For presentation at a World Bank/DFID International Conference on Migrant Remittances*: Development impact, opportunities for the financial sector and future prospects*. London October 9th and 10th 2003

Processes of consolidation and settlement in remittance-driven Hawala transactions between the UK and South Asia

Roger Ballard
Centre for Applied South Asian Studies
University of Manchester

Migrant remittances are very big business indeed. In addition to the $72.3 billion worth of remittances which Rathore (2003) estimates were transferred to the developing countries through formal banking channels in 2001, there are good reasons to suppose that funds worth at least as much again are transmitted in parallel to this asset flow through more informal channels such as IVTS and hawala. Not only are these transfers substantially higher than the total flow of official assistance to the developing world, but they are particularly beneficial in terms of economic development. Besides incurring no debt, their recipients are not only particularly heavily concentrated in some of the least developed regions in Africa, Asia and Latin America, but are for the most part resident in rural areas, and more often than not in those where development has hitherto been particularly sluggish.

Moreover migrant remittances and economic development are – or at least should be – two sides of the same coin. As far as migrant workers themselves are concerned, the central purpose of remitting a substantial part of their hard-won earnings back home is to invest in a better future, both for themselves and their families. Whilst remittances may indeed serve to meet their subsistence needs, that is very rarely the central goal of the whole operation, especially when migrants manage to penetrate metropolitan labour markets, where wages are dramatically higher than they are at home. Hence the vast bulk of transnational remittance flows are investment oriented, and destined to be put to use to construct a fine new house to house the entire extended family, to purchase additional more land and agricultural machinery, to dig new wells, to finance a local business enterprise, and if immediately profitable investment opportunities are not available in the immediate vicinity of the remitter's home base, to be placed on deposit at the highest available rate of interest. To be sure the development potential of these capital inflows is at present all too often far from fully realised (Ballard, 2003); what cannot be gainsaid, however, is the immense *potential* for economic transformation in otherwise seriously under-developed regions which these capital transfers represent. If so, one of the most urgent policy priorities in this sphere should be to take urgent steps to enhance that potential, and to do everything possible to remove the obstacles which currently inhibit more positive developments.

1 My own approach to the issues

In sharp contrast to the economists, bankers and security experts who have generated the greater part of the recent spate of literature on remittances in general, and Hawala/IVTS in particular, my own involvement in these matters has arisen from my long-standing anthropological interest in the dynamics of one specific instance of these processes: the flow of labour migrants from South Asia to Britain, and the consequent counter-flow of remittances sent back by settlers to their villages of origin. However my knowledge of these issues was further enhanced as a result of being instructed to act as a defence expert in a series of cases in which Customs and Excise had charged a number of wholesale hawaladars operating in major centres of Indian and Pakistani settlement in Britain with being engaged in a conspiracy to launder money.

It follows that my perspective on the Hawala system highly specific in character. Not only is it very much from the bottom up, but in empirical terms it is largely restricted to a that part of the multi-stranded network of global value transfers which became engaged in the process of facilitating the delivery of funds to destinations in northern India and Pakistan. But whilst my detailed prior knowledge of Indian and Pakistani migrants' settlement strategies, as well of their practices and priorities with respect both to the making and investment of remittances was undoubtedly of considerable assistance to the defence team, my role as an expert also provided me with an unprecedented opportunity to make a detailed exploration of Hawaladars' business methods, and on that basis to gain an insight into the way in which the contemporary global Hawala system actually operates.[1] This paper seeks to build on that experience to provide an analytical view of Hawala/IVTS which will, I trust, complement the existing literature on the subject, the greater part of which has been generated by economists.

In the upshot my efforts to assist the court – and most especially the jury – to understand how Hawala systems actually operate about bore relatively little fruit: in general Customs and Excise secured the convictions which they were seeking. However the very experience of being instructed to act as expert witness also enabled me greatly to deepen my knowledge of the way in which the whole hawala system operated, since by doing so I was also able to gain access to all of the hawaladars' records – which turned out in every case to be very extensive – which Customs and Excise had impounded in the course of their investigations.

Hence this paper is based on the one hand on my own extensive ethnographic knowledge of the communities from which the Hawaladars and their customers were drawn, and on the other on the rich seam of information into which I was able to tap as a result of being able to examine the records of a series of major wholesale Hawaladars, who were between them participated in the overseas transfer of funds worth well over £600 million during a period of approximately two years. As a result of doing so I have been able to generate a far more complex understanding of the contemporary organisation of global hawala transfers than that set out in any of the existing literature, including that set out in the recent IMF/WB report on Informal Funds Transfer Systems (El Qorchi *et al* 2003).

2 Hawala as a system of consolidation, de-consolidation and settlement

As the vast bulk of the current literature quite correctly indicates, Hawala is essence a system of swaps. Moreover it is a system of swaps with which the staff of foreign exchange department in any international bank will be entirely familiar. If they can contrive to match their receipts of currency A from remitters with payments out in the same currency to local recipients with a parallel set of payments, both out and in, denominated in currency B at some distant branch in another country, the Bank can maximise its profits, for it can avoid the cost of settlement. However as every international banker is well aware, operations in the real world are far more complex. Even though the sum of all foreign exchange transactions on a global scale must by definition be zero, given a multiplicity of currencies, a multiplicity of foreign exchange operations and a huge daily volume of individual transactions, the books of any one institution, no matter hw vast it may be and how global its reach can at the end of the

[1] The basic document on Hawala which I prepared for use in the courts can be found at http://www.art.man.ac.uk/CASAS/pdfpapers/hawala.pdf

day only be balanced by engaging in an extremely complex – and necessarily expensive – process of consolidation and settlement with other like operators.

Contemporary remittance-driven hawala operates in just the same universe – and consequence can only proceed by constructing settlement processes which are identical in structural character – although not in organisational terms – to those deployed by more formally constituted international banks. Nevertheless from the customers' perspective the operation could not look more different. In the first place Hawaladars do not operate from within expensive marble-clad banking halls: on the contrary their central premises are a great deal more modest, and the system can be accessed through a multiplicity of agents, many of whom offer hawala services as a side-business within a small local grocery store or a travel agency. Moreover the transaction itself is much more informal. The Hawaladar and his customers are usually members of the same small ethnic colony, so they are in no sense strangers to each other. Having established the sterling cost of the rupee sum required, the customer hands over his payment – invariably in cash – supplies the name, the address, and a few additional personal details of the recipient to whom the payment is to be delivered. The funds are normally available within 48 hours, and may either delivered in person to the recipient, or failing that available for collection at the office of a nearby distributing hawaladar – no matter how remote the recipient's place of residence may be.

From its users' point of view the system has everything to recommend it. The process of sending money is simple and straightforward, and involves a transaction routed through someone whom he already knows, and is not only extremely safe but is also provides a delivery system which is far swifter, and a great deal more straightforward than that provided by a formally constituted Bank or a specialist money transmission agency such as Western Union. Best off all the exchange rate offered by Hawaladars is frequently significantly better than the 'official' rate offered by the Banks, and the commission – if charged at all – is rarely much more than 1%. In straightforward commercial terms hawaladars offer an extremely good financial deal. Although the great majority of the transactions involve transfers ranging between a few hundreds to a few thousands of pounds (i.e. small sums in foreign exchange terms), the cost of transmitting funds through the Hawala system – thanks amongst other things to intense competition between rival Hawaladars – is but a small fraction of those incurred by those foolish enough to use the services of MoneyGram or Western Union, let alone the services of a formally constituted bank.

Yet just how do hawaladars manage to achieve such a striking position of competitive advantage? The answer – as I soon discovered once I gained access to their records – was that although they use exactly the same procedures of consolidation and settlement as those deployed in the formal banking sector, they dramatically reduced their overhead costs by replacing formal bureaucratic procedures with relationships of personal trust whenever and wherever they possibly could. As a result their operation was far more efficient, so much so that they could still make a profit even though their fees were dramatically lower. However despite widespread suggestions that 'Hawaladars keep no records' I soon discovered that this was not at all the case. Indeed given the large number of individual transactions which major Hawaladars processed, let alone the scale and complexity of the settlement processes which were integral to their execution, there is no way in which the system could operate as swiftly and efficiently as it did in the absence of formal records. Indeed it was precisely by tracing through those records – significant proportion of which are held, paradoxically enough, in the formal banking sector – that I began to appreciate the scale and sophistication of the system's consolidation and settlement processes. This is by no means a 'system without records':

indeed there would be no way in which global IVTS (of which Indian Ocean based Hawala operations are but a local component) could process a flow of funds in the order of $80 billion per annum in their absence. What I did notice, however, was the record-keeping was parsimonious and therefore highly efficient, since Hawaladars only kept records of the information which they and their immediate partners needed to have access in order to process the transactions in which they themselves were involved. All other information was treated as superfluous.

3 Hawala in practice

How, though, did all this work out in practice? If we begin with the driven remittance arm of these processes, the lowest rung in the operation is one in which local hawaladars take in deposits in hard currencies (£ sterling in my case), takes down details of the person to whom an agreed upon sum of rupees is to be delivered in India and Pakistan, and then transmit (usually by fax but sometimes by email) a tranche of details of rupee payments to be made to specific recipients to a series of partner-distributors in India and Pakistan. An examination of those faxes not only enables on to identify the sender of each payment, but also provides a wealth of detail about the precise location of each recipient. However it is also worth noting that only a small proportion of those taking in payments in the UK actually faxed instructions overseas in this way. Instead the vast majority of those who did so were (often unbeknownst to their customers) acting as agents for hawaladars proper, who typically ran considerably bigger operations from the heart of one or other of Britain's major South Asian settlements in Britain. In other words what we find right at the bottom of the system is a complex network of agencies and sub-agencies whose central role is to funnel in a large number of instructions of the kind outlined above to the hawaladar proper, who is then able to take advantage of very substantial economies of scale by bundling whole tranches of instructions together in a single fax, a series of which are then sent off to specific partners in India or Pakistan. As we shall see, consolidation is a key to the success of the whole operation.

However as El Qorchi and his colleagues make clear, there is very little prospect of deals of this kind being settled by a simple bilateral swap. In the areas of high emigration to which the bulk of such remittances are despatched there are few, if any, customers seeking to exchange rupees for £ sterling or $US. Settlement is a much more complex process, as is evidenced by the fact that virtually all the cash deposited with Hawaladars in the UK is (or at least was) normally bulked up into large tranches, usually somewhere in the region of £100,000, deposited with a local bank, transferred from a £sterling to a $US account, and promptly despatched by TT to an account in a major institution such as Bank of America or Midland Marine in New York. Part of the logic for all this was quite clear. Those Hawaladars whose business credentials were accepted by the manager of a local Branch of a UK bank were not only able to set up foreign exchange accounts which could handle such a daily volume of business for at a relatively low rate of commission, but also to negotiate reduced deposit charges by undertaking the task of counting and bundling the currency notes on an in-house basis. Clearly the more these operations could be consolidated, the lower the transaction cost became, with the result that only a minority of the Hawaladars engaged in sending faxes to remittance distributors in South Asia (whom I shall describe hence forth a retail hawaladars) had access to such foreign exchange facilities. Hence in yet another layer of consolidation, anywhere between eight and fifteen of these retail hawaladars channelled their funds onwards through a wholesale hawaladar (of whom there appear to have been somewhere between 15 and 20 serving the South Asian market in the UK), who in turn converted the funds into $US and sent them on to New York – and rather less frequently to a range of other overseas destinations, although these were rarely if ever located in South Asia. Just as in the case of the retail hawaladars' faxes to their distributing partners in India and Pakistan, there were voluminous records of all these transactions, since the account number and beneficiary of each such transaction was recorded in detail in the wholesale Hawaladar's bank statement.

Nevertheless to those observers unfamiliar with settlement processes, this whole scenario appeared to be highly suspicious. Huge sums of cash were delivered to wholesale Hawaladars on a daily basis, allegedly from a network of retail Hawaladars, as well from an even larger network of agents and sub-agents; but when the cash finally met the formal banking system it was transmitted not to India or Pakistan, but overwhelmingly to New York. The only sensible explanation for transactions on this scale – so HM Customs and Excise argued – was that this whole operation was in fact a major exercise in money-laundering, to which the sending of remittances to India and Pakistan merely provided a conveniently obfuscatory front.

Whilst there is no way of gainsaying the fact that the validity of this argument was accepted by the juries before whom this case was made, with the result that the Hawaladars on trial are currently serving lengthy jail sentences, there nevertheless good reasons for proceeding with my analytical arguments. Even if the retail hawala transactions were indeed no more than a convenient cover for money laundering and terrorist financing (an issue to which I will return once again below), serious issues still remain. Given that Hawaladars hardly sent any funds at all to Pakistan, how was it that their distributor hawaladars in India and Pakistan were able to pay out very large sums in rupees to the nominated recipients? After all they were not in the business for charity's sake.

To any international banker there is an obvious answer to this conundrum: there must be a process of settlement going on somewhere or other. Moreover the more closely I examined the hawaladar's record, the more I was able to bring an outline of these processes into focus, as well as the identity and location of the brokers who put them together. The vast majority turned out to be located in Dubai. With that in mind let me introduce a third level of hawala operator, whose swaps more or less match (at least in structural terms) the simple bilateral settlement model set out in most of the current literature. However such *global* Hawaladars have no contact whatsoever with the relatively tiny sums remitted by labour migrants. Instead such hawaladars characteristically broker deals on behalf of lower-level hawaladars, both wholesale and retail, and also on behalf of large commercial clients. Such deals are very large: since the minimum unit of account in such operations appears to be US$ 100,000, there are good reasons to believe that each of the swaps so brokered will be in the multi-million dollar range.

4 Hawala as a vehicle for settlement

Yet just how much evidence is there for the actual existence of global hawaladars, given that as far as I am aware there is no mention whatsoever either of them and or of such settlement activities in the current literature? My own response to this question is two-fold: partly theoretical and partly empirical.

In the first place it is quite clear that if the annual outflow of migrant remittances from the developed to the developing world through informal channels is of the same order of magnitude as $US 80 billion per annum outflow through formal channels, then there must also by definition be a similarly sized counter-flow of value by way of settlement. But whilst the IMF Report outlines a range of possible means whereby the necessary settlement processes might be implemented (El-Qorchi *et al* 2003: 14 - 17), the authors make no effort to explore how, where and by what means settlements on the massive scale required are achieved in practice; and whilst I would not suggest for a moment that my bottom-up perspective can allow me to gain a comprehensive grasp of what is happening in the financial stratosphere, the empirical material to which I have managed to gain access has enabled me to make a considerable degree of empirically grounded progress towards doing so.

The window of opportunity through which I have been able to peer was nevertheless very narrow, since I have only had access to UK wholesale hawaladars and their records.[2] Nevertheless it soon became clear that a number of Pakistani-owned Exchange Houses in Dubai played a key role in the settlement process: it was precisely in the course of negotiations with these settlement houses (and/or their agents) that wholesale Hawaladars in the UK were drawn into deals which enabled the delivery of bulk payments in rupees to their delivery hawaladars in South Asia to matched with the transmission of an equivalent sum in US dollars to New York. Hence UK-based wholesale Hawaladars daily dealings entailed close coordination along three quite separate but closely inter-connected vectors of communication. The first of these was the faxing of instructions specifying exactly how many rupees should be paid out to whom to their distributor-partners in Pakistan; the second involved daily negotiations with global Hawaladars based in Dubai for the for the delivery of the requisite quantity of rupees to their distributor partners, against the delivery of an agreed amount of US dollars, which were normally sent to an account maintained by the Exchange House in New York; the third element was the delivery (usually by Brinks or Securicor) of a consignment of ready-counted cash to their bank, together with instructions for conversion to US$ and onward transmission by TT to New York.

Since these carefully choreographed moves, which were repeated daily, were part of a global settlement process, it follows that each such deal was matched by an equally carefully choreographed set of moves whereby the customer or customers who released the rupees in Pakistan for onward delivery to the distributor hawaladars in exchange for the consignment of US $ which had been sent from UK to New York. Sometimes – although relatively rarely, as far as I could determine – this transaction might take the form of a direct bilateral swap, in which case the US$ payment might be made directly into an overseas account held by a business or individual based in Pakistan. More usually, however this result appears to have been achieved in the context of a much more complex multilateral (and hence multinational and multi-currency) settlement engineered by one or other of the Exchange Houses in Dubai. I should emphasise that I use the word 'appear' quite deliberately: given the data to which I had access I was only a very distant observer of these transactions. Nevertheless having pieced all the snippets of information available into a reasonably coherent picture, the best explanation that I have been able to come up with runs as follows.

As labour migration into the gulf region took off during the 1970's, a small number of Indian and Pakistani entrepreneurs based in Dubai began to offer money transmission services back to migrants' villages of origins in South Asia, doubtless facilitated by hawala deals with

[2] In normal circumstances these records would also have been inaccessible, if only for the reason that bankers everywhere would not normally open their records to outsiders; however given that the Hawaladars in question were facing long terms of imprisonment, that Customs and Excise had already impounded their records (such that I too could gain access to them in my role as an expert for the defence), and that the Hawaladars had nothing to loose by explaining all their trade secrets to me, I was able to gain an exceptional insight into their operation. But since, by the same token, all their partners at every level in the operation, whether in the UK or overseas, were in very real danger of finding themselves dragged into the dock if they discussed such matters with me, it was hardly surprising that they became even more reluctant to talk than ever before.

individuals and commercial enterprises in both India and Pakistan whose access hard currency was severely restricted by draconian foreign exchange controls. As the years passed these Exchange Houses became more numerous, and the scale of their activities grew equally steadily. This pattern of growth received a major boost when the oldest and largest of these Exchange Houses, UAE Exchange, gained access to the SWIFT system of global inter-bank electronic money transfers around a decade ago. However if I am right in thinking that Dubai is a settlement centre, it also followed that the Exchange Houses also needed to do deals between themselves. Hence it should come as no surprise that the UAE Exchange soon set up a secure intranet which not only took in all the other Exchange Houses in the city but also linked them to its SWIFT facilities.

So just what was (and is) the core business of these Exchange Houses – all of which are properly constituted LLCs licensed (and in that sense regulated) by the UAE authorities? At one level they operate quite straightforwardly as both retail and wholesale Hawaladars, taking in funds from innumerable agents across the whole Gulf Region as well as on over-the-counter in Dubai itself, and arranging their delivery to migrants' families across the length and breadth of South and South East Asia. However at another level it also seems equally clear – at least on the basis of the evidence to which I now have access – that these Exchange Houses also play a crucial role in setting up hawala-style settlements on a truly wholesale basis, since as appears that all the transactions in which they engage at this level take place in multiples of $100,000. Moreover the central source of liquidity in this process is equally clear: it stems from the huge sums which migrants from South, East and South East Asia working in West Asia, Western Europe and North America are currently remitting back home to their families through informal channels.

But what about the counter-flows? At this point I must admit that I am still not in a position to identify the source of these with any great precision: other than the global Hawaladars themselves – or failing that access to their bank accounts in New York – could provide a final answer to that question. Nevertheless all the evidence that I have so far accumulated suggests that source of these counter-transfers remains much the same as they were when the UAE Exchange first opened for business. If so they are overwhelmingly the outcome of innumerable value transfers made by individuals, and above all by commercial enterprises, which find themselves located in financial jurisdictions where access to foreign exchange is so tightly restricted that they have no alternative but to turn to the 'black market' if they wish to finance almost any kind of transnational commercial activity. In these circumstances – and they are circumstances which hold good in a substantial part of the whole vast Asian region – it follows that hawala transactions provide the only effective means of means of participating in the global commercial order.

Hence whilst I can offer no concrete proof in favour of such a proposition, I would submit that what we have here is a plausible explanation of the source of the funds to match the total outflow of value tied up global informal migrant remittance transfers, but one which also suggests that the inflow of remittances down informal channels, no less than those funnelled through more formal structures and institutions are a vital source of hard-currency liquidity for business enterprises (and sometimes even often for governments) in some of the least developed corners of the developing world.

5 The status of the informal sector

Even though a large part of the real economy in most parts of the developing world is best regarded as lying in the informal sector, from a formal sector perspective the grey and/or black markets in which most transaction in that sector take place are invariably perceived as dens of unregulated criminal and near criminal iniquity. In the case of Hawala that perception was strongly reinforced in the aftermath of the events of 9/11, and as a result of the provisions of Patriot Act a whole host of regulatory efforts currently identified as AML/CFT were let loose on a global scale.

Before considering the logic and likely effectiveness of this new global regulatory regime which both the Fund and the Bank are now so actively sponsoring, it is worth making a few comments about the *commercial* efficiency of hawala as a system of money transmission. Although my personal experience is limited to transactions in the UK – South Asia arena, all indications suggest that the system is extremely reliable. Funds invariably arrive on time at their destinations, and despite the huge value of the sums transmitted, and the absence of any regulatory order other than that of personal trust, defaults have been extremely rare – at least until very recently. Moreover these recent defaults have not arisen because of scams internal to the system, but rather as a result of regulatory interventions. These interventions – largely justified on the grounds that hawala was merely a vehicle either for laundering profits of the sale of drugs or for terrorist finance – have by no means restricted to the UK alone. Nevertheless Customs and Excise 'success' in impounding several millions of pounds of cash in transit through the system, supplemented by the confiscation of all the convicted Hawaladars' personal assets necessarily caused a serious system default, and rendered the whole system far more risky than it had been hitherto.

Other than this system appears both to be highly efficient in organisational terms, and to be very effectively self-regulating. Yet just how was this achieved? As we have seen hawaladars do indeed keep records, but on a very different basis than that deployed in the formal sector, with the result that they are far less voluminous. The information which each operator at each level in the system actually records is largely restricted to solely that which is vital to the completion of the transactions in which he is involved with his own immediate partners. Taking view that the next set of transactions further on down the network in which his partners are involved are of no concern to him, there is no need to explore - and still less to record the details of – those transactions. All that mattered was that just as his partners trusted him to implement his agreed-upon deals swiftly and reliably, so he in turn trusted them.

This, then, was a distributed system in which there was no central record-keeper, nor any excess of record keeping at each of the many nodes in the network. In other words it was a system where security was grounded in mutual trust, rather in system where the central guarantee against malfeasance was the availability of detailed, checkable and auditable and endlessly reduplicated bureaucratic records at every level in the system. But whilst such informality, and above all the absence of any kind of centralised records might be a complete nightmare from an accountant's point of view, Hawala fitted its purposes as a value transmission system extremely well. By cutting out all unnecessary bureaucratic procedures Hawala, and by cutting profit margins at every level in the system to the bone, Hawala offered its customers a deal which was far superior to that which either Banks or specialist money-transmission agencies could ever hope to achieve.

Nevertheless it is also worth noting that Hawala does not wholly disregard the formal banking system. Quite the contrary. In keeping with its commitment to taking strategic advantage of all available facilities as and when they suited its purposes, Hawala in no sense operated outwith the formal banking system. Hence whilst the collection and distribution of cash as well as processes of consolidation and de-consolidation (for both of which Banks charge substantial fees) are invariably handled informally, once consolidation had reached a sufficient scale Hawaladars promptly turned to the Banks' wholesale money transmission facilities as a means of completing settlements. This also explains the key role of New York in the whole system. Since opportunities to arrange simple bilateral swaps relatively rarely occur, despite their greater profitability, the services of Dubai's Exchange Houses were invariably needed to construct the necessary settlements. However once arranged, those settlements were invariably implemented in US$, the global medium of exchange, and thus ultimately transacted on the computers of major international banks in New York, where they presumably leave a very clear audit trail. To sum up, Hawala does not operate outside the formal international banking system. Rather Hawaladars routinely utilise its facilities, although they do so judiciously and for there own purposes. Any other approach would pile on the overheads, and undermine the fine-tuned logic of their commercially successful business

6 The relationship between Hawala and the formally organised financial sector

Nevertheless there is an important sense contemporary hawala is a child of regulatory restrictions. If such severe restrictions on access to foreign exchange had not been introduced in so many parts of Asia and Africa in the immediate post-colonial period, such that many commercial enterprises had no alternative but to rely on the black market to do business, and if an ever-growing volume of migrant remittances had not emerged as a means of satiating the equally rapidly growing demand for hard currency, the contemporary hawala system would not have developed nearly so swiftly as it did. However that is by far from being the whole story. If it was the steady relaxation of foreign exchange controls in recent years would have fatally eroded the hawala system. That has not happened because many further strands underpin its success and stability.

One of these is, of course, the sheer commercial efficiency of the whole operation, which provides a vehicle for the transmission of value within a global arena at a fraction of the expenses incurred when the same operation is channelled through the formal banking sector; secondly it provides a highly effective vehicle for sustaining commercial transaction in regions where the formal banking sector, and indeed the state, has collapsed, as in Somalia, Iraq, Afghanistan and in much of Central Asia; thirdly its principle are immediately congruent with the cash-based informal economies within which the greater part of the rural population in many of the least developed economies operate on a day to day basis – and from whose ranks a large proportion of global labour migrants are recruited. Last but not least Hawala provides a ready means of facilitating trade across nominally 'closed' borders: after all what was the Iran-Contra Affair but a classic example of a carefully engineered piece of *ad hoc* hawala finance, designed to achieve otherwise unattainable ends?

However it is not regulation-busting strategies of this kind which is currently causing global financial regulators – from James Wolfensohn onwards – so much concern. Rather it is the fear that Hawala not only could be, but actually is, primarily a front for the laundering of funds which have been illegitimately acquired through the sale of narcotics, together with the principal means whereby international terrorists finance their operations. As a result elaborate AML/CFT programs are currently being rolled out – at vast expense – on a global scale. If these were to successfully fulfil their objectives Hawala as we currently know it would effectively be ruled out of order, not only would that many millions of migrant workers would have no alternative but to use the much more expensive facilities of formal sector to remit their savings back home, but the initiatives in the informal economy which have grown up as a result of their arrival in so many parts of the developing world would be equally seriously disrupted.

But before pressing on to explore these issues – which lie at the core of the Conference's agenda – we must first address the terrorist agenda. Just how far are the fears which lie behind the current drive to implement AML/CFT programmes, and hence to comprehensively regulate financial transactions on a global scale, actually justified? In doing so one point is quite beyond question. There can be no doubt whatsoever that hawala-style operations *could* be used to launder the proceeds of the international trade in narcotics, and also to supply all manner of terrorist groups with the funds they need to carry out their nefarious activities. However that should not be a cause for any surprise. By just the same token the formal banking sector could be used – and plainly has been used – for precisely these purposes. Hence the central issue here is not so much whether Hawala could be so used, but whether it has *actually* been so used, and perhaps more pertinently still whether the Hawala has, as a system, has any built-in safeguards against the prospect of it being so misused. If so, it also becomes possible to explore how those internal safeguards might be reinforced as an alternative to the sledgehammer approach which seeks to regulate the whole operation out of existence.

7 Hawala as a vehicle for money laundering?

So just how much concrete evidence do we have of Hawala being used to surreptitiously transmit funds which were either the product of, or were being used to finance, serious criminal activity? Before addressing that question directly, several vital caveats must be introduced. Firstly I should emphasise shall my remarks here apply to Hawala *systems*, rather than to *ad hoc* bilateral swap. These can indeed very easily be set up as a means of covering up criminal activity – as in the case of the Iran-Contra affair, for example. Secondly I am mindful of the fact that formal logic insists that proving a negative is an impossible feat, and also that any attempt to insist that illegal transactions *never* occur in a system of transactions so large, complex and global as IVTS/Hawala would be extremely foolish. In like manner even the most carefully regulated Bank would be leaving a large hostage if it went so far as to suggest that those engaged in criminal activities had never been amongst its customers, or that its implementation of all the latest AML/CTF measures could be guaranteed to prevent that from ever recurring.

Let me therefore begin by asking whether there is any concrete evidence that the Hawala transactions with which I am intimately familiar, in other words those between the UK and South Asia and which involved the transmission of in excess of £500 million overseas, actually included a significant amount of funds which were the profits of drug smuggling, or which were intended to finance terrorist activities. On the face of it this question can be answered very straightforwardly: at least one of the hawaladars pleaded guilty as charged, and in all the other cases which have so far been tried, the jury found the hawaladars guilty as charged. As a result that they were sentenced to long terms of imprisonment and all their assets (both commercial and personal) were seized by the Crown. However closer examination of these proceedings throws up a much more disturbing picture. The hawaladar who pleaded guilty did so in substantial part because he was advised by his counsel that although in terms of sheer logic he was in a position to but an extremely strong case in his defence, there was no way in which he could come anywhere near guaranteeing that the jury would accept the validity of his arguments. Indeed given that such huge sums of money were involved, that the defendants were all South Asian, that the events of 9/11 lay in the very recent past, and there popular hostility to the South Asian presence appeared to be running high in the area from which the jury was likely to be drawn, he had to report that he was pessimistic about the likely outcome if the case went to trial. In the face of this advice the hawaladar concerned concluded that his best strategy was simply to plead guilty, in the expectation that he would receive a substantially lighter sentence than he would if he had mounted a defence. His decision was well-advised. Several further cases have been to trial since then, and all led to convictions.

Sceptical readers may well be asking whether the juries' verdicts in the cases cited above were actually quite correct. With that in mind let me provide a brief summary of the evidence led by the Crown. Despite having conducted very extensive surveillance operations prior to arresting the suspects, Customs and Excise Officers were not in a position to produce no direct evidence that the large sums of cash delivered to the Hawaladars' premises were actually profits accrued from the sale of drugs. Indeed as far as I am aware they arrested no wholesale drugs traffickers the course of these operations. Instead they relied on circumstantial evidence – showing that some of the couriers making cash deliveries had associations with drugs traffickers, although all of these appear to have been very low level operatives.

However the Crown bulked out this surely very flimsy circumstantial evidence by arguing that 'sensibly' there could be no other explanation as to why huge sums in cash should have been carted around the country in holdalls and cardboard boxes, or why the funds so collected should have been sent to New York rather than to Pakistan, or why the Hawaladars were unable to identify the specific individuals to whom the wholesale consignments of cash which they received actually belonged, or to identity of ultimate beneficiaries of the funds despatched to New York. Hence the Crown argued that whilst retail Hawala (which it assumed was grounded in straightforward bilateral swaps) was in broad terms legitimate, the Hawaladars in question were using this legitimate retail business as a convenient front behind which to conceal massive money-laundering operations. Despite all efforts by the defence to counter this view, the Crown's argument was accepted by the jury in every case that has so far gone to trial. Nor did there appear to be much disagreement about the matter, since they required little time for deliberation before reaching their verdicts.

To set these verdicts in context it is also worth noting that if these Hawaladars activities had been inspected using the IMF's currently preferred AML/CFT instruments, their practices would also have been found wanting on precisely the same grounds as those deployed by the prosecution: the Hawaladars were unable to identify the original source of the wholesale funds passing though their hands, and to the extent that the bulk of the funds sent to New York were sent into one or other of the Exchange Houses accounts, there was no way in which the could identify the ultimate beneficiaries of these transfers either. But is this clear-cut evidence of money laundering, as the Crown alleged, or is it precisely what one would expect to find in the context of a decentralised system of consolidation and settlement?

My own understanding of hawala as a system points strongly to the second conclusion: indeed it seems to me that whatever point an investigator chose to tap into this global network, exactly the same patterns would be revealed. Whilst every hawaladar records full details of all his transactions with his immediate partners, the further transactions in which his partners were involved he would little or no knowledge of the next set of transactions in which those partners were involved further down the line. It is, of course, precisely this lack knowledge – and of records – AML/CFT activists find so alarming: from their perspective a system such as this appears to be wide open to penetration by drugs barons and terrorists.

8 Formal and informal methods of ensuring system security

But just how justified are their fears? To those wedded to the merits of bureaucratic procedures, the only way in which system security can be guaranteed is through the maintenance of comprehensive records systems, which can then be opened to inspection by a whole series of accountants, auditors and regulators, both internal and external. However the informally organised Hawala system utilises an entirely different approach: security is guaranteed not by formal bureaucratic procedures, but rather by ties of absolute mutual personal trust between each pair of hawaladars, which consequently become a characteristic of the network as a whole. Yet how just how can that trust be guaranteed? And are there any sanctions against malfeasance? It is quite clear that such sanctions do exist – although they are rather different in format from those deployed in the formal sector.

If security is guaranteed by relationships of absolute trust, it follows that every hawaladar's most pressing responsibility is not to betray that trust, not least because just as in the formal banking sector, a default at any point in a chain of transactions can have exceedingly far-reaching repercussions. To put it in more formal terms, all hawaladars have an unspoken duty of care towards each other. If this is so it also follows that any hawaladar who knowingly entered a deal with a person whom he knew[3] to be a major drug-smuggler, and or to have terrorist operations in mind, would not only be taking a major personal risk, but would also be engaging in a transaction which – if discovered by his partners – would not only most likely obliterate the relationship of trust between them, but would precipitate severe sanctions. Not only would the hawaladar and his entire family find themselves excluded from hawala operations, but most likely from their entire ethnic community as well.

In view of all this it is quite clear – no less theoretically than empirically – that regulation and security can be achieved just as effectively – and possibly more effectively – through informal networks of personal trust as through the formal bureaucratic procedures. Two points are well worth considering on this score. Firstly there is plentiful evidence to suggest that that at the very highest levels of commercial activity – international banking, for example – relationships of personal trust play a key role in guaranteeing security; and secondly that bureaucratic procedures to achieve that goal can be and are regularly circumvented by those who occupy a position of sufficient bureaucratic seniority. If Enron is but one example of such malfeasance in the developed world, such scams are even more frequent in the developing world, as migrant workers are only too well aware. Hence migrants' strong tendency to rely on the informal sector is to a large extent an entirely rational choice.

9 Migrant remittances, economic development and AML/CFT initiatives

To return to the core concerns of this Conference, there can be no doubt whatsoever that the current global flow of migrant remittances has a tremendous potential for generating economic development, especially in the otherwise capital-starved regions from which the great majority of labour migrants are drawn. To be sure that potential has so far been largely unrealised, at least in part because that potential has either been overlooked or mishandled by the formal sector – whether in Washington DC or in national capitals in most parts of the developing world. However there are now clear signs that the resulting logjam is now

---

[3] It goes without saying that the personal relationship of trust between hawaladars who introduce cash into the system and their customer, as well as between the hawaladar who makes the final delivery and the recipient will also be extremely close. There is no way in which unknown outsiders can penetrate the system, particularly if they seek to use it as a means of transmitting large sums in cash. Who knows, in current circumstances such strangers might well be AML/CFT investigators.

beginning to break, and that all manner of new policy initiatives are now being developed. Against that background this Conference's exploration of the contribution which the financial sector can make towards releasing this potential can only be regarded as extremely welcome. However if real progress is to be made, we must take great care to avoid past mistakes.

Administrators, policy makers and planners sit in offices, and as a result their view of the world is almost inevitably formal, numerical and top-down in character. However if I have learned anything during the course of my anthropological 'bottom up' observations of transnational migrants, it is their refusal to take no for answer, their refusal to be cowed by apparently overwhelming obstacles, and most especially their immense success in devising strategies by means of which to take opportunistic advantage of whatever niches which they able to identify in the global labour market. Not did they devise these entrepreneurial strategies with little assistance from anyone else, but they are currently using just the same tactics to deliver a huge inflow of development capital into their home villages, and hence into the local economy of the immediate localities within which those villages are set. In almost every case the scale of that inflow is that provided by the combined efforts of national governments, international aid agencies, and assorted NGOs. Yet despite the scale of these (heavily localised) inflows, sustainable development has failed to take off, leading many more centrally located planners and administrators to argue that returnee migrants are their own worst enemies, and that the principal reason why the development potential fails to take off is that the returnees and their kinsfolk are handicapped by their lack skills, foresight and entrepreneurial abilities amongst the migrants themselves. In my view this top-down view is largely specious. As I have argues in some detail elsewhere (Ballard 2003, 1988), observed outcomes in so many high-emigrant regions are far better understood as a consequence of externally imposed structural constraints than on the absence of appropriate skills and abilities within the local population: their immense entrepreneurial success once they leave their villages of origin gives the lie to all such suggestions.

Within that conspectus, current international efforts to regulate Hawala transactions on AML/CFT grounds, and to divert the remittance flow into more expensive and less efficient institutionally regulated channels such as Western Union can only be read in one way: as a potential further obstacle to – or to be more specific a significant tax on – migrants' efforts to invest in, and to promote the economic development of, their home villages. Moreover the benefits of that tax are most unlikely to be ploughed back into their own villages: on the contrary they are much more likely to be paid out to meet the salaries of the army of clerks and bureaucrats who will need to be hired if remittances are to be channelled through formal rather than informal channels.

A large question also needs to be put over the issue of whether the tightly ordered regulatory regime which is now being planned will actually work, for one of the most consistent characteristics of the behaviour of these skilled exponents of 'globalisation from below' (Smith and Guarnizo 1998) is that their capacity to circumvent the worst of the obstacles placed in their path. Hence it would appear that Hawaladars at all levels have already begun to develop strategies by means of which to cope with new AML/CFT regimes, although these necessarily invariably add – sometimes marginally and sometimes very significantly – to their transaction costs. However there are few signs that these are anywhere near as high as those of formally constituted – and hence bureaucratically top-heavy – agencies such as Western Union. Hawala – just like so many other institutions and practices in the formal sector – clearly has a future, come what may.

10 Conclusion

If so, the time has surely come to get real. It is not just that far reaching transformations are being wrought socio-structural order in all of world's highly developed economies as a result of mass migration 'from below': the same is true of the global financial order, and also of those specific localities from which the bulk of that outflow currently takes place. With that in mind it is worth turning to another area in which formally constituted authorities' efforts to impose centralised (or perhaps more accurately *hegemonic*) control over the entrepreneurial activities of transnational migrants: border controls. As Bhagwati (2003: 99) has recently argued, all developed economies now need to recognise that despite all their efforts – both individual and collective – to hold the pass, in *de facto* terms all have now lost control of their borders. In consequence he argues that all governments must now recognise that the inflow of migrant workers "cannot be effectively constrained and must now be creatively accommodated". Just the same argument holds true – or so I would suggest – in many other spheres, including those with which we are concerned in this conference.

Remarkably enough a prescient argument along just these lines has already been developed by a former World Bank officer in a monograph strikingly entitled *Undermining the Centre* (Addleton 1992). So germane are the conclusions of his study – which is based on his observation of developments in Pakistan during the 1980's – that I feel I can best close my contribution to the deliberations of this Conference by quoting him at length. No less than I, Addleton is clearly deeply impressed by the *autonomous* basis on which the whole migrant enterprise was proceeding, so much that central attempts to manage those processes – to the extent that they had any impact at all – precipitated far more negative than positive consequences. Hence as he puts it:

> "Nowhere were the decentralising aspects of migration more clear than in the area of remittances. Controlled entirely by individual workers rather than government entities, investment and consumption decisions rested entirely with individual migrants themselves. Remittance earnings also fuelled an active parallel market which grew rapidly in the 1970sa and 1980s and seemed impervious to centralized government control. This parallel market extended not only to the *hundi* foreign exchange markets ... [but] also a flourishing black market in consumer goods, characterized by the development of alternative trading networks beyond the reach of government. Neither the *hundi* market for foreign exchange transactions nor the black market for imported consumer goods was penetrable by the government in terms of taxation or any other kind of control. Taken in the aggregate, the remittance segment of the national economy emerged as one of the most vibrant and important areas of activity … overshadowing foreign aid disbursements and … exceeded the resources that the government itself was able to earn off exports or channel toward national development programmes.
>
> The decentralizing aspects of migration were felt in other areas as well. The emphasis on personal consumption and individual preference meant that the largest investments in community goods relating to health and education, and usually regarded as the responsibility of central and provincial governments, were difficult to finance. … While millions of Pakistanis were undoubtedly better off in material terms, poor literacy rates and an abysmal health care system continued to pose enormous challenges. …. On the policy front, the most obvious implication from the Pakistan experience is that governments can do little to affect or influence a migration process which is largely demand-driven. …attempts to 'regularize' or 'control' the process are more likely to be damaging rather than beneficial. On the contrary, they will more likely result in an active blackmarket … and

> circumvented government controls. The development of these parallel markets … carries a financial cost and introduces inefficiencies into the migration process…
>
> Viewed in this fashion, the best government response to migration is one that aims at improving the overall economic environment in all sectors. A banking policy that makes sense from a banking perspective will probably be attractive to the migrant community. Similarly, a foreign exchange policy where official exchange rates approximate .those prevailing on black markets will be most effective in attracting remittances from overseas emigrants through official channels.
>
> Migrants departed as a result of individual initiative or because of the efforts of hundreds of small private recruiting agents. Remittances were returned to hundreds of thousands of households, often as a result of services rendered by independent *hundi* agents acting alone. The spending and investment power made possible by remittances did not accrue to the government, but was widely diffused throughout the country. Remittances made parallel and informal marketplaces even more attractive than ever. The end result was a far more complex economy, marked shifts in investment and consumption patterns – and, most importantly, an undermined central government whose own role in mobilizing resources and directly managing the economic future of the nation was seriously diminished. (Addleton 1992: 207 - 212).

On the face of it Addleton's conclusion might appear to be entirely negative: mass emigration and the inflow of remittances on an equally massive scale undermines the capacity of Governments to control their own economy. However a closer inspection of his argument suggests that his position is actually far closer to Bhagwati's: namely that in a world where transnational networks – from below no less than above – are becoming ever more salient, it makes far greater sense to develop policies which seek to manage (and hence assist and promote) the entrepreneurial potentialities embedded within these networks than to make vain attempts to corral them within a necessarily hegemonic regime of centralised regulation and control.

References

Addleton, Jonathan (1992) *Undermining the Centre: the Gulf, Migration and Pakistan* Karachi: OUP

Baldwin, Fletcher (2002) Money Laundering Countermeasures with Primary Focus Upon Terrorism and the U.S.A. Patriot Act 2001, Journal *of Money Laundering Control*

Ballard, Roger (2003) "A case of capital-rich under-development: The paradoxical consequences of successful transnational entrepreneurship from Mirpur" in *Contributions to Indian Sociology* Vol. 37, p. 49 – 81.

Ballard, Roger (2003) "The South Asian Presence in Britain and its Transnational Connections" in Parekh, Singh and Vertovec *Culture and Economy in the Indian Diaspora*, London: Routledge.

Ballard, Roger (2002) The Principles and Practice of Hawala Banking" <www.art.man.ac.uk/CASAS/pdfpapers/hawala.pdf >

Ballard, Roger (1988) "The Political Economy of Migration: Pakistan, Britain and the Middle East", in Eades, J. (ed.), *Migrants, Workers, and the Social Order,* London: Tavistock

Bhagwati, Jagdish (2003) "Borders Beyond Control" in *Foreign Affairs* January 2003, p 98 – 104.

Darbar, Johnston and Zepherin, (2003) "Assessing offshore: filling a gap in global surveillance" in *Finance and Development,* September 2003, p 32 - 35

Development Finance in *World Bank Development Report 2003*

El Qorchi, Maimbo and Wilson (2003) *Informal Funds Transfer Systems: and analysis of the informal Hawala System* Washington DC: IMF/World Bank

Passas, Nikos (2000) "Informal Value Transfer Systems and Criminal Organisations: a study into so-called underground banking networks" The Hague: Netherlands Ministry of Justice

Ratha, Dilip (2003) Workers' Remittances: An Important and Stable Source of External

Smith and Guarnizo (1998) *Transnationalism from Below*: London: Transaction