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Financial Access for Immigrants: The Case of Remittances

Remarks by

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I am delighted to join you here at the Federal Reserve Bank of Chicago to address this conference on financial access for immigrants.

As everyone attending this meeting knows well, immigrant communities in the United States have become increasingly visible as well as economically important. Unlike some earlier periods, during which political refugees made up a larger share of the inflow of migrants to the United States, most immigrants today come for economic reasons, driven by the hope of making better lives for themselves and their families. Immigrants today tend to be younger than in the past, and in most cases they are imbued with a strong work ethic and an entrepreneurial spirit. Indeed, although they represent about 11 percent of the U.S. population as a whole, immigrants today constitute nearly 13 percent of the labor force (Population Resource Center, 2002). Even more impressive, when we consider the limited financial resources of most immigrants, is the rate of entrepreneurship among the foreign-born; at 10 percent, this rate is nearly equal to the 11 percent rate of business ownership of people born in this country (Camarota, 2002). The positive values and attitudes of most contemporary immigrants hold the promise of upward mobility, particularly for the second and third generations, and they help to make immigration a key source of American economic dynamism.

As we discuss the barriers that immigrants must overcome to achieve full integration into American society, we should keep in mind that virtually all of us here are immigrants, even if at some remove. To speak personally for a moment: All four of my grandparents were foreign-born, coming from Europe to the United States either just before or directly after the First World War--a period, incidentally, that represented a high-water mark of immigration to the United States.[1] My grandfather Jonas, who came to the United States from Austria after a stint in the army of the Emperor Franz Josef, was probably the most entrepreneurial member of my family. He put himself through school and became a pharmacist in New York City, on the East Side. He didn't like working for someone else, however, and so he resolved that he would become the owner of the pharmacy where he was employed. The owner was interested in selling, and my grandfather had some savings, but not enough to meet the owner's price. Evidently impressed by the young man's potential, the storeowner agreed to lend my grandfather, on a handshake, the $1,000 he needed to buy the pharmacy, with the remainder to be paid back out of future profits. My grandfather, who had the restlessness characteristic of many immigrants, owned several drugstores around New York City before finally buying a store and settling in what became my hometown of Dillon, South Carolina. My father and his brother purchased that same South Carolina store from their father with the same type of owner financing that Jonas had used in New York. I understand that they even got a good interest rate.

My grandfather's method of financing the purchase of a small business, as well as his subsequent sale of the South Carolina store to his sons, illustrates the traditional importance of informal networks, especially family networks, in the financial lives of immigrants. Informal credit networks have some important advantages; for example, lenders in informal networks tend to know their borrowers well, and borrowers may feel a particularly strong obligation to repay lenders who happen to be friends or family

[1] In 1910, the foreign-born made up nearly 15 percent of the U.S. population, compared with today's figure, already noted, of about 11 percent. Thus, the challenges posed by the current influx of immigrants are hardly unique in our history.

members. But informal credit networks also have important drawbacks, such as limits on the scale of financing and on the range of financial instruments available. As the papers and discussions at this conference have emphasized, full economic integration of immigrants requires that they have access not only to the informal financial sector but also to the formal one, including banking, insurance, pension funds, and other institutions. Only by using such institutions will immigrants successfully expand their range as entrepreneurs, become homeowners, build credit histories, save for retirement, and insure against financial and other risks.

How do we provide immigrants, many of whom have little experience with financial institutions, with access to the U.S. financial system? Many approaches are possible. At the risk of anticipating some of the themes of a session to be held later today, I will talk briefly this morning about the provision of remittance services as a way to bring immigrants into the formal financial sector. This topic is especially appropriate because, as I will discuss, the Federal Reserve System has recently expanded its support for international money transfers. However, I should say that my remarks today represent my own views and not necessarily those of my colleagues in the Federal Reserve System.[2]

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Many immigrants to the United States send substantial shares of their earnings--sometimes half of their incomes or more--to family members in their home countries. The U.S. Department of Treasury estimates that remittances to developing countries

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[2] I wish to thank Sandy Braunstein and members of the Federal Reserve Board's Division of Consumer and Community Affairs for their excellent assistance in the preparation of this talk.

totaled more than $90 billion last year.[3] These remittances have a significant economic impact on the receiving countries. Remittance flows to developing countries typically exceed official development assistance, are similar in magnitude to foreign direct investment, and are more stable than either of these other flows. For example, in 2002, the Latin American and Caribbean countries received $32 billion in remittances, of which $25 billion came from immigrants to the United States. These remittances constituted about 2 percent of the gross national products (GNP) of the region in that year. In 2002, remittances from citizens working abroad accounted for nearly 30 percent of the GNP of Nicaragua, 25 percent of the GNP of Haiti, and 15 percent of the GNP of El Salvador. Mexico receives the largest absolute amount of remittances in Latin America--about $9 billion in 2002.[4] Just-released figures show that total remittances to Latin American and Caribbean countries in 2003 rose about 19 percent from the total in 2002, to $38 billion (Inter-American Dialogue Task Force on Remittances, 2004).

Who sends remittances? In its report *Billions in Motion: Latino Immigrants, Remittances, and Banking*, the Pew Hispanic Center/Multilateral Investment Fund (2002) profiled a typical remitter. Of Latinos in the United States who send remittances to their home countries, 63 percent are under the age of forty, 59 percent have not completed high school, 72 percent rent their homes, 54 percent speak little or no English, and 64 percent of those who are employed are low-skilled laborers. One would not expect this group to be financially sophisticated, and that expectation is borne out by the data: The

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[3] Testimony of Treasury Secretary John W. Snow before the Committee on Financial Services, U.S. House of Representatives, State of the International Financial System, March 25, 2004.

[4] *All in the Family: Latin America's Most Important International Flow*, Inter-American Dialogue, January 2004).

Pew Center found that 55 percent of these remitters do not have credit cards and 43 percent do not have bank accounts.

In particular, Latino immigrants, about half of whom send remittances, tend not to use banks when sending money home, employing services such as wire transfer companies instead. For example, in Los Angeles, according to the Survey of Financial Activities and Attitudes administered by the Office of the Comptroller of the Currency, 37 percent of immigrant remitters used wire transfers, compared with only 14 percent of non-immigrants who remitted. Immigrants are also much less likely to have any kind of banking relationship. In Los Angeles, only 53 percent of low- and moderate-income immigrants reported having a bank account, compared with 82 percent of low- and moderate-income non-immigrants. Concern that opening a bank account may require proof of legal residence may inhibit some immigrants from doing so (in fact, many banks now accept foreign-provided documents such as the *matricula consular*); but lack of knowledge about the services banks offer and the fees they charge is likely an important factor as well. Indeed, the Pew Center study found that, of remitters without bank accounts, fewer than 25 percent understood that sending a remittance through a bank was even possible.

Supporting the idea that information and previous experience are critical for financial access, the research of Una Osili and Anna Paulson (2003) found that the propensity of immigrants to the United States to use financial services is closely linked to their financial experience in their home countries. In particular, these researchers found that immigrants from financially underdeveloped countries, like most of those in Latin

America and the Caribbean, are significantly less likely to participate in U.S. financial markets than are native-born people of similar age, education, and income.

I do not mean to imply that using nonbanks such as money transfer companies for remittances is a poor choice in all circumstances. Nonbank providers of remittance services vary greatly in quality, and in some cases nonbanks can provide better service or greater convenience than banks can. For example, wire transfer services may allow remittances to be sent to rural areas of the home country where access to banks (which tend to be urban institutions) may be limited. Anecdotal evidence suggests that some nonbank providers are attractive to immigrants because of their "personal touch"--a Spanish-speaking agent who lives in the community, for example. Moreover, increased competition among providers has lowered the cost of sending money home through nonbanks as well as banks. According to Manuel Orozco (2003), who has done much interesting research on remittances, the typical cost of sending remittances to Latin American and Caribbean countries has fallen from 15 percent of the principal amount in the 1990s to between 5 percent and 9 percent today, depending on the receiving country.

Nevertheless, typical nonbank fees for remittances remain high on an absolute basis, and consumers who deal with the less-scrupulous providers of remittance services may bear a significant financial cost. One problem in practice is that users of remittance services often do not know precisely how much they are paying. For example, many remitters do not appear to be aware that some services exchange dollars for foreign currencies at rates less favorable to the consumer than the market-determined exchange rate.

A related concern is that regulatory oversight of nonbank remittance services remains somewhat uneven, both in the United States and in the immigrants' home countries. In the United States, federal law requires funds transfer services to register with the Treasury Department, but these laws are concerned primarily with preventing money laundering rather than with protecting consumers. The consumer protection rules that exist in the United States are set mostly at the local level. For example, twenty-eight states and the District of Columbia have regulations requiring transfer services to be licensed by the state banking agency, and some of these states have specific laws regarding foreign transmittals. California has a mandatory disclosure law that requires funds transfer services to provide each consumer with a post-transaction receipt, in English and in the language used by the wire transfer licensee, listing the fees charged, the amount presented by the customer, and the amount to be delivered to the beneficiary. In June 2003, Texas passed a similar law, under which consumers are entitled to receive, upon request, certain pre-transaction disclosures from money transmitters, including the exchange rate that applies and the amount that will be paid in the foreign currency.

Of course, these protections are effective only to the degree that consumers know their rights, such as how to file a complaint. It is interesting that one of the more effective sources of information about remitters' rights in the United States is Profeco, the Mexican consumer protection agency. Profeco provides consumers with practical advice about how to remit money to Mexico, including information on the costs of remitting, a comparison chart of the prices charged by twenty-three money order transmitters in eight U.S. cities (updated weekly), and information about where to lodge complaints, both in the United States and in Mexico (through a toll-free number).

Beyond the quality and cost of remittance services provided by nonbanks, however, another factor should be considered: By using nonbanks for making remittances, many immigrants forgo the opportunity to enjoy the wider benefits that arise from an established relationship with a bank. A money transfer company, for example, cannot provide the opportunity to open a savings account.

As you would expect, mainstream financial institutions in the United States are aware of the potential financial return to serving immigrant populations, both in facilitating remittances and in performing other types of financial services. Indeed, immigrants have become just too important economically to ignore. According to the University of Georgia's Selig Center, the Hispanic market represented some $653 billion in purchasing power in 2003, about 8 percent of the U.S. total, and the Asian market represented another $344 billion, about 4 percent of the total (Humphreys, 2003). According to the data from the Federal Reserve's 2001 Survey of Consumer Finances, more than 44 percent of all Hispanic households own their own homes, a statistic that implies a demand for mortgage loans, insurance, and other services. Reflecting this growing potential market, a 2003 survey of 340 banks by the American Banking Association found that 47 percent of these banks are either "active in multicultural marketing, or plan to market to different ethnic groups." Almost three-fourths of the banks that target various ethnic communities tailor their marketing to reach Hispanics.[5] Some of the more-successful programs involved a financial training and literacy component. For example, a community bank in Rogers, Arkansas obtained many new immigrants as customers through financial seminars offered through local operators of

[5] American Banking Association, "Banks Will Boost Marketing Budgets in 2004," news release, September 13, 2003, http://www.aba.com/Press+Room/091503bnkmark.htm.

poultry farms, the principal employers of immigrants in that community. In another example, a Chicago-based bank leveraged its relationship with small-business clients to provide financial education and services to employees who had not previously had bank accounts. As a result, numerous immigrant employees established relationships with that bank.

The provision of remittance services is a potentially effective method by which mainstream financial institutions can attract unbanked immigrants. If immigrants establish bank accounts for the purpose of sending remittances, they become far more likely to avail themselves of other services offered by the institution, including direct deposit services, savings accounts, and consumer loans. An article by the Federal Reserve Bank of Boston (Samuels, 2003) identifies several steps that financial institutions must take, beyond identifying a local population with a demand for remittance services, to establish successful remittances programs. First, institutions can realize great advantages by hiring staff members who speak the immigrants' language and are otherwise familiar with the immigrant community. Second, institutions should establish outreach and financial education programs (in the appropriate language, of course) that will help members of the targeted group learn about the financial services that the institutions provide. Of course, these two steps are useful as part of any marketing program to immigrant or ethnic groups. Third, and importantly, the institution must offer sufficiently competitive prices for remittance services to overcome what reluctance remains.

Controlling the cost of international money transfers can be achieved in a number of ways. One strategy is to employ an existing money transfer network, such as SWIFT.[6] Establishing a partnership with a financial institution in the home country of the group to be served is a second viable approach. For example, the Federal Reserve Bank of Boston article referred to earlier (Samuels, 2003) provides an interesting case study of how Citizens Bank, a regional bank operating in the Northeast, created a remittances program for an immigrant population from the small African country of Cape Verde by forming partnerships with two banks from that country. A number of banks have pursued a third strategy--entering the remittances market through partnerships with existing money transfer organizations. Although this strategy has some potential for abuse if mismanaged by the bank, the combination of the transfer service's transmission infrastructure and the bank's marketing services and branch network is likely to reduce costs, making lower charges to the consumer feasible (Orozco, 2003).

Yet another increasingly popular approach for banks is to build remittance services on the existing networks of automatic teller machines (ATMs). Orozco (2003) notes that Bank of America and Citibank have recently adopted this model. Bank of America's SafeSend program and Citibank's Money Card program issue debit cards to a person in Mexico designated by the U.S. remitter, allowing the recipient to gain access to funds transmitted from any ATM. Remitters are typically charged a flat fee for the transfer, for example, Bank of America charges $10 per transfer. Second Federal Savings in Chicago offers account holders an "amigo card," a second ATM card that can be sent to a family member in Mexico. One of the downsides of the ATM-based approach is the

[6] The acronym stands for Society for Worldwide Interbank Financial Telecommunication.

lack of access to these machines in rural areas. Most banks offering ATM-based services therefore also offer more traditional funds transfer services as well (Bair, 2003).

Banks still have only a small market share in remittance services, but that share seems poised to grow rapidly. Orozco (2003) notes that Wells Fargo initiated a remittances program in 1996 and released it current product, Intercuenta Express, in 2001; under this program, amounts less than $500 can be sent to Mexico for a flat fee of $10. In the first three years of its program, Wells made nearly half a million money transfers to Mexico, representing at least $100 million in revenue per year.

Credit unions, particularly those serving predominantly Latino constituencies, have been proactive in attracting customers through their remittance services. The World Council of Credit Unions began a remittances project in 1997 and introduced its IRNet service in July 2000. In partnership with other institutions (including Travelex, a major retail provider of foreign exchange), IRNet now provides remittance services to more than forty countries. At last report, nearly two hundred credit unions in thirty-seven states offer this service (Herrera, 2003).

The Federal Reserve is attempting to support banks' efforts to better serve immigrant populations, with remittances and other money transfers being a key area of interest. Since the late 1990s, the regional Federal Reserve Banks and the National Automated Clearinghouse Association (NACHA) have been working to improve cross-border payments services through enhancements of the Automated Clearinghouse system (ACH). For instance, in 2001, the Reserve Banks introduced international ACH services for payments from the United States to Canada, and in 2003 they added service to Switzerland and the United Kingdom. The extensions of service to the latter two countries are the first steps in the development of the Reserve Banks' Transatlantic Service, which will be further enhanced to include service to Austria, Germany, and the Netherlands later this year. More important for remittances, in February 2004 the Reserve Banks expanded their international ACH services to Mexico, in cooperation with the Central Bank of Mexico. The service potentially connects any bank account holder in the United States with any bank account holder in Mexico, uses an exchange rate guaranteed to be within 1 percent of the Central Bank of Mexico's wholesale rate, and costs the banks less than $1 per transaction. Providing service to Mexico is also an important step for the U.S.-Mexican Partnership for Prosperity, an agreement designed to improve financial linkages between the two countries. These Federal Reserve initiatives will support U.S. banks' ability to serve immigrants by allowing remittances to be sent to foreign banks at low cost. Ongoing improvements in the infrastructure for sending remittances, collaborations among foreign governments, and increased competition among service providers should ensure that cost savings are passed on to consumers.

Although the opening of ACH service to Mexico is an important step, broader international coverage is needed to serve the diverse immigrant population. To help meet that need, the Federal Reserve Banks will be hosting a conference in Atlanta this October to explore how best to establish compatible electronic payments systems throughout the rest of Latin America. The conference will bring together financial-sector leaders and payments systems experts to discuss ways to facilitate cross-border electronic payments throughout the hemisphere. This initiative supports a commitment made at the recent Special Summit of the Americas in Monterrey, Mexico, to reduce the cost of international remittances by at least half by 2008.

To conclude, I have highlighted how the sending of remittances is the most important type of financial transaction for many immigrants and their families. This fact engenders both a challenge and an opportunity. The challenge, for regulators, researchers, and immigrant advocates, is to ensure that remitters can send funds to their home countries conveniently, safely, and at a reasonable cost. The opportunity, primarily for banks and other mainstream financial institutions, is to find ways to leverage immigrants' need for remittance services into a broader relationship, one that will both be profitable for the bank and will also provide immigrants and their families with greater financial access.

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