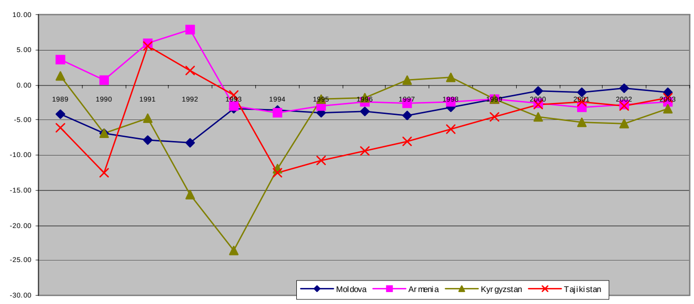
Section 1: Overview of Migration, Remittances and Financial Sector Development

This section takes stock of the patterns of migration in Eastern Europe and the Former Soviet Union, the size and regional distribution of the remittance transfer market and the degree of development of the respective financial sectors.

1.1 Patterns of Migration in Eastern Europe and the Former Soviet Union

Migration has been an important part of the transition process in the former centrally planned economies of Eastern Europe and the Former Soviet Union, and continues as these countries move beyond transition.[2] If movements between industrial countries are excluded, migration in this region accounts for over one-third of total world emigration and immigration. Russia is home to the second-largest number of migrants in the world after the United States; Ukraine is fourth after Germany; and Kazakhstan and Poland are respectively ninth and tenth. Labor migration is likely to gain in importance in view of the ageing of populations in Europe and the high-income economies of the Former Soviet Union.

Figure 1 Net Emigration Rates per One Thousand Inhabitant (1989-2003)



Note: Calculated from a residual method.
Sources: National Statistics Offices (see Appendix 1).

Early in the transition, migration patterns from the low-income CIS countries were fairly volatile (Figure 1). In the early years of transition, large quantities of migration inflows and outflows erupted, as many households took advantage of the lowering of Soviet travel restrictions to move to ethnic homelands or to areas where expected wages, employment opportunities and quality of life were higher. In addition, others moved to escape from conflicts that emerged among and within some of the former Soviet republics.

Migration volatility eased by about 1995 (see Figure 1). Previous to this, Armenia swung from being a net immigration country (until 1993) to a negative migration balance. The Kyrgyz Republic's migration balance also fell sharply negative during the early 1990s, before converging with Armenia and Moldova's net emigration rates of around 2 to 3 migrants per one thousand of population. Tajikistan's migration balance remained between -5 and -10 per one thousand inhabitants before it also converged with the rates experienced in other low-income CIS economies by about 1999.

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[2] World Bank (Forthcoming) *Migration and Remittances: Eastern Europe and the Former Soviet Union*, Washington DC, World Bank.

The majority of migrants from low-income CIS economies travel to middle-income CIS countries (Russian Federation, Kazakhstan, and Ukraine). From the start of transition to 2002, over 90 percent of migrants from Armenia and Moldova traveled to one of the middle income CIS, while 80 percent of Kyrgyz migrants and 87 percent of Tajik migrants relocated there (Table 1). The majority of these flows were to Russia, though sizeable numbers also traveled to Ukraine (see Figure 2).

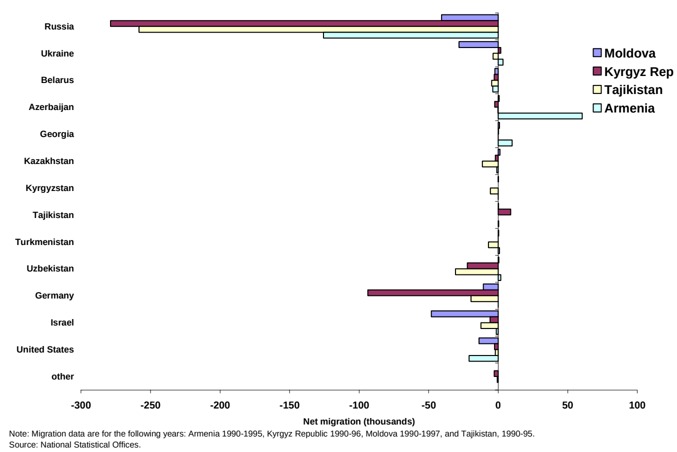
Table 1 Low Income CIS Countries' Migrants Destinations (Percentage of Total Outflows to European and CIS Countries)

	Western Europe	EU8	Middle Income CIS	Low Income CIS
Armenia	0.57	0.49	92.02	6.92
Kyrgyz Rep	11.86	0.11	79.95	8.09
Moldova	0.17	0.35	94.91	4.57
Tajikistan	0.03	0.10	87.98	11.88

Sources**:** National Statistics Offices (see Appendix 1).

There are some variations in migration patterns among countries. A sizeable portion of migrants from the Kyrgyz Republic from 1990 to 2002 traveled to Western Europe (12 percent), particularly Germany. A significant number also traveled within the low income CIS, particularly from the Kyrgyz Republic and Tajikistan to Uzbekistan.

Figure 2 Net Migration Flows for Armenia, the Kyrgyz Republic, Moldova, and Tajikistan



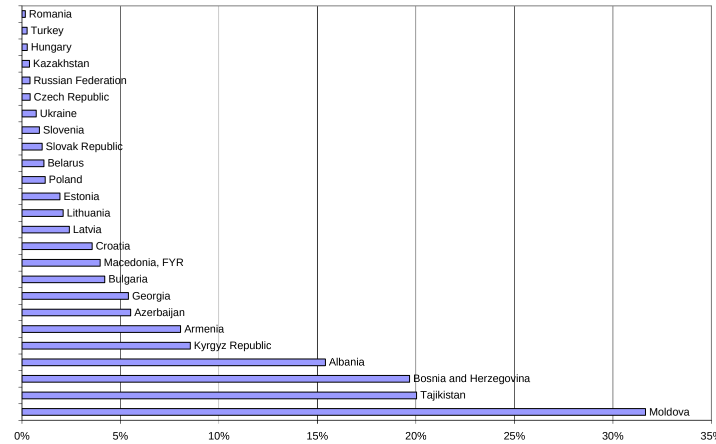
Undocumented migration flows are likely to be important. Undocumented immigration is, by definition, difficult to quantify, although it represents a large proportion of migration originating in the low-income CIS countries. Currently, there is an estimated 3 million undocumented immigrants in the EU, and between 3 million and 3.5 million in Russia. Due to their irregular situation, most labor migrants do not benefit from the same protection rights and do not have access to the formal financial system for the purposes of depositing their income and transferring remittances.

1.2 Patterns of Remittances

Remittance flows in the ECA region are large. In 2004, officially recorded remittances to the ECA region amounted to over US$15 billion, the equivalent of 7 percent of the global total (US$72.3 billion) and 10 percent of remittances received by developing countries.

Many of the world's largest recipients of international remittances are found in the Former Soviet Union, particularly in the low-income economies of the CIS (in % of GDP). Remittances measured in the balance of payments (Figure 3) constitute over 30 percent of GDP in Moldova, 20 percent Tajikistan, and just below 10 percent in Armenia and the Kyrgyz Republic.

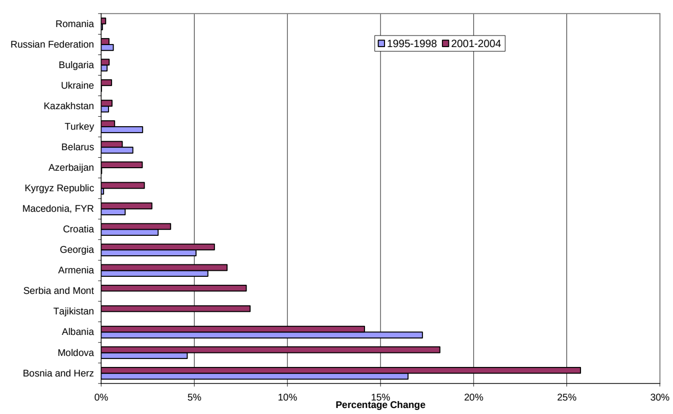
Figure 3 Remittances in % of GDP in Europe and Central Asia (Current US Dollars)



Source: Balance of Payments Statistics Yearbook.
Note: Remittances defned as the sum of received workers' remittances and compensation of employees in 2005 or latest available year. Both remittances and GDP are measured in current US dollars.

The balance of payments statistics may underestimate actual remittance inflows by as much as fifty percent.[3] Surveys conducted by the World Bank found that as many as two-thirds of migrants may send remittances home through transfer channels that government authorities do not or can not monitor -for example, through friends and family or by public transportation drivers.[4] Of the low-income CIS countries, only Moldova estimates remittances sent through these 'informal' channels, perhaps explaining why remittances to Moldova appear so much larger a percentage of GDP when compared to other countries in this sub-region.[5]

Figure 4 Growth Rates of Remittances in Select Europe and Central Asian Countries, 1995-1998 and 2001-2004.



Source: IMF Balance of Payments Yearbook.
Note: Remittances defined as the sum of received workers' remittances and compensation of employees in current USD dollars.
Missing columns indicate that data was not available.

Remittance growth rates have accelerated in the majority of ECA countries during the last five years (Figure 4). In Moldova, remittances from 2001 to 2004 grew by 18 percent, compared to less than 5 percent during the period 1995 to 1998. The growth in remittance inflows in Armenia and

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[3] World Bank (2006) *Global Economist Prospects 2006: Economic Implications of Remittances and Migration*, Washington DC, World Bank.
[4] World Bank (Forthcoming) *Migration and Remittances: Eastern Europe and the Former Soviet Union*, Washington DC, World Bank. Full survey results available at http://www.worldbank.org/eca.
[5] De Luna Martinez. Jose (2005), "Workers' Remittances to Developing Countries: A Survey with Central Banks on Select Policy Issues," Policy Research Working Paper 3638, World Bank.

Tajikistan were also over 5 percent during this latter period of time. In some cases, this growth may not represent a change in remittance inflows so much as the increased use of formal transfer channels by migrants or enhanced government capacity to measure remittances.

Table 2 Source of Remittances to Low-Income CIS Countries (percentage of total remittances inflows)

	EU15	EU8	Middle Income CIS	Low Income CIS	USA & Canada	Other
Armenia	19.85	0.57	11.44	2.78	54.36	11.00
Kyrgyz Rep	34.38	0.94	37.75	0.53	6.45	19.96
Moldova	29.74	0.99	25.60	0.17	30.92	12.57
Tajikistan	26.79	0.91	27.19	9.65	5.27	30.20

Note: Estimated with a Bayesian entropy method (see Appendix 2).
Source: IMF Balance of Payments Statistics and World Bank Staff Estimates.

Remittances to the low-income CIS countries originate from a wide variety of migrant destinations.[6] As Table 2 illustrates, the key destination for low-income CIS migrants are the middle income CIS, which are the source of a large percentage of workers' remittances. Yet, migrants' earning higher incomes in Western Europe and in North America contribute relatively larger proportions of the total inflow into the low-income CIS. Over half of remittances into Armenia originate in the United States or Canada, while over 30 percent of Moldova's remittances originate from North America.

1.3 Distribution of Remittances

Wealthier households receive larger remittances. Table 3 presents estimates of average remittances and consumption per quintile for receiving and for all households for the low-income CIS countries for which household budget survey data on remittances is available[7]. As would be expected, wealthier households receive more remittances. This tendency is prevalent for all countries in our analysis, data quality permitting. Notably, for the lower quintiles, remittances per capita are high, with the exception of the Kyrgyz Republic.

[6] Table 2 presents estimates (through a Bayesian entropy model) and should be treated with caution.
[7] Note that no data is available for Moldova. By contrast, data is available for Georgia.

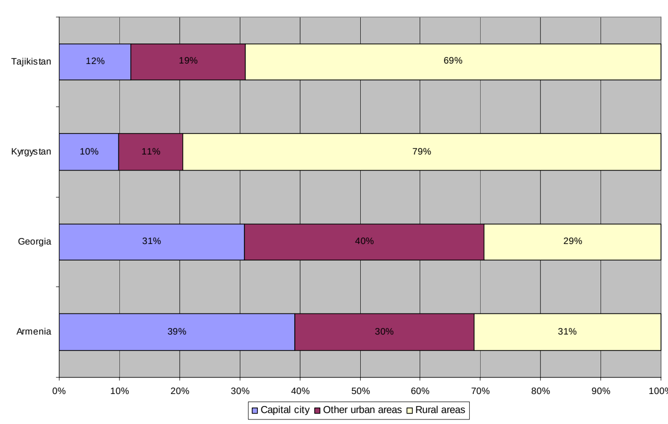
Table 3 Annual consumption and remittances per capita by income quintiles (U.S. dollars)

Income Quintile	1	2	3	4	5
Armenia (2003)					
Consumption per capita (all households)	135.39	194.02	244.81	312.24	547.30
Share of receiving households	16.51%	16.30%	16.40%	17.61%	21.20%
Remittances per capita (receiving households)	67.88	105.36	74.30	112.47	167.51
Remittances/Consumption (receiving households; percent)	50.13%	54.31%	30.35%	36.02%	30.61%
Georgia (2002)(i)					
Consumption per capita (all households)	24.73	46.66	67.38	96.06	193.85
Share of receiving households	2.58%	2.15%	1.83%	1.91%	2.53%
Remittances per capita (receiving households)	35.83	35.76	35.18	50.49	76.57
Remittances/Consumption (receiving households; percent)	144.88%	76.63%	52.21%	52.56%	39.50%
Kyrgyzstan (2003)					
Consumption per capita (all households)	78.31	115.55	148.32	198.93	337.12
Share of receiving households (percent)	0.84%	1.63%	1.38%	3.41%	7.04%
Remittances per capita (receiving households)	7.73	7.14	10.80	41.76	46.02
Remittances/Consumption (receiving households; percent)	9.87%	6.18%	7.28%	20.99%	13.65%
Tajikistan (2003)					
Consumption per capita (all households)	67.20	103.88	139.03	188.13	344.35
Share of receiving households (percent)	8.01%	9.82%	9.33%	8.96%	7.66%
Remittances per capita (receiving households)	23.56	28.12	34.25	41.85	55.68
Remittances/Consumption (receiving households; percent)	35.07%	27.07%	24.63%	22.25%	16.17%

(i) Quarterly.
Sources: Authors calculations; World Bank, Household Data Archive for Europe and Central Asia.

There does not seem to be discrepancies between rural and urban areas for the reception of remittances. Figure 5 shows that the distribution of remittances in-country varies across countries. The majority of remittances are sent to rural areas in Tajikistan (60 percent of total remittances) and the Kyrgyz Republic (70 percent) according to information from these countries' household surveys.

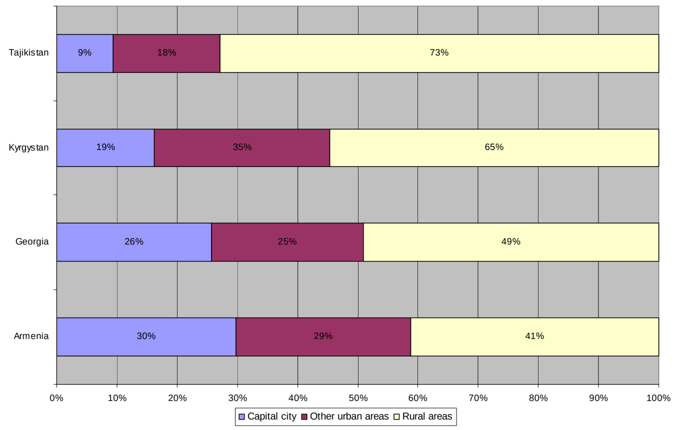
Figure 5 Distribution of Migrants' Remittances in Four CIS Countries (2002)



Note: Tajikistan data from 2003.
Source: World Bank Household Data Archive. World Bank Staff Estimates.

However, only about a third of remittances are send to rural areas in Armenia and Georgia. As Figure 6 highlights, this pattern of remittances mirrors the distribution of the populations of these four CIS countries. This suggests that there is not a rural versus urban divide in the determination of remittances levels.

Figure 6 Distribution of Population in Four CIS Countries (2002)



Note: Tajikistan data from 2003.
Source: World Bank Household Data Archive. World Bank Staff Estimates.

1.3 Financial Systems Development

In the four CIS countries under consideration the status and depth of development of the financial system, varies widely. Table 4 summarizes key indicators of the financial systems and intermediation levels in these countries.

In all four countries financial intermediation, as well as its contribution to the private sector, remains limited. Most of the banking systems, the core of the financial systems in these countries, are privately owned. All are experiencing strong growth in deposit bases and loan portfolios, nevertheless starting from very low levels. The legal and regulatory framework and the supervisory functions are generally satisfactory.

Savings and intermediation levels are low, with deposits to GDP ratios between 10 and 31 percent and loans to GDP ratios between 6 and 27 percent. Furthermore, intermediation is relatively expensive, with nominal (weighted) interest margins generally above the two digits. The product base of banks is also limited, especially in Central Asia.

Table 4 Key indicators of the financial systems

	Moldova	Armenia	Kyrgyzstan	Tajikistan
GDP (N-ccy)	36,755.4	2,228.0	100,115.5	7,300.0
GDP (in US$ million)	2,917.0	4,949.1	2,441.0	2,404.0
Per Capita GDP (in US$)	811.5	1,538.7	478.6	310.0
GDP Growth (real %)	7.1%	13.9%	-0.6%	7.5%
GDP Deflator	7.2%	3.1%	5.6%	7.0%
Unemployment	7.3%	8.1%	3.3%	n/a
Current Account Balance (% of GDP)	-9.8%	-4.2%	-8.1%	-3.6%
M2x/GDP (% of GDP)	43.1%	16.4%	21.3%	16.5%
Money Growth (% in 2005)	35.0%	37.8%	4.7%	21.3%
Banking Sector				
Number of banks	16	21	20	10
Foreign-owned Banks	2	1	7	1
Total Assets (% of GDP)	49.0%	20.2%	21.1%	22.3%
Total Loans (% of GDP)	27.2%	9.9%	7.7%	6.0%
Total Deposits (% of GDP)	30.6%	9.9%	14.1%	12.6%
Total Deposits by Individuals (% of GDP)	19.0%	4.3%	2.7%	n/a
Deposit Growth (% in 2005)	40.4%	17.8%	13.3%	22.1%
Branches	212	269	170	142
ATM Machines	n/a	116	8	17
Dollarization (FX Dep. Over Total)	38.6%	63.1%	79.6%	82.7%
Deposit Rates (US$)	5.2%	4.8%	1.6%	n/a
Deposit Rates (N-ccy)	10.6%	6.5%	4.0%	9.8%
Interest Rate Margins (US$)	5.5%	11.2%	17.1%	n/a
Interest Rate Margins (N-ccy)	6.8%	11.6%	20.9%	13.5%
Portfolio of NBFIs (% of GDP)	1.3%	0.4%	4.2%	0.7%
Clients (.000)	15.5	n/a	264.9	n/a

Source: Central Banks, SIMA and Surveys

The infrastructure to support lending and crediting is generally satisfactory in all four countries. There are credit information bureaus and collateral registries in Moldova, Armenia and the Kyrgyz Republic. However, enforcing contracts and the protection of creditors and property rights are complicated and problematic, and these make banks particularly risk-averse and increase intermediation costs.

Microfinance and NBFIs partly managed to fill the intermediation gap, especially the lowest segments of the population and in the rural areas, where banks do not seem to have engaged to satisfactory levels (limited branches, ATMs, limited housing and retail banking). Dollarization is a common issue in all countries. All countries have liberal foreign exchange regimes, and a relatively high level of dollarization depending on their economic structure and trade relations.

The main formal operators in remittances in the reference countries are: a) banks; b) specialized money transfer operators (MTOs); and c) the postal network. Informal channels are shuttle traders and migrants, which decide to repatriate remittances as they travel back to their homeland. These are discussed in Section 3. An assessment of the informal channels, in terms of volumes, frequency and direction is rather difficult and will not be discussed in this note.