



**Failures in the official forex market**

## **Is the Hundi market a scapegoat?**

Sajjad Zohir and Wasama Ahmed Khan | Sunday, 20 November 2022



We have been wondering about the rationale behind Bangladesh Financial Intelligence Unit (BFIU)'s decision to suspend "cash out from 230 customer accounts with four mobile financial services (MFS) providers for transacting remittances through hundi" (TBS, November 17, 2022). The suspicion of Hundi activities in those transactions may be valid. But, is it desirable to take actions, during the current period of scarcity, "to prevent the transactions of remittances through hundi"? This brief note argues why the actions similar to those announced may aggravate the crisis.

It is recognised that happenings in the 'official market' of foreign currency in Bangladesh have direct bearings on the 'non-official' (hundi) market. This is because the buyers of foreign currency can freely move between the two markets. Hypothetically stating, such cross-flows are also possible in case of currencies in trade. Yet, the instances of foreign currency moving from the Hundi market to the official market, mediated by banks acting as an extra tier of commission-seeking intermediary, is a recent happening that deserves critical assessment. This however is not addressed here.

The series of events that led to increasing concerns with the foreign exchange reserve suggests that the current crisis in the official market is driven by inadequate supply of foreign currency in that market, which subsequently led to abnormal increases in demand for foreign currency (and prices of USD) in the Hundi market. This increase, especially the increase in the difference in exchange rates in the two markets, will divert supply of foreign currencies away from the official market to the Hundi market. Moreover, increased divergence fuels expectations and may further increase the demand for foreign currency in the Hundi market. It is apprehended that all these may fuel a spiral move towards further instability in both markets.

In brief, we suggest that any move to curtail supply in the Hundi market will accentuate the problem stated above. That is, with other factors unchanged, the price of foreign currency will increase more than it would have in the absence of BFIU policies meant to curtail supply in the Hundi market. Commonsense suggests that the vicious cycle may only be checked if demands for foreign currency are

dampened and the government is better positioned to prioritise the needs of the country. Import sectors (activities) that have the least (or no) adverse effects on rest of the economy should come under strict scrutiny at first.

It is understandable that the MFS market should be guided so that they do not turn into instruments that facilitate illegal flow of money. The Intelligence unit can access information on flows and follow up with further queries that help in designing appropriate actions against wrong-doings. With no normative assessment, we suspect that the clamour at policy levels by stopping several accounts will adversely affect remittance inflows. Those (in foreign land) who want to send may choose to innovate new (and possibly risky) ways to transfer money (foreign currency) or may hold onto their savings till the situation is favourable.

As for BFIU and other similar agencies, isn't it more important (and desirable) to stop easy outflows of foreign currencies that are bought in the Hundi market and which sustain a high level of demand in that market? Elsewhere the lead author proposed to investigate the entitlement of out-going passengers who are foreign citizens of Bangladesh origin, and the local dailies have highlighted the demands in the Hundi market associated with travels which demand closer scrutiny.

It is unfortunate that uncalled for clamouring of surveillance and curtailing remittance inflow through the Hundi market will lead to reduction in total supply of foreign currency in the two markets together, thus, further aggravating the situation. While the Hundi market may thrive with demand from people pushed out of the official market, the reverse logic does not always apply. Let us accept that the Hundi market exists because it serves specific purposes and because the official market fails to deliver all required services. Let us not make Hundi a scapegoat for the failures in the official market! No doubt, the cost of doing business in the Hundi market will increase. Given the extensive network of money changers in the sub-continent and given the evolving inter-linkage with other activities, the authorities will hopefully find better ways to tackle the vices without jeopardising the inflow of remittances.

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