Informal Remittance Flows
and Their
Implications for Global Security

Dr. Nayef R.F. Al-Rodhan
Senior Scholar in Geostrategy and
Director of the Program on the
Geopolitical Implications of Globalization
and Transnational Security
Geneva Centre for Security Policy

September 28, 2006

To comment, please email Bethany Webster at b.webster@gcsp.ch.
Review and Critique
Remittance flows are a vital source of income for individuals within various countries around the world.¹ In 2005, an astounding estimated $232 billion in remittances were sent globally, an increase from $68.6 billion in 1990.² Dependence on this system has become an issue of international security, particularly in the aftermath of the events of September 11, 2001. Due to the misuse of this system by terrorist organizations and other potentially harmful actors, the international community has, over the past few years, demanded reform of the system in order to better regulate it. However, in so doing, some of the most beneficial aspects of the informal network may be at stake and therefore prevent many people in certain regions of the world from receiving the only income to which they have access.

As indicated in the Global Economic Prospects 2006 report produced by the World Bank, “governments in destination and origin countries can sharpen the developmental impact of remittances through the application of appropriate policies.”³ Both have a large role to play in monitoring and improving the way that remittances can be tracked without disrupting the flow of this vital lifeline. For instance, currently the cost of remittances could be greatly impacted by a system that protects the percentage charged to even the smallest transfers.⁴

The largest dilemma for states is that confidentiality and a non-governmental, non-institutional system of money transfer are exactly what make the informal transfer of remittances so attractive for many migrants and their families. At the same time, it is these very qualities – confidentiality, lack of paper trails and institutional accountability – that make such remittances a concern for governments. Often based in countries where there is an existing lack of trust in more formal banking systems or there is no access to formal banking, the informal transfer, or hawala system, has grown over the years. Specifically, hawala is an informal banking system in which funds are transferred internationally, without being physically moved. The main users of the system reside in the developed world and transfer funds to recipients in the developing world. The system makes monitoring the flow of remittances extremely difficult for states and therefore attractive not only for those who do not trust formal, traditional banking channels but also for those who would like to transfer funds illegally and undetected. This is what prompted the US to close banking institutions in Somalia in November, 2001 as it was believed that certain institutions (Al-Barakat, the Somali hawala group, in this case) were used to deliver funds to Al-Qaeda and Osama Bin Laden, an accusation that was denied by the group’s founder and chairman.⁵

Miriam Fugfugosh⁶ outlines these issues very well in her policy brief and indicates where the most pressing problems lie, both for the states where immigrants currently reside as well as for the state where their families have remained. Additionally, she clearly identifies where the policy challenges are for states, which must find quick solutions for dealing with these informal networks that are so often used by mass groups of people. How do you build trust in
a formal system in countries where a history of corruption within governmental entities has led the population to – rationally – mistrust the state’s formal institutions? How can you bring these same people to trust that the remittances upon which they depend for survival will be safely and securely transferred at the state level?

Dilemmas and Our Recommendations

The solutions required to solve some of these problems may at first seem obvious. However, the root causes and solutions are not so easily defined. The humanitarian need for remittances remains critical to most of those receiving funds in this manner; if states such as the US choose to cut this lifeline, larger humanitarian problems will become a reality. How these flows can be used as a means for reducing poverty should also be at the forefront of state thinking.

1. Untraceable cash VS. monitoring
2. Economic lifeline VS. potential misuse
3. Informal monetary transfer system VS. availability of banking facilities in remote areas
4. Humanitarian need VS. criminal activities
5. Innocent Hawala brokers VS. coordinators of criminal and other illegal activities
6. Individual efforts VS. centralized and monitored government vehicles
7. Immediacy of dependence on remittance VS. long-term local development and empowerment
8. Need to identify most needy group VS. resulting vulnerability due to their identification

POLICY RECOMMENDATIONS
1. Develop a means of remittance flows that can be redeemed through legitimate financial institutions
2. Avoid impoverishment that will result from stoppage of remittance flows, which may produce the very insecurity that is being prevented with these funds
3. Develop regional banking facilities, even if this is not possible for every small village
4. Monitor all humanitarian activities with international help if necessary
5. International and national cooperation in monitoring and prosecution of the guilty
6. If regional banking systems are not possible, work on mechanisms for a centralized system of informing individuals of the arrival of the remittance and methods of distributing it, with built-in, strict anti-corruption/extortion measures
7. Work out a short-term solution and develop long-term self-sustaining plans, investigate the potential of remittances as a development tool
8. Protection and facilitation for the most needy groups

POLICY DILEMMAS
© Dr. Nayef R.F. Al-Rodhan
GCSP, 2006
Informal remittance flows are not only a large source of insecurity for some governments, however, as mentioned, they also serve as the very lifeblood for many individuals. Thus, doing away with them totally would render large groups of people incapable of taking care of themselves. How do governments reconcile the aspects of remittances that contribute to global insecurity while still allowing for the free flow of funds that are necessary for sustainability and economic development?

The large dilemmas for states rest in the inability to monitor remittances. Cash flows may be easier to trace, but remittances leave virtually no paper trail in some cases. States should work with those that distribute as well as those that give and receive remittances in order to develop means so that these funds could be channeled through legitimate financial institutions. This would also reduce potential misuse and therefore would avoid the potential poverty that may result from halting remittances flows. This potential disruption (as was the case in 2001 when the US closed Al-Barakat⁷) would have devastating effects in the country to which the remittances are sent.

The humanitarian need for securing the flow of remittances must be carefully balanced with the need to prevent the widespread misuse of this system for criminal activities. This requires that the international community work together with governments, clans, and banks in order to develop effective monitoring solutions. This is also the case when an innocent (in some cases) hawala broker is simply trying to do his job but his efforts are undermined by those brokers who are coordinating criminal activities through their post. This leads to further sources of insecurity within these communities beyond the obvious far-reaching effects of transnational terrorism. International institutions, national institutions, and governments must work to monitor and identify those who are innocent and work within the legal framework of the system. Governments have a responsibility to protect these individuals – and their funds – from harm. Simultaneously, efforts need to be coordinated in the identification and prosecution of those that are utilizing the system for criminal activities.

All of these recommendations address the short-term effects of remittance flows and their impact in dealing with security. Nevertheless, it is also important to also think about how to best shape the remittance system in the future, regardless of the reforms required. Poor populations’ dependence on remittances is clear; however, the international community should also work towards long-term local development and empowerment in the countries where remittances are being sent. For example, micro-loans to women have been phenomenally successful in some instances.⁸ While this seems like a large order for the international community, small changes are happening sporadically in Africa and other parts of the world, but larger international players such as the European Union and the US need to work out these short-term solutions. The focus should then also be on what can be done in
order to implement long-term, self-sustaining plans to reduce the dependence of these communities on remittances.

Conclusion

The number of communities that are dependent on these funds is staggering. Formal systems of transfer and banking have, for a number of reasons, co-existed with these informal networks. Trust has been built within this traditional system due to its informal networks and its reliability in countries such as Somalia, where there are no formal networks available for individual use. With the advent of new technologies that can provide new opportunities for solving some of these dilemmas, states need to find solutions that not only provide security in the system for those wishing to transfer funds but also allow for policing functions, when necessary, by the states involved. Only then will the remittance system help produce long-term stability and security for individuals as well as for states and thus the entire international system.

References

1 In the *Global Economic Prospects 2006* report produced by the World Bank, remittances were specifically addressed. The report stated that “in aggregate, remittances are more than twice as [sic] the size of international aid flows,” p. xi. The report may be downloaded in its entirety at http://web.worldbank.org/external/default/main?contentMDK=20709766&menuPK=615470&theSitePK=612501&pagePK=64218950&piPK=64218883.

2 Ibid, p. 88.

3 Ibid, p. xv.


6 The policy brief may be viewed in its entirety at http://www.gcsp.ch/e/publications/Globalisation/Publications/index.htm.

7 For an entire overview of the US decision to close Al-Barakat, please see http://news.bbc.co.uk/2/hi/in_depth/world/2002/september_11_one_year_on/2219680.stm. Al-Barakat was an informal firm that handled a large amount of remittance transfers for numerous countries at the time of its closure because of alleged links to Al-Qaeda. The disruption in remittance flows had devastating effects for the country of Somalia, a state lacking in formal banking systems.