Remittance and Remittance Service Providers in Ethiopia

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Abstract

Remittance is an extremely important source of foreign exchange for Ethiopia, perhaps larger than the export earning of the country in its foreign exchange generation capacity. However, the industry is besieged by a number of problems. In this study we have administered structured questioners to six private banks operating in the industry; the only two public banks engaged in the remittance business, the only cooperative bank engaged in the business; and two remittances business firms which are currently in operation in the country and one informal sector operator. The result of our analysis shows that the volume of remittance in Ethiopia could be between US $ 2 to 4 billion per year (an average of about US$ 3 billion). This is about the size of Ethiopia's total export and development aid combined. We found that the formal procedure of getting a license and operating in the sector is not a major problem, at least on paper. However, implementation is problematic for most banks, especially to work with the private sector operators. For informal sector operators the major problems is general policy environment and lack of deepening in the financial sector liberalization. Finally it is worth emphasizing the importance of the remittance industry (which is at least twice that of the Ethiopian export sector) on the one hand and the lack of commensurable policy emphasis by the government to sector on the other, which is in a stark contrast with the incentive the government gives to the export sector. Thus, it is imperative that the government needs to design attractive incentive systems and offer an enable environment by addressing problems outlined in detail in this study to benefit from the remittance industry

Key Word: Remittance, Ethiopia, capital flows.

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1. Background

Various writers hold different views regarding the concept of remittances. Migration Policy Institute (2003), Adams and Page (2003) and Harrison (2003) treat remittances as transactions that are initiated by individuals living or working outside their country of birth or origin and related to their migration. The components of remittances are compensation of employees, workers' remittances and migrant transfers. IMF's Balance of Payments Manual (1993) defines these components as:

- *Compensation of employees* comprises wages, salaries, and other benefits earned by individuals—in economies other than those in which they are residents—for work performed for and paid for by residents of those economies.
- *Workers' remittances* cover current transfers by migrants who are employed in new economies and considered residents there. A migrant is a person who comes to an economy and stays there, or is expected to stay, for a year or more.
- *Migrants' transfers* are contra-entries to the flow of goods and changes in financial items that arise from the migration of individuals from one economy to another.

If migrants live in the host country for a year or longer, they are considered residents, regardless of their immigration status. If, however, the duration of stay is less than one year, their entire income in the host country shall be classified as compensation of employees (*Ibid*).

Despite this clear classification of remittances, official remittances data and their compilation thereof are problematic. De Luna Martinez (2005) indicates that a survey of several central banks revealed the presence of widespread problems in remittance data collection. Most central banks use remittance data reported by commercial banks, but leave out flows through money transfer operators and informal channels. The methodology for making estimates of informal transfers is also not uniform across countries. World Bank (2008) points that even with the readily available data a clear delineation in accordance with IMF's guidelines, noted above, is lacking. Distinction between the various categories appears to be purely arbitrary, depending on country preference, convenience, and tax laws or data availability.

Remittances mobilized through informal sectors and remain unrecorded are significant in developing countries. World Bank (2006) estimates this figure at around half of the officially registered remittance flows through formal channels. This seems to be quite underestimation in Ethiopia as we try to argue below. Various studies ascribe the choice of informal channels over formal channels for different factors. According to Russell (1992) individuals' choice between formal and informal channels for sending money back home depends on the socio-economic characteristics of their household members, level and type of economic activity in the hosting countries, exchange rate and sending charge differentials and relative efficiency of the formal sector relative to the informal sector. Ratha (2003) emphasizes the role of transaction costs in this regard. The latter seems a reasonable hypothesis in the case of Ethiopia.

The size of remittance that flows into a country depends, among other factors, on the size of emigrant population (World Bank, 2008), facilities for facilitating funds (Puri and Ritzema, 2004; Ratha, 2003), the level of economic activity in the host country (Swamy, 1981), and the inflation rate in the recipient country (El-Sakka and Mcnabb, 1999). The views on the role of domestic inflation have been mixed. El-Sakka and Mcnabb (1999) hold that inflation has a positive relationship with the size of remittance inflow as migrants raise the amount they send in response to inflation in the home country to maintain the consumption of families back home. Elbadawi and Rocha (1992), on the other hand, argue that high rate of inflation is a sign of economic instability and, thus, may discourage remittances. In Ethiopia the former arguments seems to work for remittances destined for consumption while the latter view may relate to the investment related flows.

1.1. Recorded Remittances, Overall Volumes and Trends

A noticeable degree of out-migration in Ethiopia started in the 1970s following the revolution and the political unrests afterward. During the early days, migration was limited to the urban elite, especially the young and the educated, who for political reasons sought refuge in Western countries. Gradually, however, migration has become an aspiration of most urban people, mainly for economic reasons. After the mid 1980s, even rural peasants began flocking to the Middle East and the Gulf region in search of jobs and better pay. Currently, over one million Ethiopians are believed to reside abroad (Aredo, 2005).

Various authors note that despite its large migrant population, Ethiopia has not fully tapped its potential. Berhanu et al (2004) cited in Aredo (2005) indicate that the current flow of remittance to Ethiopia is only one-sixth of its potential. It covers just 8 % of budget deficit. They indicate that if the potential level was to be materialized, it would generate a level that is higher than the current level of ODA.

As noted above, data on remittance flows is highly problematic. The same problem is observed in Ethiopian remittance time series data. Various data sources give different figures for the same year. According to World Bank (2008) remittance has averaged 1.3 % of GDP over the last 30 years. Between 1977 and 2003 remittance flows have steadily grown from 4 million USD to 47 million USD per year. Afterwards, however, the growth has been sharp reaching 172 million USD in the year 2007. In 2004, the largest remittance sending countries to Ethiopia were United States, Israel and Germany with 46 million USD, 25 million USD and 10 million USD respectively (IMF, 2005).

Using MoFED (2007) data, which is based on the National Bank of Ethiopia (NBE) data, reveals the same trend in the remittance flows. There has been sharp increase in flows after 2003. There is, however, a marked difference between the World Bank figures and MoFED figures. According to MoFED, remittance flows averaged 307 million USD per year between 1997 and 2006, while the same figure according to World Bank is just 70 million USD. According to MoFED (and the National Bank), in

2007, the figure surpassed the 1 billion USD mark for the first time (see Table 1a below). In Table 1a the first column which reads as 'individual transfer' is this officially recorded figure by the National Bank. It is different from 'Private transfer' because it excludes transfer by NGOs. The latter share is becoming increasingly less important, however, as the last column of Table 1a shows.

In Ethiopia formal channels for money transfers are commercial banks and money transfer operators, Western Union, Money Gram and Dahabshiil being the most important ones. Such figures are officially recorded both by the National Bank of Ethiopia and MoFED. The latter in fact used the information from the National Bank. Because official figures are better (relatively accurately recorded by the proper government agencies) and due to details in the data, hereafter the MoFED or National Bank data (which is the same) is used.

According to this official data, the level of annual remittance flow has increased by over 8 fold in 2006 compared to its level in 1997. This growth derives mainly from sharp increase in cash transfers while transfers in kind have remained stable over the period (MoFED, 2007). One of the reasons for this fast increase is the narrowing of the spread between official and parallel market exchange rates (NBE, 2006/07). MoFED estimates that the unofficial remittance flows to Ethiopia have reached over 402 million USD in 2006 jumping fast from its 2001 level of 81 million USD. A rough estimate based on international transfer operators would indicate a significantly higher figure. AMAP (2004) estimates that migrants send between 100 and 200 USD monthly to their relatives back home. Applying the average of this estimate to the estimated one million Ethiopian migrants makes up around 1.8 billion USD in informal transfers (a figure which is close to our estimation below)[1].

[1] We are grateful to Getachewu of the National Bank (Now at Ethiopian Economic Association) for providing us with data used here and excellent ideas that he was grappling with to estimate the size of remittance in the course of this estimation.

Tabulate: Table 1a: Estimate of the Size of the Remittance Industry in Ethiopia

	Individual Transfer	Informal (Method 1)*	Informal (Method 2)	Total Remittance (Method 1)	Total Remittance (Method 2)	Exports	Total Remittance /Export Ratio (Method 2)	Individual transferee as % of Private Transfer
1997/1998	133.7	361.5		495.3		1034.4		42.8
1998/1999	87.8	237.3		325.0		917.1		31.7
1999/2000	117.8	318.4		436.1		985.0		30.9
2000/2001	111.5	301.4		412.8		958.2		29.4
2001/2002	102.5	277.1		379.5		939.7		29.4
2002/2003	164.5	444.8	235.6	609.3	400.1	1139.6	0.40	33.2
2003/2004	233.4	631.2	349.8	864.6	583.2	1347.1	0.40	34.8
2004/2005	370.8	1002.5	949.9	1373.3	1320.7	847.2	1.60	45.7
2005/2006	736.7	1991.8	998.8	2728.5	1735.5	1003.0	1.70	60.0
2006/2007	1173.3	3172.3	1515.8	4345.6	2689.1	1185.1	2.30	69.2

*The Informal estimation is ours. Method 1 is based on Page & Plaza (2006) who estimate that unrecorded remittances are 73 % of total remittances in Sub-Saharan Africa (Compared to 45-60 % in LAC, EAP and ECA). Method 2 is our estimation using data of Customs Authority and National Bank as detailed out in Table 1b below

Table 1b: Estimation of Informal Remittances

Particulars/Time	2000/01	2001/2002	2002/03	2003/04	2004/05	2005/06	2006/07
Total imports (Customs valuation)	1556.8	1695.7	1856.4	2586.9	3633.2	4592.7	5126.2
Food aid imports	22.6	136.6	176.9	134.8	100.1	65.7	65.7*
Aircraft	12.6	11.4	17.3	126.1	138.8	67.5	67.5*
Franco Valuta imports	7.4	9.1	23.9	22.4	20	16.7	16.7*
Imports Excluding food aid, franco valuta and aircraft	1514.2	1538.6	1638.3	2303.6	3374.3	4442.8	4976.3
Imports for which Letter of Credit (LC) is opened	1108	1053	1294	1805	2324.3	3225.8	3225.8*
Recorded Imports less LC opened	406.2	485.6	344.3	498.6	1050	1217	1750.5
Net FDI (NBE, data)	100	149	123	150	150	365	482
Cash FDI (NBE data)	n.a	n.a	14.3	1.2	49.7	146.8	247.3
Imports by Foreign Direct Investors (Net FDI less Cash FDI)	n.a	n.a	108.7	148.8	100.3	218.2	234.7
Imports financed by the Informal transfer (Remittance)	n.a	n.a	235.6	349.8	949.7	998.8	1515.8

Computation based on the data of the National Bank of Ethiopia, Ethiopia; Customs Authority and Ethiopia's Disaster Preparedness and Prevention Authority for food aid data.
*No data is available hence previous years amount is assume to prevail in 2006/07

The estimates of informal transfers though may be inaccurate, point to the size of foreign exchange the formal sector is missing on and calls for immediate policy interventions that facilities for the operators to channel them to the formal sector. In fact when one looks the incentive package for the export sector, which generates less than half what the remittance industry generates each year, such a policy focus by the government is long overdue.

1.2. Internal Migration and Remittances

Ethiopia experiences one of the highest levels of internal migration and population redistribution in Africa (RESAL, 1999). Ethiopia's internal migration is largely an individual or family response to adverse socioeconomic, physical and political environment as well as direct government policy. In this context, the character, direction and volume of migration in Ethiopia in the last three decades have been shaped by political instability, decline or stagnation in the growth of the agricultural sector and government resettlement programs of the 1980s, whose official objective was to tackle famine and attain food security (Gebre, 2001; Ezra, 2001) cited in Mberu (2006). Another important factor in Ethiopian internal migration was the ethnic federalism of the 1990s, which may have engendered stress migration (Mberu, 2006).

An important aspect of Ethiopian internal migration is its association with urbanization. The level of urbanization in Ethiopia, even by African standards, is very low. During the post-revolutionary period urban centers became increasingly attractive destinations as a result of opening of branch offices of mass organizations, and government and non-governmental agencies (Golini *et al*, 2001). There are, however, studies that suggest rural-rural migration is as considerable as that of rural-urban migration. A study of the what is called Amhara region found that rural-rural migration was more common than rural-urban migration. But the migration had generational pattern, with the young preferring to go to urban areas (Devereux, 2000).

The Ethiopian internal migration is dominated by female flows. About 55 % of those who move are women and these form about 57 % of those who leave from rural areas. However, women are less involved than men in urban-rural flows forming only 44 % of such flows. What are called Oromiya, Amhara and Southern Nations-Nationalities Peoples' Region (SNNPR) are the most dominant one in terms of attracting migrants. The city regions of Addis Ababa, Dire Dawa and Harari receive inflows predominantly to their urban centers than their rural sections (Golini et al, 2001).

The 1999 Labor Force Survey identifies over 2.3 million people who stated that they lived at their current place of residence for no more than five years, which it refers to as recent migrants. The survey shows a result consistent with Devereux (2000) with rural-rural migration being the dominant pattern of internal migration. A rural-rural flow of close to a million (36.8%) and a rural-urban flow of half a million people (22.9%) are reported. There is also significant flow of people from one urban centre to another to a rural area. Urban-urban migration amounted to over half a million people (24.2%) and urban-rural migration stood at around 370,000 (16.1%). It might be sensible to hypothesize that this interwoven migration might be accompanied by a web of internal remittances. However, we lack information about this important aspect of the remittance story in the country.

1.3. Financial Sector Development in Ethiopia

Level of Development

The Ethiopian financial sector is one of the least developed (if not the least developed) in Sub-Saharan Africa (Kiyota et al, 2007). It is characterized by shallowness and closed nature as well as strong government control. There is no capital market in operation, denying the business sector of formal investments in private and public sector equities. Financial infrastructures in rural areas are poor. This is manifested in the low domestic saving rate (around 4 %). The financial assets on offer are also limited.

To improve the financial sector, the government embarked on a series of reforms as one of the important components of the economic reform program under Structural Adjustment Program (SAP) since 1992. These reforms were aimed at deregulating the financial sector with the view to improve mobilization of domestic resources for investment, improving the efficiency of financial intermediation through greater reliance on market forces in resource allocation and creation of conditions for use of market oriented instruments in the implementation of monetary policies (Alemu, 2001).

The salient features of the Ethiopian financial reform strategy are: gradualism, gradual liberalization of the sector to private banks and insurance companies and of the foreign exchange market; strengthening domestic competitive capacity before full liberalization, restricting the sector only to domestic investors, strengthening NBE's regulatory and supervision capacity, giving the banks autonomy and opening up the inter-bank money market (Alemayehu, 2008).

The financial reforms carried out since 1992, have led to flourishing of domestic private sector participation in the sector. The post-reform period saw decline in the dominance of state owned banks and the rise in the share of private banks. In 1998, the three state owned banks (Commercial Bank of Ethiopia (CBE), Development Bank of Ethiopia (DBE) and Construction and Business Bank (CBB)) accounted for 93.6 % of the assets of Ethiopian banks. This figure however has fallen to 69.6 % in 2006, while the share of private banks increased to 30.4 % from 6.4 % in 1998. Over the same period, the total asset of the banking sector has doubled (Kiyota et al, 2007). This indicates the fast growth in the Ethiopian financial sector and even more so the private sector. Alemayehu (2008) also notes that the role of the private sector has grown in Ethiopian financial sector. The largest commercial bank to date, for example, accounted for 90 % of the deposits mobilized, but this figure had fallen to 75 % in 2002/03, while that of private banks reached 20 % from 4 % in 1996/97. At the moment there are 9 private banks and 9 insurance companies operating in the country with 2 more banks in the pipe line to launch operation. In addition to the growth of the role of the private sector, another notable development in Ethiopian financial sector are the launch of Ethiopian Commodity Exchange (ECX) in April 2008 and the establishment and operation of foreign currency account for non-resident Ethiopians and non-residents of Ethiopians origin .

Despite the reforms, however, the Ethiopian financial market remains the most highly controlled in all Sub-Saharan Africa. Financial liberalization index, which measures banking security and independence from government control, on a scale of 10 to 100 (100 being the most liberal), is only 20 for Ethiopia (Kiyota et al, 2007). There has been no significant change (improvement) in the financial assets operational. Although one could be sympathetic to the government's policy of gradualism in liberalization at the initial stage, this policy has been there for the last two decades with no fundamental change. This underscores the need to set out a time frame for this policy of 'gradualism'.

Payment and Settlement Systems

The type of payment and settlement systems is the one of the important elements that contributes to the development of financial markets, instruments and transactions. In Ethiopia Payments and settlement systems are underdeveloped. One may classify the payment and settlement systems in Ethiopia into traditional and modern (or electronic) systems. The traditional payment system includes cash, checking transfers and letter of credit (LC) while electronic payment system includes SWIFT, Western Union money transfers and card based transfers (Tadesse and Kidan, 2005).

SWIFT (Society for Worldwide Inter-bank Financial Telecommunication), on the other hand is the most popular means of transferring money with banks. According to the National Bank of Ethiopia, at the moment, most Ethiopian banks use SWIFT to settle international payments. SWIFT is a cooperative society based instrument that facilitates exchange of financial messages at international levels for fast and effective money transfers. It is a secure method of telecommunication and is extremely cost effective. In this system, banks are identified through two important secret codes called Bank Identifier Code (BIC) and International Bank Account Numbers (IBAN). The former represents the bank's address and distinguishes the financial institutions in question while the latter is a code that uniquely connects the bank with the respective account. These guarantee secure communication and reliable services. The SWIFT facilitates central bank's monitoring systems, settlements and clearing systems as well as in cross-border and cross-currency settlement systems. Remittance service providers are all expected to clearly advertise the BIC and IBANs on their websites, Brochures and Ethiopian embassies and consulates abroad (NBE, 2006).

Card based payments systems are registering fast growth in recent years in Ethiopia. Two of the commercial banks in the country (Dashen Bank, CBE) have introduced a wider use of debit cards and ATM cards to great effect. The use of such system has been there before with other non-financial institutions such as Ethiopian Airlines, however.

2. Characteristics of the Remittance Industry

2.1. Number of Firms, Type of Firms and Coverage

The Ethiopian remittance services sector is characterized by co-existence of government and private operators as well as a significant informal sector. Unlike other African countries such as Kenya or Ghana, the number of formal remittance service providers is extremely limited in Ethiopia. There is also lack of information about the number of informal operators. There are two public banks, six private banks, one cooperative bank and about four private remittance service providers officially operating in the country. In this study we have surveyed all the banks (three of them ailing to respond), the cooperative bank, two private sector operators and one informal sector operator. Thus, the analysis below is based on the information from this survey. Table 2 shows the number and name of firms engage in remittance service provision in Ethiopia and used for this study.

Table 2 Number and Name of Remittance Service Providers in Ethiopia

No	Name of Remittance Service Provider	Surveyed for this study
1	Commercial Bank of Ethiopia	Yes
2	Construction and Business Bank	Yes
3	Bank of Abyssinia S.C.	Yes
4	United Bank	Yes
5	Wegagen Bank S.C.	Yes
6	Awash International Bank S.C.	Couldn't respond
7	Dashen Bank S.C.	Couldn't respond
8	NIB Iinternational Bank S.C.	Couldn't respond
9	Cooperative Bank of Oromia S.C	Yes
10	Dahabshiil	Yes
11	Amal Express Money Transfer	Yes
12	KAAH Express	Couldn't respond(not found)
13	Mustaqubal Transfer Service	Couldn't respond (not found)

Two of the operators (20% of the operators surveyed) are state owned banks and the rest (80%) are privately owned (formal and one informal). Among the firms providing remittance services in Ethiopia and included in this survey, only 30% are specialized in money transfers (Amal Express, Dahabshiil and one informal sector operator), while others specialize in various activities: 20% of the firms operate as exchange bureaus, 40% are private commercial banks one of the surveyed firms is an informal sector operators; and one of them, the construction and business bank, is a savings and loan institutions.

The survey indicated the lack of diversification in the operation of the different service providers in the country. Important players in the service sector, who have the infrastructure to provide remittance services such as postal service providers, telecommunication services providers, credit unions and microfinance institutions still having not moved into the area,.

Remittance operators can potentially be involved in a number of functions in the chain of remittance transfers. In Ethiopian case, however, firms tend to focus on just one or a few at most functions in the chain. This can, partly, be explained by the lack of capacity (infrastructure, legal as well as financial) to handle the various functions. As would be expected of an underdeveloped financial system, the remittance services providers are concentrated around the task of receiving and sending international and domestic remittances, respectively. Only 40% of the firms in the survey, however, send as well as receive both domestic and international remittances, with the rest limited to a receiving task. All in all, while most of the firms receive remittances (50% reporting as receiving domestic remittances) only 40% are engaged in sending international remittances and domestic remittance. Not many firms offer settlement services, though. 20% of the firms are engaged in cross-border settlement services and another 20% operate domestic settlement services. Surprisingly, however, only 20% (two firms) are reported to exchange currencies for remittance service users (CBE and Cooperative Bank of Oromiya).

The size of the network of the remittance operators in Ethiopia partly reflects the ease with which people can transfer remittances overseas as well as across the country. The larger the network of the remittance service operators, the relatively easier remittance transfers and hence the higher the gain to the country provided its large migrant population do send money. In their international operations, the firms vary in their network coverage. The majority of firms operate in numerous remittance corridors. 50% of the firms have more than 10 remittance corridors. 10% of the firms reported to have 5 to 10 remittance corridors and another 10% of them have 2 to 5 remittance corridors while 20 % of them have 1 major remittance corridor[2].

2.2. Size of the Remittance Market

[2] There is problem of non-response. Especially, the data from the informal operators is incomplete. Moreover, the way the alternatives are designed is vague. What does 1 major remittance corridor mean? A firm with more than 10 corridors may have one major corridor. The response of such firm may not be clear.

2.3. Business Models

Due to the in Ethiopian financial sector regulation that prohibits the involvement of foreign firms in the sector, there are no firms that operate as the franchises of large foreign firms or are branches or subsidiaries of large foreign companies. There is no domestic firm that operates in other countries either (except that the CBE has branch offices in Djibuti). The survey indicates that 50 % of the firms giving remittance services in Ethiopia are independent firms[3]. In their remittance services, most of the firms (70%) engage with domestic and/or foreign partners. 40 % of the firms have domestic partners while 60 % have international partners such as Western Union and Money Grham. Western Union, for instance, being an international money transfer operator, it is required to work with domestic banks to offer remittances service in Ethiopia. Accordingly, it is working with three banks in Ethiopia: Commercial Bank of Ethiopia (CBE), Construction and Business and Bank (CBB) and Dashen Bank. The most common type of institutions in terms of their partnership with domestic remittance services operators are money transfer operators with 80 % of the operators using them; followed by banks, which 60 % of the firms use.[4] Among these, 30 % have both domestic and international partners. It appears that only a small proportion of the remittance operators (30 %) have their operations limited within the country[5].

The terms of partnership vary among the firms surveyed in this study. The firms operate on one or a set of the return package that includes commission on remittances, access to foreign exchange and access to payments infrastructure. For the majority of the firms the term of partnership with their partners is commission on remittances payments/receipts. 70 % of the firms fall in this category while 40 % of them noted that commission on remittances as well as access to foreign exchange is the term of agreement with their partners. Only 10 % of the firms have varied terms with their partners with commission on remittances, access to foreign

[3] The other 50% must therefore be associated with another organization (international or domestic) for their operation; however two firms haven't got any association in their response.

[4] There is confusion with the responses to the yes/no questions. The answers under the 'yes' column usually don't match those under the 'no' column.

[5] Thus, the other 70 % have some operation outside the country but none has reported that they operate outside the country in earlier questions.

exchange and access to payments infrastructure all being used.[6] From among the firms engaged in partnership with other operators in their remittance services the contractual agreement of only 30% of the firms is, however, exclusive. The rest (70 %) are not contractually bound to work only with the specific firms they are currently working with. The exclusive agency agreements are in stark contrast to NBE's requirement that remittance service providers should arrange non-exclusive conditions when making agency agreements between them (NBE directive no FXD/30/2006).

2.4. Remittance Products

The firms use various instruments for transferring remittances. Some use many instruments while others offer their services using only one instrument. The most popular channel among the firms (including the informal one) is account-to-account transfer, which 60% of the firms used. Money order is the least popular with just 10% of the operators using it. The Construction and Business Bank (C&BB) is the most diversified service provider in terms of the instruments it uses. Four firms use electronic cash transfers (Amal Express Money Transfer, Dahabshiil, Bank of Abyssinia and Cooperative Bank of Oromiya). Four firms use bank drafts (CBE, Wegagen Bank, C&BB and United Bank). C&BB and United bank also accept checks in transferring remittances. CBE and Wegagen bank also offer swift wire transfer service. None of the firms, nevertheless, uses pre-paid cards transfers in their remittance operations. There is, nevertheless, no use whatsoever of emerging instruments such as mobile money transfers, partly related to the snail pace at which the national telecom monopoly operates in the country.

Among the firms surveyed, CBE, Wegagen Bank and C&BB offer relatively more financial services geared towards the senders/recipients. The most common financial services provided by the surveyed firms are deposits. 40 % of the firms provide deposit services. 30 % of the firms provide one or more kinds of credits (be it

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[6] Dahabshiil reported that it doesn't work with partners, yet it has also indicated in question 10 that the term (financial) of its relationship is commission on remittances payments/receipts. The data on %ages is not complete either. Only two firms have reported here. If we had the data on all firms it would give more sense using it.

customer loans, small business loans, large business loans or mortgages). C&BB is found to be the most specialized in this function. None of the firms surveyed, however, provides senders/recipients with insurance products, educational loans, and credit cards.

Like in any business, remittance service providers/operators may fail to deliver remittances to their intended final recipients. There is a need for a department or a section to handle issues related to consumer dissatisfaction that may result from such events. 90 % of the firms have a system to deal with consumer grievances. In case of failure of delivery of remittances as promised, the option open to the customers varies across the operators. According to 80 % of the firms customers need to contact the sending agent in the wake of such events while 20 % of the firms have a system in which the customer may contact both the sending and the receiving agents.

The frequency of occurrence of such failures markedly varies from none to once every day among the operators. With the majority of the operators, consumer grievances due to failure of delivery are quite common stressing the need for a dedicated system to handle those. 50% of the firms indicated that consumer grievances occur once a week and 10% of the firms noted that it occurs once in two or three months while 10% indicated that they receive one grievance everyday on average. 10% of the firms hold that customer grievances are rare and only occur once every six months and another 10% are yet to receive grievances on failure of delivery of remittances.

There is also difference in the speed with which different operators address the problems once grievances are received. The fastest is one day and the slowest is up to one month. 20% of the firms address the grievances within just one day, 40% take one week and 10% of them take up to one month to address the problems[7]. It appears that there is lack of personnel to handle customer grievances, which reflects

[7] Here the slowest in addressing the problem is CBE. But the duration of addressing the problem is not clear. At one point it is noted that it would take 2-3 months and then there is a one month note. We took the later as the former is a bit too much compared to the other operators.

the relatively low level of competition in the sector. 30% of the firms reported that they have only just one staff to handle complaints. 10% have two staff member and 20% have three staff members. 10% of the firms indicated that the size of the staff to handle such complaint depends on the size of the customer grievances. But 10% of the firms have no such staff at all.

Another problem that the remittance operators in Ethiopia face is that some recipients may fail to turn up to fetch their remittances. The extent to which this problem occurs varies among the firms. It appears that this problem is more common, with 50% of the remittance operators stating that they experience them over 10 times per month. 10% of the firms indicated that the problems occur twice or thrice a month, while another 10% reported to have encountered the problem four to ten times a month.

2.5. Access to Financial Services

Like the financial sector at large, the remittance operators in Ethiopia offer limited financial and non-financial services to their customers. Among the firms surveyed, CBE, Wegagen Bank and C&BB offer better financial services geared towards the senders/recipients. The most common financial services provided by the surveyed firms are deposits. 40 % of the firms surveyed provide deposit services. The informal sector operator, however, do not provide those services. 30 % of the firms provide one or more kinds of credits (be it customer loans, small business loans, large business loans or mortgages). The C&BB is the most specialized in this function. To date, however, there are no remittance operators that provide senders/recipients with insurance products, educational loans, credit cards. There is, however, no notable level of use of revenues from such financial products to subsidize provision of remittance services.

In addition to the underdevelopment of the Ethiopian financial sector, there appears to be lack of financial knowhow among the public. This requires concerted effects to improve the public's knowhow by the government as well as operators in the financial market. The survey, however, revealed at the delivery of remittance services only one firm said it offers literacy materials to its customers.

3. Regulatory and Business Environment

3.1. Entry barriers to starting a remittance service business

One of the notable features of business operation in developing countries, especially Africa, is the high cost of doing it. Both start up and running costs are considerably higher than other regions of the world.

Starting operation in the remittance service business in Ethiopia one needs to be registered with the country's central bank, National Bank of Ethiopia (NBE). For obtaining the license interested parties need to pay some fee. The major institutions eligible to provide international remittance service in Ethiopia include: international money transfers operators in association with banks, which are licensed entities to provide money-transferring services internationally such as Western Union, Money Gram, Maniflo, and Adam Funds etc; commercial banks, which are licensed business organizations to provide financial intermediation; non-financial organizations that are allowed to engage in remittance services through their branches overseas, Ethiopian Airlines and Ethiopian Shipping Lines (NBE directive,2008).

In accordance with NBE's regulation, depending on the nature of the firms and their network some needed partnership with intermediaries for their remittance operations and others don't. 40% percent of the firms noted the need for intermediaries while another 40% said that they don't need to have a partner[8]. The partners in question could be domestic or international. International money transfer operators and companies are required to work with domestic partners, while domestic operators may need to work with foreign partners as in most cases they lack the capacity to work overseas. Non-bank operators are required to operate with banks. Some are allowed to operate having their own branch offices while others are required to host their operations within the bank branches.

[8] The response from CBE, however, is both yes and no.

It is curious to note that almost all the private operators that we managed to trace and not are working with Wegan Bank and most of them are operated by Ethiopians of ethnic somail origin[9]. Some of our informants revealed that other banks, except Wegagan, couldn't practically able to work with private operators (although legally they can) as that of Wgagan. Moreover, none-ethnic Somali Ethiopians are also practically unable to get license to operate (although legally they can). Given that Wegan bank is strongly associate with governing party (which borders ownership), one notes some irregularities here which might be motivated by the government (the ruling party) to control flow of foreign exchange to the country.

NBE, which is the regulatory authority of the Ethiopian financial sector, obliges remittance service providers to: reveal the terms and tariffs applicable to remittance service including their correspondent bank, agent fees and other different types of services they provide; indicate the estimated time that it will take the money to reach the receiver; the exchange rate that the remittance service providers use to convert the foreign currency to domestic currency and vice versa; and facilitate remittance transfer service to their customers within 24 hours.

In general, the perception of the remittance operators about the effect of the laws and regulations that govern the operation on doing business in Ethiopia appears to be evenly divided between those that felt it is a major problem and others who thought it was no major problem. The main barriers to entry in the remittances services business in Ethiopia are access to distribution network, access to capital/finance, and access to financial infrastructure in descending order. Licensing appears to be less of a problem for starting up the business, in consistence with the previous response. Once a remittance business becomes operational, on the other hand, the

[9] Focusing on 'ethnic Somali' Ethiopians could be motivated by two factors. First, there is a large Somali Diasporas which sends money both to ethnic Somali Ethiopians and also the vast number of Somalia citizens leaving in Ethiopia. Second, 'ethnic Somali' Ethiopians are not as active as other linguistic groups in Ethiopian politics and hence Wegagan's preference to work with them, given the irregularity proposition we noted above.

most difficult obstacles (barriers) in running it include reporting requirements, lack of access to banking facilities, lack of access to clearing and settlement systems and exchange control in order of their significance.

3.2. Exchange Controls, AML/CFT and Know-Your-Customer (KYC) Requirements

As noted above, Ethiopia has one of the most regulated financial sectors in Sub-Saharan Africa and the most controlled in East Africa. One of the ways that this control is expressed is through the NBE's tight regulation of the foreign exchange market. NBE, which is the regulatory authority of the Ethiopian financial sector, puts a cap or limit to foreign holdings or remittance inflows of private operators. The cap is at around 15% of paid up capital (this result is derived based on just two responses- United Bank, however, puts this figure at 50%).

NBE also requires the operators to file currency transaction reports for an amount greater than the threshold of 7000 USD (according to CBE). The reporting conditions in cases of suspicious activities is not clear with 40% of the firms surveyed reporting that they are required to do so while another 30% said that they are not required to report.

Remittance service providers are also required to submit remittance data providing details of transfers of government, international organizations, individuals, PLCs and NGDs to the NBE on a monthly basis (NBE directive no. EXD/30/2006).

3.3. Competition in the Remittance industry

The level of competition in the Ethiopian financial sector at large is very low. Partly due to the regulation that prohibits foreign participation in the sector and the initial capital requirements, the number of firms in the sector still remains very low despite the high levels of profits being realized by the incumbents. There is increasingly growing interest from the private sector to engage in the financial sector as a result.

The picture in the remittance services sub-sector is no different. There are just few firms operating legally. The resulting lack of competition in sector is reflected in the high service fee that they charge. This has, among others, has paved way for the emergence of a considerably large informal sector.

In addition to the laws and regulations that the remittance operators felt are detrimental in starting up and running a remittance services business, as noted above, competition from informal remittance operators has also been found to be an important barrier to formal operators' activities in the business. The informal operators being unregistered will have no tax and associated costs which give them an unfair competitive edge over the formal ones (although they have a huge risk of being crack down by the government). This is clearly reflected in the fact that informal operators are among the three major rivals to firms operating in the remittance services business. According to the firms surveyed in the study, their main competitors are credit unions followed by informal service providers.

3.4. Laws/regulations (including taxes) that might create preference for informal providers

Although the information from our survey is very limited there (because our respondents declined to respond to issues under this section), unlike most other businesses with annual turnover of over half a million Birr, who are legally required to collect VAT on their sales, remittance operators are not required to charge taxes on their remittance services.

In 2006, the NBE issued directive no. 30 in the view of improving the operations of the formal remittance service in Ethiopia, reduce the associated costs of transfers and facilitate the access of international remittance service for Nationals and make the service reliable, fast and safe.

4. Remittance Costs and Identification Requirements

4.1. Remittance fees for major remittance corridors, differences in fees and foreign exchange commission for different corridors

NBE encourages remittance service operators to provide their remittance transfer service for free when remittances flow into the country (NBE, 2008). However, the experience regarding the fee that remittance operators charge recipients of remittances have been mixed. 60% of the remittance operators charge commission/fee to the receiver when receiving remittances, while 30% of the firms do not. The average fee/charge on remittances is 2.5% of the amount of the remittance (based on four results – CBE, Wegagen Bank, CBB and United Bank). There has been no significant change in the remittance fees over the past two years (only one firms responded- United Bank). The fees on domestic remittances are very small usually being less than 1% of the remittance amount.

All of the firms surveyed in the study provide inward international remittance services. Because of the relatively small number of firms operating in the remittances business, it appears that individual firms carry out significant volume of remittances transactions annually. A single remittance operator could process around USD 100 million per annum. Three firms responded about the volume of remittance. Two have an average remittance volume of USD 100 million but the third one has a surprisingly low volume of remittances (around two million USD). We may need to be cautious about these figures, however. Our discussion about one key informal sector operator pointed to the fact that about five small informal sector operators do receive a total of about USD 140 million per annum. This is excluding a couple of significant informal sector operators each of them at the minimum send as much as this about five operators. This put the annual figure by individual informal sector operators to be much larger than organized banks. Thus, it is highly probable that those banks who gave us information under reported their operation.

The main sources of international remittances to Ethiopia are United States, United Kingdom, Sweden, Norway, Canada, Lebanon, UAE and Australia (based on just three of the responses obtained).

Despite NBE requiring that remittance service providers deliver remittances to the receiver within 24 hours, with some firms it may take days. There is considerable difference in the time required for remittances received from abroad to reach destinations in urban and rural areas. In most cases remittances can reach urban centers with no more than two days: the day it is sent and the following day. The weakest operator in this respect is CBB which requires up to 5 days delivering remittances. It takes, however, relatively longer for remittances to reach rural destinations than urban ones; it could take twice as much for rural destination compared to that of urban areas.

Furthermore, according to 20% of the firms, there is a limit on the amount of money that can be received by customers. The remaining 80%, however, stated otherwise. According to CBB, for remittances through Western Union the limit per transaction is Birr 60,000.

4.2. Identification requirements

In the Ethiopian remittance services sector both senders and receivers of remittances are required to produce identification documentation for international as well as domestic transaction. For sending international remittances, remittance operators require, irrespective of whether the individuals sending the remittances hold accounts at the firms (operators) carrying out the remittance transaction, identification documents such as passports, driver's licenses, verification of employment, proof of residence and even letters from local authorities are accepted. The most popular identification documentation required to receive remittances from overseas are national passport, national identification card, and driver's license. The state banks also receive employment verifications in addition to the above.

Like the identification documentation requirements in overseas remittance services, such documents are also required in domestic remittances. As that of the external remittances the most widely used documents are national passport, national identification card and driver's license.

The use of such identification documentation could deter the rural poor's access to remittance products. A typical rural farmer may have difficulty acquiring those documents.

5. Remittance Volumes, Sources, and Destinations

5.1. Understanding flows through various types of providers

The NBE directive emphasizes that due attention needs to be given to improving the inward remittance services on view of mobilizing increased foreign reserves. Remittance operators also offer outward remittance services as much as they do inward remittances. This is in particular an important activity for the informal sector operators. Except 20% of the firms, the rest provide outward international remittance services in addition to their inward such services.

Among the firms surveyed, only 10% have a system in which remittance senders could specify the uses of the remittances (30% answered that they don't have a system- the rest however, didn't respond). According to the operator with such system, remittances are sent for purchase of housing, purchase of land and support of family.

In the formal sector remittances sent from abroad are paid in local currency (Birr). The NBE's directive on foreign exchange does not allow remittance recipients to cash in their balances in foreign exchange. As a result, the formal remittance operators pay recipients the domestic currency (Birr) equivalent of the amount of remittance. The informal operators, on the other hand, allow foreign exchange payments. This may partly explain the fast growth of informal operators and the growing preference to those in the face of the recent high inflation in the country.

The volume (based on just one response) to domestic remittance received has grown from Birr 7 billion in 2006 to 24 billion in 2007/08 fiscal year, while the number of transactions has also grown from over 468 thousand to 1.48 million over the same period. During the same period remittances sent within the country have grown from Birr 4.9 billion to 14.4 billion and the number of such transactions from 304 thousand to 831 thousand.

5.2. Seasonality

The inflow of remittances to Ethiopia follows some sort of seasonality. Flows peak during august to September and December to January. Particularly the months of January and September remittance flows are the highest. There is also a tendency for remittances to peak during holidays. In fact, the high flow of remittances during the stated periods of the year may relate to the holidays such as the Ethiopian New Year and epiphany that are celebrated around that time.

6. Conclusion and Recommendation

In this study an attempt to understand the issue of remittance and problem of remittance service providers in Ethiopia has been made. As the study is perhaps the first of its kind we couldn't benefit from previous work on this area. This lack of studies in on remittance in Ethiopia is surprising given that officially recorded remittance is greater than the total export revenue that the country currently generating, which is about one billion USD. We estimate the informal sector operators also handle about as much. Notwithstanding this, the issue of remittance received little attention in policy circles in terms of creating conducive atmosphere and attractive incentive structure to retain what is available and attract more. We hope that this study will highlight the importance of remittance and the problem of remittance service providers in Ethiopia to make an informed policy by the government.

We found that the formal procedure of getting a license and operating in the sector is not a major problem, at least on paper. However, implementation is problematic for most banks, especially to work with the private sector operators. Some of the private banks and informal sector operator have difficulty of getting license to engage in the sector, notwithstanding the clarity of the law and its applicability to any operator. For those in operation, regulatory environment places moderate obstacle. On the other hand banking licence requirement, minimum capital requirement and access to financial instruments are major problems for moist firms. In addition, exchange control and the global money laundering is a barrier to remittance business. For all formal firms competition from the informal sector is a major obstacle and a severe one for some. However, if the regulatory and financial sector environment is improved, the informal sector operators could be easily pulled in the formal sector, as the risks of operating for informal sector is very large.

In terms of access to the remittance sector operation ID requirements - may limit access of poor households, however the problem is not sever in Ethiopia as most operators use about 4 types of IDs. Networks in urban/rural areas are very limited, specially the latter. In terms of time required a remitted money to reach urban and. rural recipients, we found rural areas to be more difficult to reach. Currency covert ability is also found to be one of the major problems for the formal sector operators. This (and related less transaction costs) has led most people to dependence on informal sector operators.

For informal sector operators the major problems is general policy environment and lack of deepening in the financial sector liberalization. As a result they operate in an environment where the administrative risk of operation is very large, and hence the cost of operation for themselves and their clients is high. Given conducive environment it is highly probable that informal sector operators could be attracted to the formal sector. Moreover, as our one case of a cooperative bank experiences shows and credit unions and cooperative bank may be more forthcoming to the sector.

Thus, it is imperative that the government needs to design attractive incentive systems and offer an enable environment by addressing problems outline above so as to benefit from the remittance industry. There is a need to move away from administrative control on the formal sector operators and crackdown on the informal sector to open system with the right incentive and regulatory framework. Controls and crack down may trigger negative effect on other sectors of the economy. The latter can be read from the long queue that banks currently experiencing to open a letter of credit for their customers following the crackdown in the informal sector remittance sector and forex bureau operators by the government.

Finally it is worth emphasizing the importance of the remittance industry (which is at least twice that of the Ethiopian export sector) on the one hand and the lack of commensurable policy emphasis by the government to sector on the other, which is in a stack contrast with the incentive the government gives to the export sector. It is high time to work on this policy issue for the government. A related issue important for sustainability of remittance flows is to encourage Ethiopian's abroad to invest in the country, which the government is actually doing. This may help to sustain remittances by rekindling the link the offspring's of the first generation migrants will have with the home country of their parents.

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