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STRATEGIC ISSUES LINKED TO THE MEASUREMENT OF INTERNATIONAL TRANSACTIONS

SESSION IIA: SELECTED MEASUREMENT ISSUES: SOME CURRENT ACCOUNT ISSUES

THE WORK OF THE LUXEMBOURG GROUP ON REMITTANCES

Note by Eurostat[1]

I. INTRODUCTION

1. The importance of remittance flows[2], both in political discussions and in economic and social analyses, has increased tremendously over the last few years. As more data become available on cross-border remittances, these financial flows are attracting greater attention from the private sector, governments and development agencies alike.

2. In recent years remittance flows have emerged as a major source of external financing in developing countries. The growing importance of remittances as a source of foreign exchange is

[1] This paper has been prepared at the invitation of the secretariat.
[2] In the Balance of Payments statistics framework workers' remittances covers goods and financial instruments transferred by migrants living and working in new economies to residents of economies in which the migrant formerly resided.

reflected in the fact that remittance growth has outpaced private capital flows and official development aid (ODA) over the last decade. For some countries, remittances constitute the largest single source of foreign currency and often rival foreign direct investment (FDI) in size. Because of their volume and their potential to reduce poverty, remittances are attracting growing attention from policymakers at the highest levels in both developed and developing countries.

3. Many national governments now identify remittances as a major policy concern and want to analyse their impact on economic development. Numerous international institutions have programmes or projects designed to analyse or promote remittances and related policies. Some governments and international organisations wish to promote the volume and effectiveness of remittances through better regulatory and institutional arrangements. The European Commission is committed to this issue in a broader perspective. In September 2005, it brought out a Communication entitled "Migration and Development: Some concrete orientations" (European Commission, 2005). The document contains a series of recommendations for fostering the links and synergies between migration and development, in particular with regard to facilitating remittance flows and enhancing their development impact.

4. The purpose of this paper is to illustrate the work of the Luxembourg Group on Remittances in preparing a guide to compile data on remittances. The paper first highlights the growing importance of remittances in the world economy. It addresses the international initiatives undertaken in order to clarify the concepts and definitions related to remittances. It then describes the work of the Group in providing better guidance on data collection. It finally presents the results of a recent Eurostat survey on remittance flows to and from the EU.

II. GROWING IMPORTANCE OF REMITTANCES

5. According to the World Bank, recorded remittances sent home by migrants from developing countries reached US$199 billion in 2006, up from US$188 billion in 2005 and more than double the level in 2000 (World Bank, 2006b). Worldwide flows of remittances, including those to high-income countries, are estimated to have grown to US$268 billion in 2006. This amount, however, reflects only transfers through official channels. Given measurement uncertainties, notably the unknown extent of unrecorded flows through formal and informal channels, the true size of remittance flows could be much higher – perhaps 50 percent or more (World Bank, 2006a).

6. Including these unrecorded flows, it can be estimated that the true size of remittances is larger than foreign direct investment flows and more than twice as large as official aid received by developing countries. Remittances are the largest source of external financing in many developing countries.

Table 1: Global flows of remittances (US$ billion)

	1990	1995	2000	2005	2006
All developing countries, of which:	**31**	**58**	**85**	**188**	**199**
Latin America and the Caribbean	6	13	20	42.4	53
South Asia	6	10	17	32.0	36
East Asia and the Pacific	3	1	17	43.1	45
Middle East and North Africa	11	13	13	21.3	25
Europe and Central Asia	3	8	13	19.9	32
Sub-Saharan Africa	2	3	5	8.1	7
High income OECD	**37**	**43**	**46**	**68**	**68**
World	**69**	**102**	**132**	**257**	**268**

Source: World Bank (2006a, p. 88), World Bank (2006b, p. 1)

III. INITIATIVES TO IMPROVE DATA QUALITY

7. Data on remittances are difficult to compile, because they represent numerous, small transactions through a large variety of channels. A pre-requisite for improving compilation of data on remittances is a proper understanding of demographic aspects, transmission channels and the regulatory environment affecting the volume, frequency and transaction modes. The transmission channels may vary according to the demographic structure, financial system and overall institutional environment of the sending and receiving countries. As a result, considering their volumes and relative importance, the quality of data on remittances is quite poor. This poor quality is in stark contrast to data on international financial flows more generally (in the balance of payments framework), where there has been a tremendous improvement in the quality of data over recent decades.

8. Furthermore, the definitions of remittance-related items in the balance of payments framework require clarification, do not fully meet user needs, and make analysis of data more onerous than necessary. As a result of the lack of clarity on what should be included in remittance statistics and the inconsistency in methods of collection and reporting, currently available remittance data are incomplete. They fail to capture a significant proportion of remittance flows and are not comparable across countries and regions and over time (see Reinke, 2006).

9. The importance of remittances, and improved statistics on them, was emphasised by the G8 Heads of State at their meeting at Sea Island in 2004. The G8 leaders issued an action plan in which they gave a commitment to intensify work on migrant workers' remittances, including improvement of the data. This message was reiterated by the G7 Finance Ministers, who called for the establishment of an international statistical working group bringing together technical experts from various countries and international organisations, which would be responsible for:

(a) Clarifying the concepts and definitions concerning remittances; and

(b) Providing better guidance on data collection.

10. The task of clarifying the **concepts and definitions** concerning remittances was carried out by the United Nations Technical Subgroup on the Movement of Natural Persons (UN-TSG). The UN-TSG has proposed new definitions for remittances within the balance of payments framework and has recommended changing the definition of "workers' remittances" to the broader concepts of "personal transfers", "personal remittances" and "total remittances" – for details see UN (2006). These changes will be incorporated in the forthcoming revision of the IMF Balance of Payments International Investment Manual (BPM6) and should substantially improve the accessibility and clarity of data on remittances.

11. Furthermore, in June 2006 an expert group called the Luxembourg Group on Remittances was created with the objective of providing better **guidance on data collection** by drafting a guide for compiling statistics on remittances.

IV. WORK OF THE LUXEMBOURG GROUP ON REMITTANCES[3]

12. The Luxembourg Group on Remittances was established in June 2006 with a constituting meeting in Luxembourg, organised by Eurostat on the premises of the European Commission. The principal objective of this Group is to draft a guide for compiling statistics on remittance flows. 27 experts from 14 countries and 5 international organisations are members of this Group. A second meeting of the Group was held in Frankfurt in December 2006 and a third and final one in Brasilia in June 2007. Leading sending and receiving countries are represented in it. The diversity of experiences of this group helped to assure that a wide variety of remittance flows, data sources and compilation practices were considered, and that the resulting guide has the widest possible appeal. The draft version of the guide will be made available on the IMF's website soon for comments from all interested parties. The final version is planned by the end of 2008.

13. The primary purpose of this guide is to offer compilers a menu of possible methods for measuring remittances and to assist them in their efforts to provide accurate, complete and timely data on remittances that are consistent with the improved concepts and definitions. The compilation guide is primarily aimed at those whose task is to obtain, process, verify and publish data on remittances. However, the guide will also be a useful source for data users who wish to understand the definitions and processes that shape the data they employ for analytical purposes.

14. The biggest obstacle to improving data on remittances is the nature of the flows, involving often small transactions, by private individuals, using a variety of transaction channels many of which are informal or personal. The small size of individual transactions means that they often go undetected by more typical data source systems, although the aggregate level of transactions may be substantial. As a result, this guide focuses on the problems and solutions to obtaining better data on remittance transactions, but it also summarizes compilation and data dissemination issues. It describes the institutional and regulatory context of remittances, illustrates various transaction channels, discusses relevant concepts and definitions, analyses different approaches to obtaining data on remittances, reviews good compilation practices with a view on remittances and concludes with a look at dissemination options.

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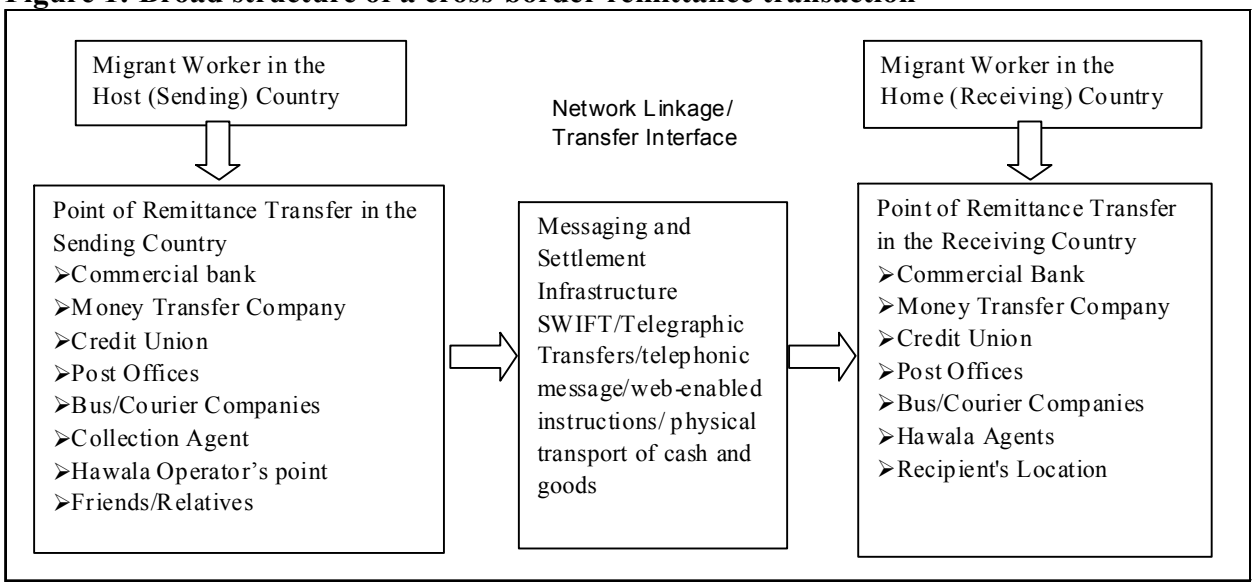
[3] This section is based on unpublished working materials prepared by the Luxembourg Group.

A. Inventory of transfer channels

15. A money remittance transaction involves sender, recipient, intermediaries in both countries, and the payment interface used by the intermediaries. Most remittances are person-to-person, of relatively low value, and regular, as they are generally targeted at family maintenance. Remittances assume the form of cash or credit transfers and non-cash transactions. Cash transfers are either sent in the foreign currency or the local currency by means of physical transfer of cash. Credit transfers are based on payment instructions from providers in the sending to the receiving country. While the payment instructions using the messaging services enable contact between the entities operating at the sending and the receiving ends, the settlement process enables actual transfer of funds between these entities. Non-cash or in-kind transfers, which comprise mainly consumer goods, involve physical delivery predominantly through informal routes. It is important to understand broadly how the remittance transactions take place. A typical transaction between sender (migrant) in the host country and recipient (beneficiary family) in the home country may assume the following processes (see figure 1):

Figure 1: Broad structure of a cross-border remittance transaction



16. The relative attractiveness of competing methods of transfers is determined by a host of factors. A high level of penetration of the formal banking sector in the sending and receiving countries may encourage migrants to use account-to-account transfers. Despite the availability of bank services, fixed transaction cost and onerous documentation requirements to meet the regularity obligations may render small value transactions unattractive for the banks and clients. The cost of sending money home may significantly influence the choice between the formal and the informal methods.

17. In addition to costs, time of delivery has an important role in influencing the decisions of the sender to choose a particular channel. It is often reported that the transfer through hawala takes less than 12 hours to reach the recipient. Although online methods offered by the formal modes are relatively more efficient in terms of speed of delivery, their usage is constrained by the availability of information technology infrastructure at the sender's end and the access at the location of the receiver.

18. Apart from the explicit costs, the hidden cost in terms of exchange rate may significantly influence decisions regarding a particular method. Risk of money in transit may also influence the decisions regarding choosing a particular mode. Where migrants are able to frequently visit their home country, they may carry cash or goods themselves or send them with friends. Migration status may significantly impact on the usage of a particular mode. Illegal migrants may prefer to remit money through informal channels as they lack proper identification requirements to open bank account and remit money.

B. Data collections frameworks

19. A big part of the guide is devoted to possible data collections systems. In addition to a detailed description of the collection system it describes the preconditions necessary to function the collection system efficiently, the transfer channels that can be covered, merits and drawbacks of the collection system, practical compilation guidance, i.e. how to realise the system, breakdown into sending/receiving countries perspectives as well as potential output in terms of BPM6 definitions.

International Transactions Reporting Systems (ITRS)

20. An ITRS is a data collection system that obtains data from banks and enterprises at the level of individual transactions. It should measure individual balance of payments cash transactions that pass through domestic banks and through enterprise accounts with banks abroad, non-cash transactions, and stock positions. Not all ITRS systems are developed to include non-cash transactions and stock positions. Where an ITRS exists and produces data for BoP, compilers should use it for compiling remittance flows even if these data have shortcomings. The guide does not recommend establishing an ITRS only for the purpose of collecting data on remittances.

21. The strengths of the ITRS as a data source lie in timeliness and periodicity, since data are generally registered at the moment of settlement of the transactions. In countries with an appropriate regulatory and institutional framework, including foreign exchange restrictions, it is likely to be a cost-effective source for remittance data. Well structured, comprehensive ITRS tends also to be very accurate in what it measures. The ITRS also shows some weaknesses as data source. In many cases remittances are transferred through informal channels. In this case, an ITRS, which relies exclusively on remittances sent through formal channels, may present significant omissions. Misclassifications are a frequently identified problem with ITRS-based compilation system because intermediaries are responsible for classifying transactions. Moreover, existence of exemption reporting thresholds may lead to loss of a significant amount of information.

Direct reporting by Money transfer operators

22. Direct reporting refers to the practice of obtaining data from a group of transactors directly instead of indirectly from settlement facilities. Money transfer operators (MTOs) occupy a dominant role in the remittance industry, and direct reporting seems particularly appropriate to obtaining data from them. Since transactions by banks are often covered by an ITRS, direct reporting is also a useful supplement to an ITRS. It is an effective source if MTOs account for a

large share of remittance transactions in the reporting economy and if appropriate legal environment can be set up to ensure that reporting requirements can be established and enforced.

23. In the case of remittances, direct reporting has further advantages compared to compilation based on an ITRS alone. These include better information on gross flows (outbound and inbound) and the geographical distribution of counterparts, and greater detail and accuracy of the data collected, as the information is directly provided by the information holders, without any intermediate communication step. The weaknesses of this system are classification errors in relation to residence of transaction parties and purpose of transactions. MTOs agents cannot always reliably establish whether payments are from short-term workers or from migrants who are residents in the reporting economy. Although a great majority of transactions through MTOs are household-to-households transfers, it cannot be excluded that some of the transactions are not related to remittances, and are rather payments for the purchase of goods or other commercial services.

Household surveys

24. Household surveys that are well designed and ask the right questions can be a valuable source of information for compilers of remittance data. They can be used to improve the quality of data directly, and provide more detailed insights into the nature of flows and their impact as they can provide information on the mode of transaction, and the volume and direction of flows. They may be useful as a direct data source, to improve the accuracy of estimates, to better understand remittance flow mechanisms, and to provide estimates of parameters for use in econometric modelling techniques.

25. The merits of using household surveys as a data source for compilers include the potential for collecting data on transfers sent through both formal and informal channels. Additionally, surveyors have more direct control over the information collected, since it is not produced as a by-product of administrative or financial systems. In countries where questions can be added to regular surveys, fresh data on remittances can be obtained at the same frequency as the household survey. Surveys can also provide insights about how remittances are transmitted and what are they used for, which can be useful information for the Balance of payments compiler when evaluating the coverage of data obtained from other sources. There is, however, the possibility of sampling errors and non-sampling errors as well of samples that may not represent the target population. This is particularly true where the target population under study is relatively rare and the number of respondent households in the sample is small. Information on remittance flows may be under-reported, as these data are often considered sensitive by respondents. Moreover, balance of payments concepts and definitions need to be considered when designing surveys or using survey results, and carefully compared to the concepts and definitions used in surveys. The costs of using household surveys vary significantly between countries. Obtaining estimates with larger precision usually require larger samples, which increase costs or decreases freshness. Adding questions to an existing survey may be the cheapest method, but resulting usable sample sizes may be small unless consecutive samples are pooled because households making or receiving remittances are likely to be relatively rare.

Indirect methods based on modelling

26. Secondary data, like observable demographic or economic variables can be used to estimate remittance flows. Depending on the nature and availability of secondary data, estimation approaches can be tailored to the needs and possibilities of each compiling economy. Estimation approaches are referred to as models, reflecting the fact that they are a representation or description of a system or process designed to show its structure or functioning. The basic idea behind demographic models is to obtain an estimation of the remittances payments by using the information on the number of immigrants who send remittances, their family structure, duration of stay, the average income of different groups, the propensity to remit, etc. The idea behind econometric modelling is that the compiler would identify the determinants of remittances for which data are available, like income differentials between sending and receiving countries, GDP growth differential, exchange rate differentials, migration and related demographic statistics, remittance costs, etc., then specify and estimate a mathematical model to estimate remittances based on these determinants. A third approach are models that estimate remittances from information on current account imbalances and other information sources. These residual models rest on the assumption that, once all observable inflows and outflows have been recorded, discrepancies are most likely unobservable remittances. In its simplest form, such a model could then derive remittances as the residual under the assumptions that foreign exchange inflows equals foreign exchange outflows and that all foreign currency inflows are converted to domestic currency for use in the domestic market.

27. Estimations based on models can cover remittances sent through both formal and informal channels. Through the use of existing data, the cost of estimating data on remittance flows can be rather low. However, only reliable input data will lead to sound estimates, regardless of the sophistication of a model. Indirect data are converted to remittance estimates using a set of assumptions. These assumptions should be plausible, but it is often not possible to test or verify them in practice.

C. Comprehensive approach to improving remittance data

28. The guide gives a detailed description of strengths and weaknesses of different data collection systems. However, the availability of sources, and the relative merits of using them, varies from country to country. Therefore, the purpose of the guide is not to recommend one specific data collection system for all countries. Compilers have to decide which data sources to use in the circumstances of their country, knowing their relative merits and drawbacks, and depending on institutional, legal and practical considerations.

29. The guide discusses the limitations of reliance on a single data source, the combination of data from multiple sources in compiling all relevant remittance aggregates and the use of secondary data for estimating missing components such as specific informal remittance flows or adjustments. It outlines a comprehensive approach to improving remittance data and also discusses the problems arising from a misalignment of definitions with data classifications.

30. Remittance transactions are heterogeneous and no single data source can ensure that all transactions are reported adequately. Data obtained from ITRS and direct reporting from MTOs, capture only transactions routed through the respective formal sector institutions. Surveys are

subject to underreporting and misclassifications. Also, survey data is typically less timely and frequent. Administrative data are collected for purposes other than compiling remittance data, so neither its coverage nor definitions may be well aligned.

31. Given the shortcomings of each individual data source, data from different sources may be combined. Additional data or estimations may be required to account for transactions passing through channels not captured by the main data source. Compilers therefore have a need for data from numerous sources to ensure accuracy, good coverage, and sufficient timeliness and frequency of output data. Compiling data on remittances is more demanding in this regard than most other balance of payments items. A practical approach towards building a work programme for improving remittance data, with due consideration to reporting burden and compilation cost can be illustrated as follows:

Step 1. Understanding the Current Situation

32. Compilers wishing to improve remittance data first need to understand the current situation regarding remittance transactions, focusing on two factors: identifying possible remitting channels, and recognizing the predominant remitting channels used in the country among those possible channels.

Step 2. Evaluation of Current Data Collection System

33. Compilers should then evaluate the current data collection system on remittances in the balance of payment statistics. By comparing the major remitting channels and the data collection system identified, compilers can check the match between important channels and data sources covering them, identifying the most important omissions. For the channels that are insufficiently covered in the current data collection system, compilers can assess their relative importance.

Step 3: Prioritization

34. A sound compilation strategy needs to prioritize tasks by taking into account data needs, including the coverage, accuracy, timeliness and periodicity of data, as well as the costs of improving data (this includes an assessment of the need for improved remittance data versus other data needs and the capacity of the compiling agency to implement improvements). The channels identified as being insufficiently covered in step 2 are the targets for the expansion of the coverage.

Step 4: Improvement and Expansion of Data by Channel

35. Different data sources and approaches cover different channels and transactions. Compilers should therefore improve and expand their data source program with specific reference to data gaps and omissions in existing source and priorities identified in step 3. The effective ways to capture data vary depending on the major remitting channels as well as whether the country is the remitting country or the recipient country. For example, it is generally easier to identify remittances in ITRS data in the remitting than in the receiving country. In contrast, it may be easier for the recipient country to conduct household surveys on remittances than for the remitting country, due to sampling problems related to remittance sending households.

Therefore, compilers should understand the situation of the country, identify their specific data needs and choose effective ways for improving and expanding their data sources.

36. The guide reviews also good practices in disseminating data on remittances, including the dissemination of supplementary information, the importance of bilateral data to some users, the dissemination of data to users who are not otherwise users of balance of payments statistics, and the dissemination of metadata.

V. RESULTS OF A EUROSTAT SURVEY ON REMITTANCE FLOWS FROM AND TO THE EU

37. In response to the increasing demand for data on remittances, Eurostat launched an ad hoc survey in April 2007, asking Member States to provide statistics on remittances and compensation of employees, collected within the framework of balance of payments statistics (Eurostat, 2007).

38. Migrants in the EU Member States sent, in total, to their former country of residence an amount of €26.1 billion in 2006 (compared with €23.2 billion in 2005). These figures include both intra-EU and extra-EU flows. Flows to non-EU countries accounted for a much higher share than flows between Member States. In 2006, extra-EU flows accounted for €19.1 billion or three quarters of the total, and intra-EU flows for €7.0 billion or one quarter, the same proportions as in 2005. Spain, the UK, Italy, Germany and France are the main remitting Member States. These five Member States account for more than 85% of total EU remittances. The data show that, in 2006, the EU as a whole remitted more than double the amount it received from third countries (€19.1 billion sent compared to €8.5 billion received).

39. The results of the Eurostat survey also show that, in 2006, the total amount of "net compensation of employees" (i.e. compensation of employees minus taxes and social contributions, and minus transport and travel expenditures related to short-term employment) transferred from the EU Member States to non-EU countries reached €3.0 billion (€3.1 billion in 2005). However, extra-EU flows are negligible when compared to intra-EU flows. In 2006, the total outflow of net CoE from EU Member States to other Member States amounted to €15.4 billion (€14.0 billion in 2005). Luxembourg and Germany are the biggest sending countries in this respect.

40. In addition to global flows, the document identifies and quantifies the major corridors of remittances. Remittance flows from Spain to Colombia account for the largest corridor, followed by Spain to Ecuador (€1.3 billion and €1.2 billion respectively in 2006). In 2006, other major corridors were Germany to Turkey (€0.8 billion), and France to Portugal and Morocco (both €0.8 billion). From the standpoint of the receiving countries, the biggest corridor in 2006 was that of €1.6bn to Romania from Italy. This was followed by Spain from the UK and Romania from Spain (€1.2bn and €1.0bn respectively).

41. An increasing number of EU Member States are now publishing remittance data on a regular basis. Eurostat is also considering doing so in near future.

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