



THE FOUNDATION FOR
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Leveraging Remittances with Microfinance: Timor Leste Country Report

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This report on *Leveraging Remittances with Microfinance: East Timor Country Report* has been undertaken by The Foundation for Development Cooperation (FDC) under the general direction of Craig Wilson (Executive Director). This is the first piece of analytical research work which has sought to estimate the value of inward migrant remittances to independent East Timor and to assess the impact of these financial flows on the livelihoods of the poor. As a pioneering piece of work, the report's scope was deliberately kept finite, noting the limited information available in East Timor, in order to arrive at some defensible interim conclusions within a relatively short space of time. Further research work is warranted, in particular to help define necessary policy responses from the Government, as well as initiatives that the financial sector in East Timor may want to pursue. Future research should examine ways to help facilitate access to overseas work opportunities, grow inward migrant worker remittance flows and reduce transaction costs faced by migrant workers and remittance-receiving households.

The lead editor was Dr Fikreth Shuaib (Head, Research Initiatives) with contributions to data analysis by Ms Joyce Malmo (Project Officer). A leading contributor to the work was Kiera Zen of East Timor Insight Research Laboratory who implemented field survey work, data collation and focus group discussions. This study is part of a wider Australian Research Council (ARC) funded research project on 'Leveraging Remittances with Microfinance: A Cross-country study', being done in collaboration with Dr Judith Shaw of Monash University and Dr Robyn Eversole of the University of Tasmania. The same project also covers Sri Lanka, Samoa, Philippines, Fiji and Indonesia. The results of all six country studies will be published in a combined volume.

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EXECUTIVE SUMMARY

This is the first piece of analytical research work which has sought to estimate the value of inward migrant remittances to independent Timor Leste and to assess the impact of these financial flows on the livelihoods of the poor. As a pioneering piece of work, the report's scope was deliberately kept finite, noting the limited information available in Timor Leste, in order to arrive at some defensible interim conclusions within a relatively short space of time. Further research work is warranted, in particular to help define necessary policy responses from the Government, as well as initiatives that the financial sector in Timor Leste may want to pursue. Future research should examine ways to help facilitate access to overseas work opportunities, grow inward migrant worker remittance flows and reduce transaction costs faced by migrant workers and remittance-receiving households.

Inward remittances received in Timor Leste from migrant workers overseas are estimated to be around US\$5 million per annum or around 1.4% of 2006 non-oil GDP (estimated at US\$356 million). The value of inward remittances to Timor Leste makes labour the country's second largest export after coffee. In the context of other remittance-receiving countries, however, the overall contribution of remittances is relatively small. For instance, in Sri Lanka and the Philippines remittances represent about 10% of the GDP. In the island economies of Samoa, Tonga and Fiji, inward remittances equate to approximately 26%, 42% and 7% of GDP, respectively. In Indonesia, inwards worker remittances are about 1% of GDP.

The majority of remittances are sent through Western Union, with significantly lesser volumes sent through the three foreign-owned commercial banks, in approximate descending order, CGD (Caixa Geral do Depositos), ANZ and Bank Mandiri.

Microfinance institutions in Timor Leste have limited direct involvement in the flow of migrant worker remittances. However, as evidenced from the findings of this study, there is potential for increased involvement of MFIs in the growing remittance transfer market in Timor Leste. Reasons to leverage the involvement of MFIs include:

- general growth of the microfinance industry in Timor Leste.
- growing presence of MFIs in rural and regional areas, and their ability to serve clients in these locations.
- majority of remittance receiving households have an income of less than US\$2/day and are therefore within the market segment targeted by pro-poor MFIs.
- demand for capital for business development.
- some indication by households of the application of remittance receipts for business investment, for instance, businesses selling second hand clothes or flowers.
- increased access to mobile phones (often funded from remittance receipts) and thus the potential for the application of new e-banking technologies to provide convenient money transfer services.

Nevertheless, constraints exist, including the following:

- Western Union is the only licensed foreign exchange dealer, and has secured a significant share of the remittance market.
- the volatile and insecure political environment for business development.
- the absence of a regulatory and institutional framework to support the growth of MFIs.
- limited active public policy support for increasing the migration of excess labour.

Some of the key findings identified in this study are:

- households with one or members who have migrated overseas to work and send home remittances are better off financially by many multiples than households pursuing employment in the local market.
- the transaction costs faced by Timor Lesteese sending and receiving remittances are far above the international average.
- MFIs need to explore their 'legal' rights to be able to transact in foreign exchange. One suggestion is to form partnerships with those already licensed such as Western Union, with a view to serving clients in rural and remote locations.
- programs and initiatives to increase the skills base for Timor Lesteese workers in order to promote continued access to labour markets in developed counties will be valuable.
- government programs to fund potential migrants' travel for overseas employment are necessary to drive the export of labour and grow remittance receipts. Rephrase: pre-departure and travel costs are a significant burden on migrant families and a policy issue for governments seeking to promote remittances.
- the Government's migrant worker program to South Korea should be evaluated in order to identify valuable lessons learnt, and a direction for scaling up its program to both South Korea and other labour receiving countries.
- There is a need to investigate the outreach of financial services in peri-urban and rural areas, with a view to broadening access to remittance services.

1.0 INTRODUCTION

There has been no previous research conducted on migrant worker remittances flowing to independent Timor Leste. Although information remains sketchy, this research has tried to capture details on the value and sources of migrant worker remittances flowing to Timor Leste, their impact on livelihoods at the household level, transaction costs faced by overseas Timor Leste workers and recipient households, the interface of remittance inflows with microfinance institutions, and prevailing policy and regulatory conditions as they affect remittances and the export of labour. This report sets out a series of findings and conclusions and puts forward a number of recommendations.

1.1 TIMOR LESTE - BACKGROUND

Timor Leste is a newly independent country of 14,609 square kilometers in Southeast Asia. The country includes the eastern half of the Timor Island, the Oecussi enclave located within Indonesian West Timor, and the islands of Atauro and Jaco. The official languages are Tetum and Portuguese.

Timor Leste's history has been characterised by more than 400 years of colonial rule by the Portuguese and the Dutch. Following the end of Portuguese colonisation in 1975, the country was colonised by the Indonesian government. With UN support, a referendum was held in Timor Leste in 1999, which resulted in 78 percent of the people favouring independence from Indonesia. The Indonesian armed forces responded with violence and, as a result, up to 85% of the country's buildings were destroyed and a third of the population fled to Indonesia and, in lesser numbers, to countries such as Australia and Portugal.

On October 25 1999, the UN Security Council established the United Nations Transitional Administration in Timor Leste (UNTAET) as an integrated, multidimensional peacekeeping operation responsible for the administration of the country during its transition to independence. On 30 August 2001, the Timor Lesteese people elected a Constituent Assembly. Fretilin, the political party historically associated with the independence struggle, won 55 of the 88 assembly seats. The Constituent Assembly was responsible for drafting Timor Leste's constitution.

While most of the state institutions defined in the Timor Leste Constitution have been established, some are still pending. In existing institutions, high-quality human resources and legal and regulatory frameworks, necessary for the functioning of a market-based liberal democracy, are not in place. The recent breakdown in national security in April 2006 has slowed down the nation-building and institutional strengthening process of the government, and resulted in a call for international assistance. The lack of strong governance and institutional weakness is affecting the socio-economic environment and the possibilities for development and growth. The 2006 IMF Article IV Consultation emphasised the importance of a stable institutional

and macroeconomic environment, highlighting the need to establish proper legal and regulatory framework for business activity, particularly with regard to pending land law and labour legislation.

1.2 Socio-economic background

Key social and economic indicators for Timor Leste are outlined in Table 1.

Table 1: Key social and economic indicators

Population	
Total population	923,198 (2004)
Annual population growth rate (%) in 2004	3.2
Median Age (in years)	15.4
Poverty Level (US\$2/day)	61%
HDI	
Human Development Index	0.512 (2004)
Human Development Index Rank	142 (2004)
Education	
Adult literacy rate in percentage	50.1 (2004)
Health	
Life expectancy at birth (years)	55.5 (2004)
Infant mortality rate per 1000 live births	90 (2004)
Total fertility rate (live births per women)	7.0 (2004)
Economy	
Non-oil GDP total (million \$)	366 (2006) estimated
GDP per capita (current US\$)	732 (2004)
Labour force participation rate	60% (2004)
Unemployment rate, total percentage	8.9 (2004)
Youth unemployment rate, percentage	23.1 (2004)
Main industries	Coffee, oil and natural gas.
Exports	Coffee, oil and natural gas.
Major trading partners	Australia, Europe, Japan, United States

Source: The 2004 Census of Population and Housing Timor-Leste; UNDP Human Development Report Timor-Leste 2006.

The 2004 Census notes the total population of Timor Leste was 923,198. For the same year, the annual population growth rate was 3.2 percent and the total average fertility rate was seven live births per woman. If the present annual growth rate continues, the population is expected to double in approximately 20 years. The median age was 15.4 years and the average life expectancy only 55.5 years. With every 100 people of working age population supporting 96 people of non-working age, Timor Leste has a high dependency ratio.

Sixty per cent of the population survive on less than US\$2/day, and GDP per capita has fallen to about 70% of its 1999 level. At US\$366 in 2004, GDP per capita is one of the lowest in the world. Subsistence agriculture, fishing and forestry accounted for nearly one-third of total GDP in 2004, and employed 70% of the labour force. The service

sector employs 28% (Ministry of Labour and Reinsertion, 2007). Less than one percent of the labor force work in value-adding and export industries such as mining, oil extraction and processing, manufacturing, construction and electricity generation and distribution.¹

Unemployment rates are high, at 8.5 percent (Ministry of Labour and Reinsertion: 2007), which includes the 'discouraged' population no longer looking for work. Amongst the younger population, the unemployment rate is even higher at 23.1 percent (Ministry of Labour and Reinsertion: 2007). Further, it has been estimated that approximately 12,000 young people will be entering the labour force annually until 2010, and thus the unemployment rate is set to grow even further (Ministry of Labour and Reinsertion, 2007). Rural unemployment is relatively low (3.3% in 2001) when compared to urban unemployment (20-21%). However, youth unemployment in the urban region of Dili/Bacau is extremely high, at 43% (Ministry of Labour and Reinsertion: 2007).

1.3 Migration

During Timor Leste's fight for independence, more than a quarter of a million people left the country, fleeing to Indonesia and, in lesser numbers, to Australia and Portugal. Most returned after the formal decree of independence in 2003. However, today there are still 28,000 refugees living outside the country (Hamilton, 2004). Australian national statistics reveal that roughly 9,000 people from Timor Leste are living in Australia (ABS, 2006).

According to US official estimates, in 2002 the net emigration rate in Timor Leste was 51.07 migrants/1,000 people, or 5.1 per cent. Economic stagnation, poverty and unemployment have led many young Timor Lesteese to seek jobs overseas, particularly in Ireland and the UK, via Portugal. Since 2003, tightened visa requirements in Portugal have reduced migration flows through the Portuguese corridor. At the same time, Malaysia has recently agreed to accept Timorese workers. According to the Ministry of Development and Environment in Timor Leste, an average of about 800 young Timorese are leaving the country each year looking for opportunities for further education and/or employment abroad (UNDP, 2005), and this may have a significant impact on future remittance levels.

It is estimated that between 300 and 500 Timor Lesteese workers have independently traveled via Portugal to the United Kingdom and Ireland to work in poultry farms, fish factories and other jobs. This group is thought to remit to Timor Leste mostly via Western Union.

The Ministry of Labour and Community Reinsertion has established an embryonic migrant worker program to South Korea. Per contract stipulation, the 17 workers (20

¹ Timor-Leste census of Population and Housing 2004, p.48-51

initially) sent to South Korea in 2006 in the first phase of this program each remit 85% of their base monthly salary of US\$1,500 (collectively about US\$260,000 per annum). These workers were drawn from an initial group of 1,900 who pre-registered in 2003-2004 for this overseas worker program. There is thought to be a nominal number of Timor Leste migrant workers in Australia, Indonesia and elsewhere.

1.4 Remittances

The Portuguese Caixa Geral de Depositos (CDG, trading under the name of BNU-Timor), the Indonesian Bank Mandiri and the ANZ Bank offer a range of financial services, including overseas transfers. However, this is mainly in the urban areas of Timor Leste, namely Dili and Baucau.

In addition, Western Union has established two outlets in Dili and Baucau catering primarily for private remittances at comparatively high costs. They report to have some 1500 customers.² Western Union is remitting about \$370,000 per month into Timor Leste. Presently, no firm information is available regarding the origin of these remittances, the bulk of which are thought to originate in the United Kingdom and Ireland.

Preparation of this research report revealed the limited extent of information on remittances to Timor Leste. There are no available data which indicate the number of remittances sent by Timor Leste residents who live abroad. However, the government has recognised that remittances from 20,000 people located outside Timor Leste will be a significant income resource for development. Also, possible future labour migration among young Timorese people may increase the remittances to the region.

The 17 workers in the construction industry in South Korea are obliged by their contract to remit 85% of their monthly salary to their BNU-Timor bank accounts. This equates to approximately \$260,000 per annum. The ANZ estimates various forms of worker remittances from Australia of between US\$500,000 and US\$1.2m. Bank Mandiri's inward remittances from Timor Leste workers are negligible. Thus, in total, combined with Western Union receipts from Ireland and the UK, these figures suggest a total annual inflow of migrant worker remittances of perhaps a little more than US\$5m. Informal remittances are thought to negligible in value although there is a reported growth in the use of mobile phones to organise financial transfers between Timor Leste and Indonesia by middle men. Some in-kind remittances were also reported by households in the present study.

² Source: FSSA Report Timor-Leste p.23-24

1.5 The policy and regulatory environment

The Government of Timor Leste has no overarching policy which applies to inward remittances from Timor Leste migrant workers. However, a number of policies and regulations do affect this issue indirectly.

Forex licensing rules and restrictions

Banks are licensed to exchange foreign currency as part of their bank license. Westpac was issued with a foreign exchange licence in 2000 but soon thereafter closed its operations in Timor Leste. Western Union is the only non-bank holder of a currency exchange license and reports at least monthly on its transactions to the Banking and Payments Authority.

Rules on mobilisation of remittance deposits by non-bank Institutions

There remains no non-bank financial institution regulation in effect. Presently, the five principal microfinance institutions self-regulate according to a code of conduct that was struck by the Association of Microfinance Institutions of Timor Leste. The continuing lack of NBFi regulation is a constraint on growth and expansion of microfinance institutions. The publicly held Microfinance Institution of Timor Leste has a limited bank license which caps its deposits at US\$1m and IMFTL has, therefore, been unable to mobilise deposits above this level for the last four years, thus limiting its lending program. *Moris Rasik* has recently reached break even after seven years of operations. Grameen of Bangladesh has been invited to set up an operation in Timor Leste.

Tax treatment of remittances

There is no particular regulation applying to remittances. Although technically income, in the absence of any operable double-taxation agreements inward migrant worker, remittances are not known to be assessed for income tax purposes.

Other policies relating to migration and remittances

- Incentives Related to Migration

The Government has a draft regulation relating to formal programs promoting the migration of labour, with a strong focus on worker safety nets and social protections. Whilst this regulation has not yet been enacted, an overseas worker unit has been established within the Ministry of Labour and Community Reinsertion which is coordinating the first batch of migrant workers sent to South Korea. There are no incentives offered other than salaries more than 15 times the local average.

- Incentives Related to Remittances

At present, there are no incentives related to remittances in Timor Leste.

2.0 THE FINANCIAL SECTOR

The formal financial system of Indonesian Timor Leste was destroyed in 1999. At present, Timor Leste's financial sector is limited in its operational activities including outreach. There are no local banks in Timor Leste. There are currently ONLY three foreign owned commercial banks: the Portuguese Caixa Geral de Depositos (CDG, which owns BNU Timor), the Indonesian Bank Mandiri and the ANZ Bank. There is also one local institution with limited banking licence (IMFTL), Microfinance Institutions (MFIs), credit unions and NGOs. The regulatory and supervisory functions are undertaken by the Banking and Payment Authority (BPA).

2.1 Banks

At present, there are three commercial banks in Timor Leste, all of which are branches of foreign-owned banks. They are:

- ANZ - The ANZ branch was established in 1999-2000. According to the IFC (2007), ANZ is effectively a non-lending institution. Key constraints faced by ANZ in extending its lending services include: difficulties with collateral documentation; absence of notary services and credible financial statements; and other uncertainties in the current legal environment. ANZ has introduced ATMs and EFTPOS (electronic funds transfer services) with participating organisations in Dili. ANZ has a number of plans to extend its banking services to rural areas (such as the mobile banking model), though these have not been implemented yet.
- CGD (Caixa Geral do Depositos) – is the branch of a state-owned Portuguese bank and was established in 1999-2000. CGD acquired the Banco Nacional Ultramarino (BNU) and operates in Timor Leste under the trading name BNU-Timor. CGD is the industry leader in terms of assets, customer numbers and branches. CGD central office is in Dili, with additional six branches located in the districts of: Baucau, Gleno, Maliana, Oecusse, Viqueque and Suai. CGD is the only bank to offer savings deposits to those engaged in informal sector employment and in rural areas (IFC, 2007). The IFC also notes that CGD has a substantial backlog of loan applications. CGD is also acts as a service provider to MFIs (through the provision of banks transfer and deposits) operating in the rural areas of Timor Leste.
- Bank Mandiri – is the branch of a state-owned Indonesian bank and was established in 2003 with a single office in Dili. Bank Mandiri main banking service is related to the provision of financing trade with Indonesia and servicing Indonesian businesses in Timor Leste. The bank rarely provides any credit to micro- and smaller businesses, with almost entirely focused on commercial enterprises. Bank Mandiri has extended a line of credit to the MFI (Moris Rasik) in return for collateral at 100% of the loan value.

The IFC (2007) notes that there is a general growth trend in the banking sector in Timor Leste, particularly the rapid growth of deposits with savings account contributing

almost a third of the total deposits. With savings account being the product of choice for lower-income people, there is projected demand for this financial product in Timor Leste.

Apart from the three commercial banks, Western Union has a 'currency exchange licence'. It has to send monthly reports on its transactions to the Banking and Payment Authority. The Western Union is located in the capital Dili. Clients have to travel to the city office to receive funds when these are remitted from overseas.

2.2 The microfinance sector

The microfinance sector (MFI) is small, but one of its key features has been its resilience to shocks and crisis, and its progress when compared to other donor investments and economic development initiatives (IFC, 2007). The Timor Lesteese microfinance sector consists of the Instituicao de Microfinancas de Timor-Leste (IMFTL), three specialised NGOs, several Credit Unions which were initiated by the Asian Development Bank (ADB) and a number of microfinance programs. Most of these organisations are members of the Association for Microfinance in Timor-Leste (AMFITIL) – the only professional association in the sector. With the exception of IMFTL, MFIs are registered as NGOs. The BPA (Banking and Payment Authority) does not regulate the activities of NGO or MFIs, though it issued a 'limited' license to IMFTL in 2002 to operate as a registered MFI.

Most microfinance activities are concentrated in Dili, Bobonaro and the Cova Lima districts. While IMFTL and Credit Unions provide a wide range of services, including individual and group credit products, as well as saving deposits services. NGO programs focus mainly on micro credit, using group lending methodologies, with some adapting the Grameen Bank model, and others developing self-help groups.

Instituicao de Microfinancas de Timor-Leste (IMFTL): IMFTL was initiated and developed by the ADB under the Microfinance Development Project, with funding from the Trust Fund for Timor Leste. Established in December 2001, it operates through branches in Dili (head quarters), Aileu, Gleno, Maliana and Oecusse. In 2002, BPA issued a license for IMFTL to operate as a registered MFI, but its license is limited to caps on microcredit loan portfolio, amount of deposit maintained and liquidity ratio. According to its performance report to the Association of Microfinance Institutions of Timor Leste (AMFITIL), IMFTL is making profits on its operations, though these are reported to be based on its payroll loan product.

Credit Unions

Credit Unions provide individual loans to members while accepting savings deposits. They operate throughout the country. However, they are small, their systems are weak and accountability is questionable. Despite an attempt by the ADB to rehabilitate credit unions, most are now reported to have collapsed, with only four out of 27 operational.

According to the ADB, some of the constraints noted included: low membership, inadequate capital and limited savings mobilisation, shortage of trainers and technical staff, governance and transparency problems (Conroy, 2006).

Specialised NGOs

Moris Rasik: means 'independent life' in the local language of Tetum. It was established in 2000 with the support of CASHPOR, the network of Grameen Bank replications in Asia, to provide micro credit to poor women in western districts. The financial resources of *Moris Rasik* come from international organisations, including \$70,000 from Touch Community Services and \$100,000 from the Lee Foundation. HIVOS has been the largest provider of funds to *Moris Rasik* over the last six years. *Moris Rasik* is the largest rural microfinance organisation in Timor Leste (with 10,170 loan clients through 13 branches and US\$1.9million loans outstanding) and probably the most successful with a 98% repayment rate. Operational self-sufficiency was achieved in August 2007.

Tuba Rai Metin (in Tetum, 'Feet Firmly on the Ground') is supported by Catholic Relief Services that receive funding from USAID. It runs microfinance programs for women in Dili and in the eastern districts of Baucau and Viqueque through solidarity groups of three to ten members. *Tuba Rai Metin* reached approximately 1,500 clients at the end of 2004. In 2005 *Tuba Rai Metin* signed accord with the Ministry for Labour and Community Reinsertion regarding credit assistance for Timor Leste women's groups.

Other NGO-led microfinance programs include the Christian Children's Fund (CCF), which provides training and technical assistance to groups managing their own credit and savings operations, and Tiimor Aid, which receives funding from the Nobel peace prize of Jose Ramos Horta.

Overall, at present, financial institutions in Timor Leste have only achieved limited coverage. In rural areas of Timor Leste, the majority of households face financial exclusion and lack access to basic financials service such as low-cost deposits, loans and remittances (Conroy, 2006).

In recent times, the level of domestic credit and bank deposits has grown as a proportion of non-oil GDP (Conroy, 2006). This is attributed to the growth the banking industry. According to Conroy (2006) this suggests the excess demand for bank credit and the need to expand savings mobilisation.

Major donor agencies for microfinance activities in Timor Leste have included over time AusAID, the ADB and USAID. Of these, the ADB has played a very significant part with the Microfinance Development Project. In addition to rehabilitating credit unions, the project sought to assist development of a policy and legal framework within which the intended microfinance institution could be developed, particularly in matters influencing the ability to lend to the poor. It also established the IMFTL and provided

technical assistance aimed to improving corporate governance and management operational and financial performance and building a pro-poor client orientation.

Despite efforts from major donors, the microfinance sector in Timor Leste still faces a number of problems:

- lack of financial resources to sustain and develop their operations, particularly the growth of their loan portfolio;
- scarcity of skilled human resources as a consequence of decades of conflict and colonisation;
- weak and nascent financial infrastructure causing higher costs and risks;
- poor physical and legal infrastructure resulting in high operating costs, low self-sufficiency ratios and dependence on donor subsidies; and
- lack of trust which might discourage entrepreneurs to start and expand income-generating activities.

Given the various challenges faced by MFIs in Timor Leste, Conroy (2006) suggests a number of recommendations to help support the sector. These include:

- Institutionalising their presence in the country with attention to sustainability and scale of the organization.
- Self-regulation of MFIs has been identified as an opportunity for the sector. However, the need to strengthen the capacity of AMFITIL to act as a supervisor has been noted.
- Capacity building of individual MFIs has also been suggested. In particular, in the areas of training and management of staff, technical assistance, transport and office equipment.
- Capacity building assistance for MFIs clients, particularly in the area of financial literacy.

Around 11 per cent of the labour force in Timor Leste is 'self-employed' (Ministry of Labour and Reinsertion 2006). Conroy (2006) notes that the potential for microenterprise sector development in Timor Leste is restricted due to limited access to the financial system in general and microfinance in particular; and the deficiencies that exist in the legal and regulatory environment. A World Bank survey also noted that access to finance was a constraint to 81% of the informal enterprises (World Bank, 2005). The World Bank (2006) identified a number of challenges facing Timor Leste, which have implications for the microenterprise sector. These include: critical gaps in land law, land and property registration, leasing and collateral, bankruptcy, business licensing, accounting and auditing, competition policy, intellectual property rights, social security, and key sectoral legislation in areas of important potential in the economy such as tourism, manufacturing and trade.

3.0 RESULTS AND FINDINGS

3.1 Methodology

Three separate instruments have been used to obtain data (structured questionnaires, in-depth interviews and focus group discussions) and these are outlined below. The fieldwork for this study was undertaken in July 2007.

- *Structured questionnaire* A total of 105 questionnaires were administered to households receiving remittances. Due to security concerns most of the questionnaires were conducted in and around urban Dili. Survey respondents were randomly selected based on the 'key informant method'. Of the 105 completed questionnaires, there was only one (1) MFI-client identified. There are only 5 MFIs operating in the country (IMFTL, Moris Rasik, Tuba Rai Metin, Christian Children Fund and Timor Aid), and while most are headquartered in Dili, their clients are mainly in the rural areas.

The questionnaire sought information on the socio-economic and demographic status of the household and the migrant; household income sources and living standards; savings and expenditures; use of financial services; and satisfaction levels related to remittance transfers.

- *In-depth interviews* The quantitative data from the structured questionnaires was supplemented by in-depth interviews with 5 remittance receiving households. Issues raised in the in-depth interviews included accessibility and use of financial services; remittance usage and savings patterns; the motivation for migration; and the household standard of living including asset availability.
- *Focus groups* Focus group discussions were held with households receiving remittances from the UK, Ireland and South Korea. The aim of the focus groups was to ascertain the usage of financial services including information on satisfaction levels, accessibility, and desire for new products.

3.2 Demographic and socio-economic characteristics of remitters

The lack of local employment opportunities and the increased desire of households to seek overseas employment was a common response in the in-depth interviews. There is a significant gender imbalance in the migrant workforce, with men constituting nearly 90 per cent of remitters. Over 80 per cent of remitters have unskilled jobs and only 14 per cent were employed in the skilled categories.

Early all of the sample remitters were based in the UK (67 per cent) and Ireland (29 per cent), with a handful in Australia and Portugal. While some workers have traveled to South Korea, these were not represented among the households surveyed.³ As employment opportunities in Portugal are limited, most migrants with a right of abode in Portugal use their EU passports to travel to the UK and Ireland via Portugal.

³ However, a separate focus group was conducted with family members of migrants in South Korea.

Two thirds the remitters migrated in 2002 and 2003. Only 8 per cent migrated prior to 2002 and 26 per cent migrated after 2003. Looking at the country's history, it would have been expected that a larger number of the remitters would have migrated in 2000 as a result of the violence and struggle for independence. The fact that the majority of the remitters had migrated after independence suggests that migration is a response to persistent unemployment.

Migration costs, reported by respondents to be around US\$3,000, are a significant constraint for the households. The costs were mainly met by family members. The lengthy and costly process for obtaining official documentation for migration was also cited as an additional constraint.

More than 85 per cent of respondents stated that they did not know when the remitters are expected to come back. This suggests that migration patterns from Timor Leste could become permanent and not result in a return of skills acquired overseas. Unless there is a continuous stream of economic migrants from Timor Leste in the near future, the sustainability of remittance flows could also be threatened. Unlike remittance transfer to Samoa (which are largely based on cultural links of the fa'samoa and extended family system), remittance flows to Timor Leste are based on economic links. In the latter, remittance transfer will only continue over the long term if there are direct links with migrants and to their immediate families back home. Most remitters (56 per cent) are children or grandchildren of the household head and 24 per cent are spouses. The remainder were siblings and other relatives.

3.3 Demographic and socio-economic status of remittance recipients

Two thirds of the recipients had/have more than five persons living in their household, consistent with the national average household size.

More than 61% of the respondents had an annual household income of US\$ 5,000 or less (Table 2). This figure corresponds to the 2004 national poverty level statistics (US\$2/day), and this confirms the persistence of poverty amongst households in Timor Leste.

Table 2: Estimated annual household Income

Estimated annual household income (in US\$)	Per cent
<=5,000	63
5,001 – 10,000	24
10,001 – 20,000	12
20,000+	1
Total	100

Other significant characteristics of recipient households include low rates of employment of other household members. Only 22 per cent had a permanent job, and 12 per cent were unemployed. In addition, some households had members undertaking casual work or who were self-employed. These figures highlight the severity of the lack of employment opportunities in Timor Leste, and large numbers of ‘discouraged’ workers. This could be one of the triggers for the desire to seek overseas employment with a view to sending back remittances to help the family economically.

3.4 Remitting behaviour

Around 43 per cent of the respondents receive remittances every month. This suggests that these households are dependent on remittances as a regular source of income support. A further 28 per cent receive remittances occasionally, usually to cover expenses related to funerals, weddings and similar social obligations.

In two thirds of cases, the respondent is the main decision-maker on how the remittances are saved or spent. The majority of the respondents (53 per cent) indicated that they normally the highest frequency was also noted for this remittance amount (Table 3). This suggests that remittance amount is generally small and sent in frequent intervals. This tends to raise the cost of remittance transactions.

More than half of the respondents (53 per cent) indicated that they normally received a remittance amount/size between US\$50 and US\$300 each time (Table 3). This suggests that remittance amount is generally small and sent in frequent intervals. This tends to raise the cost of remittance transactions.

Table 3: Usual size of remittance

Remittance value	Per cent
50 – 300	53
301 – 600	31
601 – 1000	10
1000	6
Total	100

There appears to be some correlation between the frequency of remittances and the occupational categories of remitters. For instance, unskilled migrants tend to remit more frequently than skilled migrants, suggesting the use of remittances for day-to-day consumption in low-income households.

In addition to cash remittances, 40 per cent of households reported receiving in-kind remittances. Of those responding, the main type of goods received were telephones, clothing and jeweler. Nearly a third of the respondents reported that they had obtained a mobile phone after receiving remittances. This was the single most notable asset that households had acquired since starting to receive remittances. Three respondents received a sewing machine.

While around a third of households reported that there had been no change to the amount and frequency of remittances received, almost 25 per cent reported an increase over time in the amount and frequency of remittances received. About a fifth% of households reported fluctuations over time (both increases and decreases), while 10 per cent reported that remittances had decreased, and 10% that they had ceased altogether.

3.5 Remittance usage

Around 45 per cent of households reported using remittances to support daily routine expenses. Other common uses of remittances included housing improvements (41 per cent), school fees (30 per cent) and loan repayments (10 per cent). It is notable that over a third of respondents had used at least some of their last remittance payment for business expansion or investment. These businesses included second hand clothes and flower selling.

Half of the respondents reported saving from their monthly earnings. The majority (60 per cent) of those saving money saved, on average, between US\$50-200 per month. Three quarters of those who responded are saving money for education/school. Other savings priorities were housing improvements (reported by 35 per cent of savers), weddings and funerals (18 per cent) and business investment (10 per cent).

These results are confirmed by the findings from the in-depth interviews. On the whole, remittances have positive impacts on the households, contributing to a wide range of household needs and expenses. In particular, remittances have contributed to meeting basic household expenditures, housing improvements, business expenses/investment and education. Further, remittances have also contributed to household emergency needs, savings and loan repayment. An additional element evidenced from the in-depth interviews has been the use of remittances for funding other household members to migrate.

It is clear that remittances have contributed to improved living standards and financial security for many households. Nearly a half of respondents reported spending more money on education as a result of receiving remittances, 29 per cent reported spending more on food, 27 per cent on housing improvements and 24 per cent on clothing. Nearly a quarter reported increasing their monthly savings allocations as a result of receiving remittances.

Boxes 1 and 2 illustrate the stories of two households receiving remittance from respective spouses working in England and Ireland. The stories highlight the importance of remittances to these households and the many positive benefits derived.

Box 1: Spouse of a remitter from the United Kingdom

I used to work at the National Hospital and earn US\$250.00/month. My husband never worked. He used to stay at home. He only had completed high school, and had no chance to find jobs. I supported the family. It was decided that my husband should migrate overseas to help support the family with daily expenses. We were also influenced by our neighbour who had relatives overseas, and had sent money back to Timor Leste.

With my husband sending back money now, our monthly expenditures are less, and we can afford to save more too. Some of that money is saved for education of our family members, some used to fund my husband's brother to migrate overseas as well. We were also able to buy a TV and a satellite dish, but we still can't afford to invest in land or a house.

Since my husband left for overseas, a further 10 from our village have followed him. Migration is a good experience, but one needs skills to migrate. So I strongly encourage training before migrating.

When I speak to my husband, I do not find anything worrying me. He is OK, sometimes he writes to me, sometimes via phone. He sounds OK. He never fails to send me money every month.

Box 2: Spouse of a Remitter from Ireland

My husband could normally only earn US\$120 per month if he stayed in Timor Leste. This all will be spent before the end of the month. In addition to this monthly income, we ran a small business selling second-hand clothes. That was before the 2006 crisis. But the crisis killed everything including our business. And we all faced an uncertain situation here.

With limited income, our monthly expenditures went stretched. We had no chance to save for our children's education. Then we decided that my husband should migrate, and this decision was supported by his parents, and his brother who migrated earlier. His brother is also in Ireland found him a job, and asked him to come quickly. The migration cost us US\$3,000.00, and it took nearly 6 months to get all the required documents organised including passport, birth certificate and others. That is why not many people can afford to send their family members abroad. In my village, there are only two remitters. Although people know the advantages of working abroad, most find it difficult to finance the overseas travel.

Migration experience was a positive one for us. We can now save some money in Bank Mandiri (up to US\$1,000), and the service is easy and fast. We can afford to run our business again (once we find space), we can send kids to school as well as some relatives to schools in other districts. We also are thinking to send his brother out as well. So you already can see number of benefits and opportunities of migration and remittances. By staying here, we can only work for US\$2 per day. To be honest, before he went we were facing lots difficulties. And after three months of his departure, it seems like life is much easier than before. Yet, we still could not invest in land or housing.

I can't see any negative impacts of migration, only positive ones. Though it was initially meant to be of support to the family's monthly expenditure, it is more than that now. That is why we want to send my brother-in-law soon. I guess they all prefer to go to Ireland, so they will be there together and look after each other too.

3.6 Remittance transfer methods

The commercial banks in Timor Leste have only been able to secure a limited market share of the remittance transfer market. The majority of households (86 per cent) identified Western Union as the financial organisation handling remittance transfer in the area. All respondents received remittances in the form of cash. None of the households deposited the remittance into a bank account, even though just over a third reported having at least one household bank account. Only one household had a bank account with a microfinance institution; the remainder were with commercial banks. Fewer than 5 per cent of respondents reported dissatisfaction with respect to the convenience, speed or reliability of remittance transfer services. As evidenced from this data, it would seem difficult for new players entering the remittance market.

4.0 CONCLUSIONS AND POLICY RECOMMENDATIONS

4.1 Conclusions

In general, the potential for leveraging remittances by the microfinance sector in Timor Leste looks promising. The following describes the supportive evidence for this:

- Inward remittances to Timor Leste are estimated at around US\$5 million per annum (1.4% of 2006 non-oil GDP). With many new labour markets being accessed by migrants in a more formalised way (e.g. migrant worker program to South Korea), the value of remittances sent back to Timor Leste is likely to increase in the future.
- On the whole, remittances have an enormously positive economic impact on the sampled households, contributing to a wide range of household needs and expenses. Remittance-receiving households are much better off than those without access to a remittance-sender.
- Remittances have contributed to meeting basic household expenditures, housing improvements, business expenses/investment and education. Further, remittances have contributed to household emergency needs, savings and loan repayments. Remittances have also contributed to funding other household members to migrate. These findings indicate that the migrant's rationale for sending remittances to Timor Leste is embedded in the need for supporting household income, both for consumption and investment related activities.
- The findings also indicate that 34% of households used their last remittance payments on business expenses. This indicates that the potential for development of the microenterprise sector based on remittances is significant, particularly in the context of high urban youth unemployment. This also reinforces the government's objective of adopting a private sector-led growth strategy.
- All the remittance-receiving organisations are based in the capital Dili and other major urban centres. Although this study did not focus on rural and regional areas, it is understood that many recipient households in rural and regional areas incur significant costs traveling to Dili to collect remittances sent from abroad. Thus, if MFIs embrace remittances as an additional value-added product/service, those

operating in rural and regional areas would have a natural advantage in capturing more customers with good cash flow.

- In this study, almost 29% of respondents reported obtaining a mobile phone after receiving remittances. MFIs using technology such as mobiles phones to reach their clients in rural and remote areas have proved to be successful. Thus, the potential for replication of e-banking technologies such as the G-cash model in the Philippines for remittance-related services is significant in this context.

4.2 Policy recommendations

Since the MFIs in Timor Leste do not have licences to engage in foreign exchange or the option to apply for licences, MFIs should consider forming partnerships with others to leverage their products and services. Initially this would primarily be with Western Union, and to a lesser extent with the three commercial banks in operation.

Transaction costs for sending remittances to Timor Leste was noted by respondents to be high (20% of amount sent). There is little information available on the transaction cost for remittances in Timor Leste, but the data from the surveys, interviews and focus groups suggest that these costs are high relative to other remittance receiving countries. This has particular implications for those remitters who send smaller amounts and on a frequent basis. Hence, there is a need to investigate this issue further with view to identifying mechanisms to reduce transaction costs. For instance, this may involve direct negotiations by the Government with remittance service providers in the main migrant destination countries such as the UK and Ireland. Government intervention in this process may be effective in collaboration with the financial sector.

Presently, the skills base among Timor Leste migrants is relatively low. If they are able to enhance their skill levels, they could perhaps be able to access higher paid overseas labour markets. This could in turn increase the value of remittances sent home by these migrants. Further, increased skill levels would also tend to increase the financial literacy of these remitters, and hence their ability to advise their households on potential investment in the microenterprise sector.

Accessing funds to travel overseas for work remains a significant challenge, with some families waiting for other migrants to send back home remittances to finance the travel of other potential migrants. In this regard, the provision of government, donor or private assistance through migrant travel loans could be a valuable service.

An evaluation of the Government's migrant worker program to South Korea would provide valuable lessons learnt, and a direction for scaling up its program to both South Korea and other labour receiving countries.

This study did not show the accessibility of households to remittance services outside of urban Dili. Though Timor Leste is rapidly urbanising (with 40 per cent population growth in Dili between 2001 and 2004), it would still be useful to investigate the

outreach of financial services in rural areas, and the ability for MFIs to deliver remittance-linked services.

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