Costly cash http://www.economist.com/node/21663227#print

Regulation is raising the cost of sending money to the world's poor. Reform it

SUPPOSE there were a way of getting money to some of the world's poorest people precisely when they need it. Suppose, too, that the flow hardly ever diminished, even during a global financial crisis. Finally, suppose the cash could not be creamed off by corrupt local officials. Surely every right-minded government in the world would want to encourage this and make it as cheap and easy as possible?

Alas, no. Remittances, the packets of money sent home by migrant workers from India, the Philippines and elsewhere, are individually tiny but collectively enormous. The World Bank estimates that flows to developing countries will be worth $440 billion this year—more than twice as much as foreign aid. And that is just the payments the bank can track.

The money earned from feeding toddlers, sweeping floors or writing code in richer countries brings all sorts of benefits when it returns home (see article). It eases poverty and boosts consumption. When poor families begin to receive remittances, they tend to yank their children out of menial jobs and send them to school.

Yet remitting money is expensive. In 2009 the G7, a club of rich-country governments, said it would try to cut the global average cost of sending funds from 10% (as it was then) to 5% over five years. The world is not even halfway there: the average stands at 7.7%, if wide exchange-rate spreads are counted as well as transaction fees. That is despite the emergence of rivals to giant money-transfer outfits such as MoneyGram and Western Union, which use networks of agents to collect and pay out cash. Peer-to-peer transfer services have popped up, slashing the cost of shunting money around the rich world. In poor countries, especially in Africa, "mobile money", which can be transferred from one person to another by mobile phone, has made domestic transactions virtually free.

The problem is that, even as technology boosts competition and cuts costs, regulation is pushing in the opposite direction. Guidelines intended to prevent money-laundering and the financing of terrorism imply that all sorts of cross-border transfers should be treated as very risky. The costs of complying with the rules are high, and the penalties for breaching them stringent. Western Union, for example, agreed to no fewer than 73 changes to its procedures in settlement in 2010 of claims in America that it had abetted money-laundering: it now conducts background checks on its agents, and has even adapted the software it uses to scan for suspicious transactions to account for the seasonality of marijuana harvests.

For fear of red tape and ruinous fines, banks have simply withdrawn from some markets. That means less competition and prices higher than they would otherwise be. The effect is worst in war-torn countries like Somalia, which most need remittances. This is not just unfortunate; it is also counter-productive. When it becomes inconvenient and expensive to send money legitimately, money flows illegitimately. It can be stuffed into suitcases or sent through informal *hawala* networks, which are lubricated by trust and do not actually move money across borders. At that point, the paper trail disappears.

A sharper stick

To ease the frictions that continue to make remittances costly, action is needed on two fronts. First, rich countries need to target their anti-money-laundering regulations much more precisely. Organisations like the Financial Action Task Force, an inter-governmental body, should spell out in finer detail what makes a transaction highly risky. Banks should be reassured that they will not be prosecuted so long as they follow certain procedures, such as checking wire-transfer information against lists of suspected terrorists and criminals.

Second, remittance-receiving countries should do their bit. They can invest in watertight national-identity systems, such as India's biometric one. These make it easier to track money, whether it is paid out in cash or sent to somebody's mobile account. They should also ensure that mobile money does not end up reducing competition. There are welcome signs of telecoms firms in sub-Saharan Africa allowing payments between rival mobile-money systems, even across borders. In some cases they have been prodded into so doing by courts and regulators, which should keep on prodding.

The main thing is to see remittances for what they almost always are. They are not devices for laundering drug money (which can be done more effectively in other ways) or financing terrorism. They are payments sent by loved ones, in response to need. As far as possible, they should be left alone.