MicroSave India Focus Note 28

Exploring Domestic Remittances as a New Line of Business for Indian MFIs

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Background

The domestic money transfer business offers a colossal opportunity for financial institutions in India. As a proxy indicator of the size of the domestic remittance market, India Post handled 96 million money orders last year.[1] With an average remittance of Rs.780 the total value comes to around Rs.75 billion. This is just a fraction of the total size of the remittance business in India, as most domestic remittances follow other formal and informal routes. However, despite their outreach and presence in remote areas, microfinance institutions (MFIs) have yet to tap the full potential of this market. One of the greatest impediments for MFIs to start a domestic remittance service in India is the present legal framework. The Reserve Bank of India (RBI) considers any collection of remittances as deposits and thus prohibits the service being offered by most institutional forms in which Indian MFIs operate.[2]

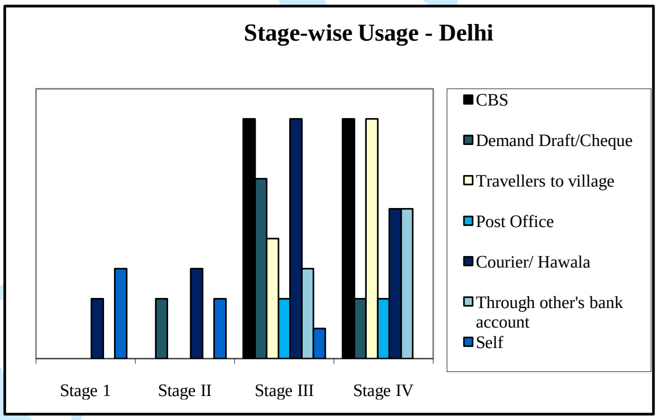
Given the size of the market and the potential for legal provisions to be relaxed, it is equally important for MFIs to understand the following before offering this type service: 1. what the existing options are (i.e. the competition); 2. who sends remittances; and what their preferences are and 3. what the major risks and challenges are when providing a remittance service.

Remittance Options Available in India

Even for the client segments that MFIs in India serve, there are multiple options for domestic money transfers. Recent market research studies, conducted by *MicroSave*, showed that (Instant) Money Order, Cash Deposits through Core Banking Solutions (CBS), Demand Drafts and ATM networks are used extensively as formal means to transfer money.[3] At the same time, and equally important, in terms of volume, many migrants use informal means like "Courier Wallahs" and friends and relatives.

Remittance Clients and Options Used

MicroSave's research categorised four stages of migration ranging from temporary migrants to resident migrants who have been living over 10 years - usually with family - but who still go back to their native village for special occasions. As seen in the chart below, each migration stage sees clients use different systems to remit. Stage III and IV migrants, who are a more settled category and have access to bank accounts, increasingly use core banking systems and demand drafts/cheques to remit money while the less settled Stage I and II migrants, who usually do not have bank accounts, use more informal means.



Even with availability of so many options, there is still a huge demand for MFIs to offer these services to the client segment they serve. This is primarily because of inherent weaknesses associated with both informal and formal means of remitting money. For the informal sector the problems are costs and security; while for the formal sector it is lack of "last mile" accessibility and time. This leaves significant gaps for MFIs to offer remittance services that are fast, secure and delivered from a convenient locale.

Preferred Product Attributes After a careful analysis of the market research data, *MicroSave* has derived preferred product attributes of a remittance product for microfinance clients. As can be seen from the table below, product attribute preferences of migrants clearly emphasise the need for speed, reasonable pricing, security, simplicity and improved access.[4]

[1] P. K. Gopinath, Postal Staff College of India, 2009

[2] However in the 2009 'Report of the Internal Group,' RBI does mention certain enabling provisions for the 'Business Correspondent Model' to offer remittance services to the clients of the MFI. Report of the Internal Group to Examine Issues relating to Rural Credit and Microfinance, Refer URL: http://rbidocs.rbi.org.in/rdocs/PublicationReport/Pdfs/65111.pdf, 21/7/2009

[3] Market research study conducted in Delhi and Mumbai by *MicroSave* staff Nitin Garg, Sachin Bansal and Krishna Thakker

[4] See *MicroSave* India Focus Note 27 "Migrant Remittances – An Untapped Market" for more details.

Product	Rs.2,500 to Rs.7,500
Price	1.5-3% up to Rs.5,000. Additional 1-2% for amounts >Rs5,000.
Promotion	Existing microfinance clients, migrant population in urban slums
Place	Door step through m-banking Confirmation through SMS
Positioning	Last mile operators
Physical Evidence	Existing branches/agents such as retail shops
People	Branch/field staff/agents
Process	Simplified and fast Little or no documentation Account to account transfer Account to non-account transfers

Risks Associated with Remittance Services

Remittances are something very new to the vast majority of Indian MFIs. Therefore, it is important to understand the risks associated with offering such a service to clients. The technical guide "Making Money Transfers Work for Microfinance Institutions", outlines some of the risks associated for MFIs offering remittance service including: [5]

1. *Cash Management Challenges*: related to the unpredictable nature of remittances and maintaining enough liquidity.
2. *Information Management Challenges*: managing the volume of transactions and ensuring transaction security.
3. *Client Service Challenges*: related to the human elements of convenience and trust.
4. *Payment Medium Challenges*: exploring the right payment medium for the clients.
5. *Compliance Challenges*: related to ensuring on-going compliance with existing regulations - particularly KYC/AML.[6]
6. *Partnership Challenges*: managing different partners in the process of money transfer (banks, telecoms, agents, etc).

In the Indian context, there are very few significant examples or models to quote or follow. However, there are few organisations, like Al Najib, which offer remittance services to its clients.

The Power and Potential of Remittances

Al Najib Milli Mutual Benefit Ltd. was incorporated in April 1990 as a Mutual Benefit Company under the Indian Companies Act, 1956. It is delivering financial services through 45 branches spread across four states in India (Uttar Pradesh, Delhi, Maharashtra and Gujarat). Al Najib plays an important role in the communities it serves, and is respected, trusted and valued by its customers.

Al Najib offers a remittance product in two variants – one based on a money transfer order that can be encashed in any Al Najib branch; and another, faster, version that involves sending a fax to the branch where the money will be withdrawn.

Al Najib has 6 branches across various suburbs of Mumbai from where they serve many migrant clients, predominantly from the state of Uttar Pradesh. In spite of the overall rising trend of remitting through core banking services in Mumbai, the remittance products of Al Najib remain popular. Andheri, one of Mumbai branches visited by *MicroSave*, remits over Rs. 3 crores annually.

Conclusions

There is increasing interest in extending remittance services to the poor due to the growing involvement of telecos, private banks and technology companies providing mobile banking and other types of platforms.[7] Quite a few such experiments are now underway to develop a robust, secure yet simple technology based platform to be married with the network of ATMs and bank branches. While the cost, security and speed aspects are being addressed in these initiatives, one aspect is still often lacking: convenient access. This is where MFIs with a robust IT-based MIS can step in.

At the present level of maturity of the microfinance industry in India, the role of MFIs could be that of a service provider, to both collect and deliver remittances, thus generating new revenues on a commission basis from their bank partners. This in effect could mean offering a new high value-add service to its clients while earning a new revenue stream to support viability.

[5] **Isern** J, W. Donges, J. Smith, "Making Money Transfer Work for Microfinance Institutions", CGAP, 2006.
[6] Know Your Customer/Anti Money Laundering
[7] See *MicroSave* India Focus Note 29 "Potential for E-/M-Banking Enabled Migrant Remittances" for more details.