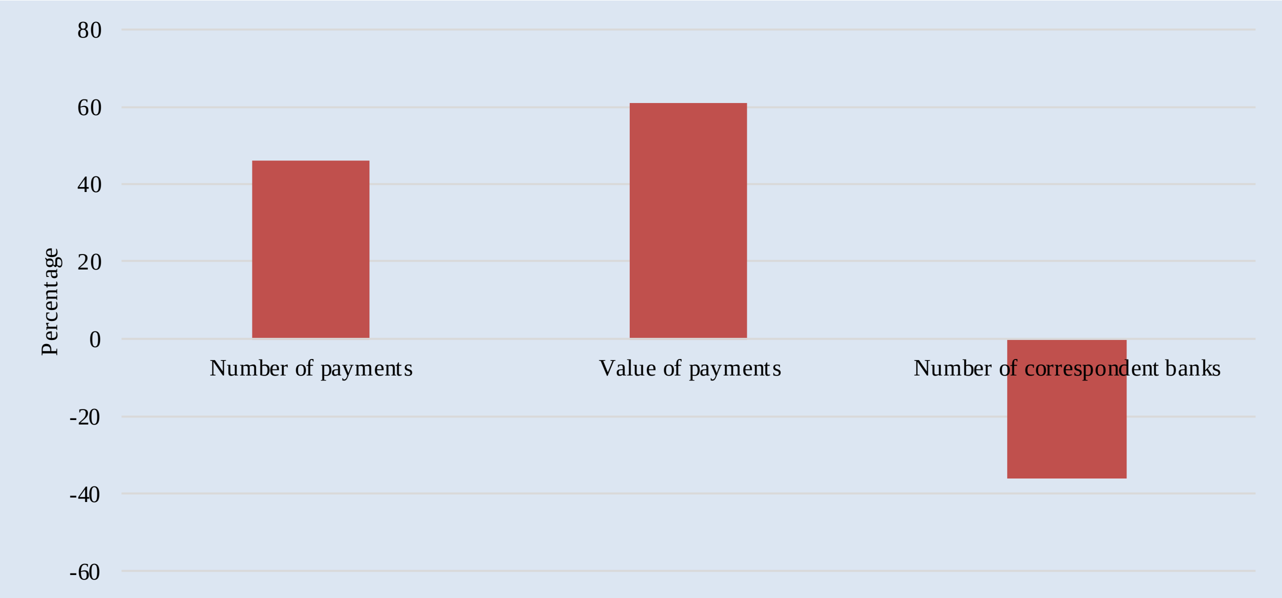
13. Recent changes in the regulatory and enforcement landscape have contributed to this phenomenon, notably regarding more rigorous prudential requirements, economic and trade sanctions, AML/CFT, and tax transparency standards. Thus far, loss of CBR arrangements has had a limited direct impact, partly because alternative arrangements have been put in place in affected countries. However, in the case of the Sudan, the country lost almost half of its CBRs between 2012 and 2015. Moreover, ongoing threats to Israeli-Palestinian correspondent banking relations could undermine the payment system, increase cash-based transactions, weaken trade, and erode the tax base. Terminating CBRs could have severe consequences given the central role of the shekel in the occupied Palestinian territories, and the economic ties with Israel via trade, employment and remittances.[11]

14. Following the outbreak of the COVID-19 pandemic, the number of international remittances via mobile money grew by 48 per cent to $16 billion in 2021 compared with 2020. However, digital channels still account for less than 1 per cent of total transaction volume, illustrating the immense potential for further digitization of remittances. Digitization could improve the affordability of remittance services, while the increase in access

[11] IMF, Recent trends in correspondent banking relationships: further considerations, 2017.

and usage between transaction accounts could foster greater financial inclusion. In low-income countries, digital financial services, driven by mobile money transactions, grew from 40 to 70 per cent of GDP between 2019 and 2021. Yet, over 40 per cent of mobile money providers do not offer any international payment/remittance services due, in part, to strict or opaque licencing requirements and vast divergences in regulatory protection between jurisdictions.

Figure 5. Percentage change in correspondent banking relationships in the Arab region, 2011–2022



Source: ESCWA based on the Committee on Payments and Market Infrastructures (CPMI) quantitative review of correspondent banking data.

15. According to the Financing for Sustainable Development Report 2023, the easing of regulatory barriers could help innovative remittance services to flourish. The rapid growth in regulatory technology reflects strong demand for technologies to manage ongoing regulatory changes, including in digital payments, crypto markets, and environmental, social and governance (ESG) standards. The shift towards innovative financial services, including those that circumvent the financial intermediation chain, such as peer-to-peer lending and decentralized finance, could help increase the efficiency, inclusivity and affordability of financial services, but they could also give rise to systemic risks.

16. Source and recipient countries should enable migrants to leverage digital remittance products, and focus on regulatory and infrastructure requisites (payment system interoperability and extension, legal, regulatory and supervisory frameworks, and cross-border data exchange and message standards). Equally, source and recipient countries should take steps to build the digital financial literacy of migrants to familiarize them with digital services, so as to disincentivize informal transfer channels to avoid digital fraud and misinformation regarding transfer costs. Recipient countries should consider establishing dedicated investment vehicles to incentivize remittances and redirect their use for productive purposes to ensure that remittances do not become a new form of rentierism. Source countries should consider waiving taxes on remittances, if any, especially in times of crisis, simplify due diligence for lower-risk accounts, allow remote account opening, review the policy framework of payment systems to enable competition and innovation, and develop emergency remittance-related savings, loans and insurance.

17. Improving the cost, speed and reliability of payments is essential to reap the benefits of international private finance. Arab Governments should consider promoting an Arab multi-currency regional cross-border payment system to process retail payments and onboard commercial banks. This approach could entail broadening participation in the platform (Buna by the Arab Monetary Fund and the GCC Arabian Gulf System

for Financial Automated Quick Payment Transfer) either by extending access to foreign entities, or by interlinking with other domestic systems or regional platforms. The second possible approach entails developing new platforms with extended reach from the outset, leveraging the latest technology and common standards while currently reviewing the 2006 Arab Declaration on International Migration in line with the Global Compact for Safe, Orderly and Regular Migration. This review should instigate the adoption of necessary mechanisms to ensure the protection of migrant workers' rights and fair treatment.

18. It is also crucial for Arab finance ministers, Arab central bankers, the Union of Arab Banks, and money transfer operators (recognized for their compliance with AML/CFT regulations) to collaborate in reducing the costs associated with remittance transfers. Furthermore, they should actively explore opportunities to leverage digital technologies for efficient, safe and timely transfer of remittances, and to direct their flows towards productive uses. To achieve this, it is imperative to develop shared banking guidelines that promote the utilization of digital assets and stimulate the growth of Arab financial markets. Furthermore, concerted efforts must be made to address the ongoing decline in correspondent banking relations.

19. The above considerations remain key given that, according to ESCWA SDG-financing simulators, should growth projections in the region materialize as forecasted by IMF, Arab middle-income countries may well witness $636 billion worth of remittance inflows by 2030, tantamount to roughly 10 per cent of the region's SDG bill.
