

# Economic Analysis of Hawala Informal Remittances

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Pakistan

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# Why make informal transfers?

Exchange controls: get better exchange rate. Suppose \$1 = PR 80 in official market, but \$1 = PR 100 in informal market, then 25% advantage to use informal market

Capital controls: avoid central bank restrictions acquire foreign assets without permissions

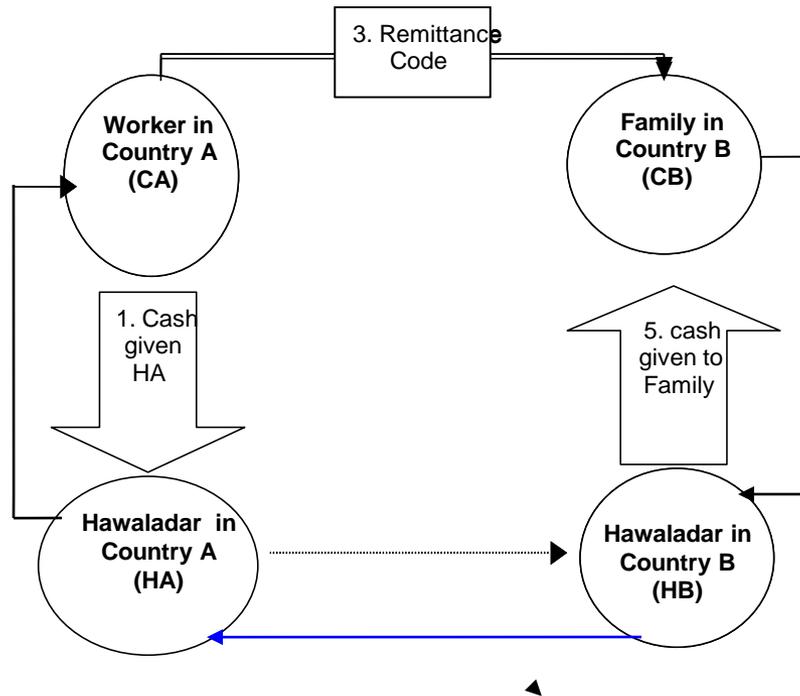
Lack of banking or exchange offices: deliver cash directly to family, NWFP sometimes mentioned

Speed and reliability: e.g., messages by cell phone

- Next: Basic Steps in the Transaction Sequence....

**Figure 1. Prototype Hawala Home Remittance**

**Transaction**



# Financial Steps so far...

## **Four parties: Worker, family, HA and HB**

- Worker in A pays cash (e.g., \$);
- Family in B receives cash (e.g., PR)
- HA (e.g. shopkeeper in London) has received \$, has a debt to HB
- HB (e.g., merchant in Peshawar) has paid out PR, now has a claim against HA
- **NO financial institution** involved so far!
- In balance sheet analysis form....

### 1. Hawala Customer Transactions: remittances to home country

Remittance Senders, Country A	
Assets	Liabilities
- \$	
	-(net worth)

Notes: Net worth of remitter declines

Remittance Recipients, Country B	
Assets	Liabilities
+ LC	
	+ LC (net worth)

Net worth of receiver increases

### 2. Hawaladar Intermediaries

Hawaladar A (HA)	
Assets	Liabilities
+ \$ (cash)	
	+ \$ (HB)

Hawaladar B (HB)	
Assets	Liabilities
- LC (cash)	
+ \$ (HA)	

Notes: HB pays out cash and acquires claim on HA.  
 Net worth of hawaladars unchanged; change in balance sheet composition.  
 Implied foreign exchange transaction.  
 \$ = U.S. dollars; LC = local currency

# IF you could measure Hawala transactions....

- BOP entries would be:

<u>Country A (Remitter)</u>	<u>Country B (Recipient)</u>
<b>Current Account</b>	
Unrequited transfers: (–)	Unrequited transfers: (+)
<b>Financial Account</b>	
Increase in liabilities: (+)	Increase in assets: (–)
<b>BUT, you can't measure these transactions</b>	

# Settlement of Hawala Transactions

- Now HA has a financial liability to HB. How to clear?
- Many possible forms. See Appendix to Paper
- -- reverse Hawala (Table A1.1)
- --through bank account in Country A (Table A1.2)
- --with exports to Country B (Table A1.3)
- --services for HB paid for by HA (Table A1.4)
- --nonbank capital flows (aka capital flight! Table A1.5)

## Settlement of Accounts with Nonbank Capital Flow

Hawaladar A (HA)		Hawaladar B (HB)	
Assets	Liabilities	Assets	Liabilities
-\$ (cash)	-\$ (HB)	+ \$(e.g., equities)	
Entity (inA or elsewhere)		-\$ (HA)	
Assets	Liabilities	Assets	Liabilities
+ \$ (cash.>invest)	+ \$ (HB)		

Notes: HA purchase securities, real estate, etc., in name of HB.

HB trades external claim on HA for these other external assets

Once these steps are done, the transaction is settled and finished!.

# No cash moves across borders!

- Cash movements across borders play no role in hawala remittances. Nothing in the home transfer, or most of the settlement variants, causes physical cash to move across borders. What “moves” are asset and liability positions, that is, bookkeeping entries of the hawaladar participants and related parties. Indeed, the nature of the hawala payments flow—from a remitter to HA (in, say, dollars) and from HB to a recipient (in local currency) is typically domestic, not cross-border. This point is worth bearing in mind because in some countries, purchases of cash dollars in the black or parallel market by the authorities are counted as part of hawala remittances in compiling net inward transfers in the balance of payment statistics.

# Hawala Consolidation

- **Higher level intermediaries.** Settlement of informal remittances is likely to go beyond direct bilateral deals and may well involve several hawaladars located in different countries. It is also plausible there are higher levels of financial consolidation in the hawala chain, that is, a smaller number of players who each take larger positions than the original intermediaries, HA and HB. Hawaladars who have large networks and conduct substantial transactions can play this role, as could individuals/entities not themselves engaged in hawala at all.

# How much Hawala is there?

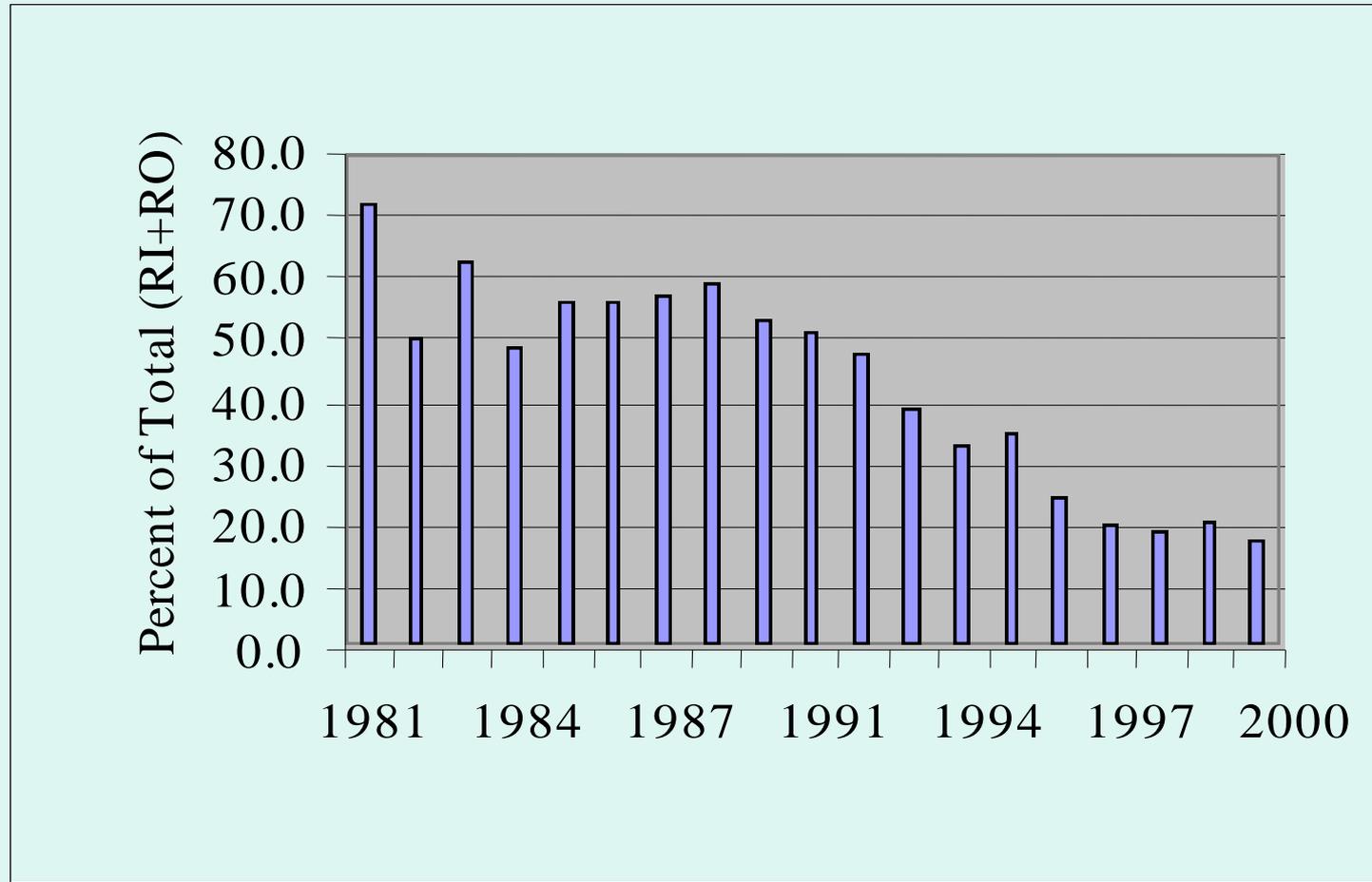
- Some estimates made in 2003 for various countries.
- In this model, Hawala flows depend on the difference between the official exchange rate and the parallel market exchange rate.
- The model is a simulation model, not an econometric model.
- See Appendix to Hawala paper for model details.

# Hawala flow estimates

Table A2.2. Summary of Estimated Private Remittances, 1981–2000

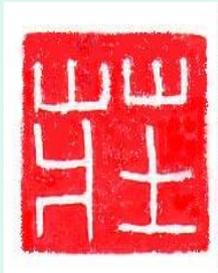
	<u>Total</u>	<u>Recorded</u>	<u>Unrecorded</u>	<u>Share of unrecorded</u>
	In billions of dollars			Percent
Algeria	53	14	38	73
Bangladesh	84	35	50	59
Ecuador	9	7	2	18
El Salvador	23	15	9	38
Guatemala	8	7	1	16
India	143	120	23	16
Indonesia	16	12	4	23
Iran	98	31	70	68
Pakistan	136	62	75	55
Philippines	55	50	5	9
Sri Lanka	23	14	9	38
Sudan	15	7	9	55
Tanzania	19	8	11	58
Turkey	87	72	14	17
Zimbabwe	6	3	3	44
Total	775	457	323	n.a.

# Hawala remittances as share of total transfers for 15 countries



# Thank you

- Can Hawala be discouraged? Yes
- Can Hawala be measured? No
- Time for comment and discussion
- Full paper is available on my website,
- [www.JohnFWilson.net](http://www.JohnFWilson.net)



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