

Competition

and Development

THE POWER OF COMPETITIVE MARKETS

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Competition Research Improves Services

Evidence-based recommendations lead to better money transfer services for Uzbekistan's migrant workers.

For migrant workers all over the world, sending part of their earnings home to support their families and communities is common practice. Until recently, Uzbek workers living abroad paid fees as high as 10 percent to transfer these funds. Thanks to growing competition, those fees are coming down and recommended innovations are leading to more choices for consumers in Uzbekistan.



Sergey Sorokin and Julia Sorokina

One issue that all migrant workers face is how to send some of that all-important paycheck home — quickly, safely, and at the lowest possible cost.

The collapse of the Soviet Union in the 1990s resulted in the creation of 15 small and relatively poor independent nation states, the poorest clustered in the former Soviet empire's Asian territories. Of these, Uzbekistan, with a population of some 27 million, has the distinction of being one of the world's two double-landlocked countries. That is, it is entirely surrounded by countries that have no coastline. Perhaps it is this remoteness from major world markets, combined with the stress of rapid transition to a market economy and an increasingly youthful population, that has made Uzbekistan a major exporter of labour.

Estimates vary depending on the source, but perhaps as many as half-a-million Uzbek workers regularly leave their home country in search of jobs and higher wages. Official counts are much lower at around 266 000, but this statistic includes only those workers who register with the Ministry of Labour and Social Security to work abroad. A large number of "unofficial" migrants simply don't bother to register, according to researcher L.P. Maksakov in the report, *Export of Labour from Uzbekistan*, which puts the total at about 500 000.

One thing almost all the migrants do, however, is send money home. In 2005, estimates placed remittances to Uzbekistan from abroad at about US\$790 million. That is a huge sum in a country that the World Bank estimates had a gross national product of just US\$13.67 billion, and it is more than double the volume of foreign direct investments in the country. While a good percentage of that money goes to provide for families' basic needs — food, clothing, and shelter — considerable sums are used to purchase consumer goods and to improve homes and communities.

Uzbek workers abroad find employment in fields as varied as construction, catering, industry, and agriculture. They travel as far afield as Australia, South Korea, South Africa, and the United States, but by far the largest number — perhaps drawn by the ties of recent history — look for work in Russia. One issue that all these migrant workers face, no matter where they are located, is how best to send some of their hard-earned wages home — quickly, safely, and at the lowest possible cost.

Few have bank accounts

This might seem like a minor issue to people who are used to the conveniences of modern banking, with automated teller machines and Internet-based electronic banking. Uzbekistan, however, was until quite recently a part of the Soviet Union, where only state-operated banks were allowed to exist, with limited services offered to the general public. The only alternative was the telegraph system — operated by the postal service — a slow means of transferring money to other Soviet republics.

Since gaining independence, the Government of Uzbekistan has demonopolized the banking system, transforming branches of the former Soviet bank into 28 independent, commercial banks.

Despite these changes, few Uzbeks have bank accounts, and much remains to be accomplished before these banks fully function as part of the international banking system. They do not participate in the international money transfer system, although they can act as intermediaries between remittance service providers and consumers.

These conditions created a golden opportunity for companies that specialize in international money transfers. The first to get a foot in the door in 2002 was Western Union, the 150-year-old American company that bills itself as “a global leader in money transfer services.” Despite the arrival in the marketplace of two competitors later that year, Western Union cornered 95 percent of the remittance business that year, according to a study conducted by the



David Astley

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Antimonopoly Policy Improvement Center (APIC) in Uzbekistan, with funds from the International Development Research Centre (IDRC).

The goal of the study was to identify anticompetitive activities and restrictive business practices in international money transfer services and find ways to promote a level playing field for participants in the remittance market. Equally important, the results of the research were to be widely publicized in the national media, highlighting the need for more information and greater transparency, as well as the potential opportunities for enterprising businesses.

Competition law enacted

In 1996, the Government of Uzbekistan enacted a competition law that defines any company possessing more than 35 percent of the market as holding a dominant position. That definition drew attention to Western Union's practice of including an exclusivity clause in its contracts with Uzbek banks. Such a clause would represent “abuse of dominance,” the study explains, if it could be shown that Western Union held a dominant market position, which it clearly did, and that the restrictive clause harmed competition, which the researchers concluded it did not, for a number of reasons. These included the steady drop in Western Union's market share and the absence of complaints from either banks or competitors. The researchers also noted that only 13 banks had signed contracts with Western Union, leaving a number still available to contract with competing service providers. Moreover, the researchers pointed out, the clause had not stopped seven of Western Union's partners from entering into contracts with its competitors.

Nevertheless, the Committee on Demonopolization, Support of Competition and Entrepreneurship (CDCE), which is the Uzbek competition authority to which APIC reports, conducted its own investigation into the money transfer business. Committee officials meeting with representatives of Western Union expressed concern over the restrictive clause. The company subsequently nullified the clause in all of its contracts with Uzbek commercial banks.

In their search for transparency, the APIC researchers analyzed the cost structure of the services being offered by the growing number of companies in the field of international money exchange — in 2006 there were 11. Overall, they concluded that “the costs of providing remittance services are much lower than fees charged for transactions.” This was especially true in high-volume corridors, such as between Russia and Uzbekistan. “Western Union’s tariffs have indeed been some of the highest in the market,” according to the research team, but “not monopolistically high.” In fact the researchers concluded that Western Union’s high rates were actually pro-competition, attracting new competitors with lower rates into the market.

Despite Western Union’s initial dominance, intense competition was forcing the company and its competitors to lower their fees. For example, in 2002 when only two companies were in operation, the average fee was a little over 10 percent. In 2006, when there were 11 companies in the marketplace, the average fee had fallen to between 4 and 5 percent. One company even offered a 2 percent rate. Based on those figures, the researchers concluded that competition has saved Uzbekistan’s migrant workers (and their families) as much as US\$45 million. These lower fees leave more money for families to pay for food, clothing, building materials, medical treatment, and medicine.



Karl Freudenthaler

Today, some 3 200 postal outlets in Uzbekistan, two-thirds of them in rural areas, offer international money transfer services.

Research leads to better service

While the situation was improving for migrant workers transferring money home, the APIC researchers made a number of recommendations to promote greater competition within the remittance system. One of their recommendations concerning the postal service, Uzbekistan Pochtasi, has led to action. Because the postal service has a network of regional branch offices and local “postal points” throughout the republic, the researchers said that it could certainly compete with existing service providers. At the time the study was conducted, the postal service had recently introduced an automated system for electronic money transfers within the country, but offered limited international service. At the end of 2007, Uzbekistan Pochtasi formally joined the international financial system of the Universal Postal Union, allowing it to compete in the international money transfer business. Some 3 200 postal outlets, two-thirds of them in rural areas, now offer international money transfer services.

Another key recommendation was aimed squarely at the fledgling Uzbek commercial banks. Under the current system the service providers act as intermediaries between migrant workers and their families, but use the banks as their agents. The researchers pointed out that the Uzbek commercial banks were missing an opportunity to attract clients, who might then be more inclined to open bank accounts and use traditional banking services. In countries with more advanced banking systems, the researchers said, the tariffs on interbank transfers are minimal or non-existent.

“Undoubtedly the development of interbank transfers from one account to another requires the development of partnership agreements between the Uzbek and foreign banks [...]. But the results obtained in the end quite probably will cover all the initial expenses incurred for this initiative,” the researchers observed.

The researchers also pointed out that a large number of credit unions have been formed in recent years, including nine in the capital, Tashkent. There is now also a formal Association of Credit Unions of Uzbekistan. Amending the legislation to allow credit unions to enter the international money transfer market would provide additional competition and more retail outlets, both of which would benefit consumers, the researchers concluded. It would also benefit the credit unions and their members.

The need for transparency and communication

No matter which institution the consumer deals with, there is a need for greater transparency, the researchers said. In addition to the fee charged by the service provider, there are variable exchange rates between currencies, and local agents charge fees to the recipients. This makes it difficult for migrant workers to know exactly how much they need to remit so that their families receive a determined amount in their own currency. The solution the researchers recommended was that service providers provide better information. Details about all aspects of the service offered should be available to consumers, they said, without their need to take any action, such as opening an account or committing to use the service.

The impact the APIC research has had to date — the elimination of the exclusivity clause and the post office's entry in the market — shows that competition research has an important role to play when it provides evidence and recommendations that policymakers and services providers can act on. APIC's success is partly due to the effort invested in communicating the study's results. APIC organized workshops and seminars, and made information widely available to newspapers, television, and radio. Finally, it held a conference in Tashkent in January 2007. The objective was to provide a forum in which to discuss the research results, and to increase public awareness of the issues and of the availability of competitive services.

The conference attracted widespread media attention, and received coverage on central Uzbek television channels, in national newspapers and Internet news sites.

APIC and the CDCE are stronger as a result of this experience, which was new for officials at both institutions. "The impact was felt from top to bottom. APIC — and CDCE — has profited by having worked through its own methodology on analyzing the financial services market [...] which is largely an unexplored field for the Uzbekistan competition authority," the researchers concluded.

APIC's new proficiency in financial services analysis will no doubt soon be called on. There is recent evidence of some consolidation in the remittances market, says Golib Kholjigitov, APIC director and research team leader. "Tariffs have been going down and seem to have reached the lowest possible levels," he says. "Therefore, the most likely scenario would be the starting point of consolidation, and the Uzbek Competition Authority is watching closely in order to prevent price collusion, cartel activities, and unfair practices."

This case study was written by Ottawa-based writer Bob Stanley.

The views expressed in this case study are those of IDRC-funded researchers and of experts in the field.

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