Republic of Yemen
Prime Minister
The Executive Bureau for the acceleration of the
Aid Absorption and Support for Policy Reforms

# General Framework for Economic Stability

**From 2022 to 2023**

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Aden – Khormaksar – Security Roundabout
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## Executive Summary

Yemen's economy passes through a critical stage, which highlights the need for a comprehensive reform package to stop the deterioration, stabilize the economy and restore confidence in the government's policies and measures. To achieve this end, the efforts of all state institutions and relevant parties at the local, regional, and international levels must be consolidated to create an appropriate political and security environment for implementing economic reforms. This framework proposes a range of short- and medium-term interventions needed to control inflation and achieve sustainable stability. These interventions fall within four main areas: improving political and security conditions, strengthening government financial stability, enhancing monetary stability, and encouraging investment. Promoting economic stability will required sharing the government's priorities and policies with local, regional, and international stakeholders and consulting with them to create the appropriate environment to stop the deterioration and achieve economic stability. The government, on the one hand, will have to take the necessary measures to enhance the stability of public finances. Such measures include adopting policies aimed at building capacity, improving the performance of public finances, developing resources, rationalizing expenditure, and developing public debt management with a view to reducing the state's public budget deficit to acceptable levels. The Central Bank, on the other hand, must adopt policies aimed at reducing inflation and controlling it at an acceptable level by strengthening the Central Bank's governance, building its capacities, improving performance, strengthening banking control, seeking sources to finance the balance of payments deficit, and taking the necessary measures to stabilize exchange rates. In addition to controlling inflation, the government must also adopt appropriate policies, create a favorable environment, and operationalize judicial and security institutions to promote private investment. Using the Special Drawing Rights (SDR) requires urgently prioritizing public investment that can be financed through SDR. Regaining the trust of the International Community in the measures taken by the state's financial and monetary institutions, together with a clear plan for government's economic stability in place is the key to securing enough resources, through which economic stability can be achieved.

## Introduction

The National economy in Yemen passes through a state of stagflation, which is characterized by low economic growth, high inflation rate, high unemployment rates, downturn in most of the economic activities, together with poor implementation of government policies. Over the past five years, GDP has contracted by nearly 50%, and it is expected to continue to decline in the next two years. The unemployment rate also rose to about 32%. In the same context, the country's inflation index rose sharply, mainly due to the expansion in monetizing budget deficit, which led to a 35% increase in the overall level of consumer prices in 2020. inflation rate reached more than 58% in 2021.[1] Public finances suffer poor planning, as well as poor budget implementation and oversight, with poor capacity to centrally collect all revenues. On the other hand, the Central Bank's policies have been unstable, as well as its lack of planning tools, institutional fragmentation, and weak regulatory role on the exchange market, which have weakened any efforts to control the exchange rate. Despite the inherent difficulties embedded in the current economic situation, which is influenced by the political and military changes resulting mainly from the coup d'état of the Houthi militias, finding sustainable solutions to the economic situation may not be easy, unless local and international parties take a completely different approach by adopting clear policies aimed at improving the economic situation. Political efforts must be combined, as well as fiscal, monetary and regulatory policies must be fully coordinated to work in accordance with a clear plan to break the state of stagflation and move towards economic stability. The framework outlines one of the most important economic policies that must be implemented (in the short and medium term) to stabilize the overall price level and improve the provision of public services. The framework also reviews the most important political and security conditions needed to create a conducive environment for the implementation of the proposed reforms. After agreeing on the terms of the proposed reforms, it is important to prepare a time-bound plan of action, where the relevant authorities responsible for monitoring, implementing, controlling, and evaluating are identified to achieve economic stability.

[1] International Monetary Fund, June 2022

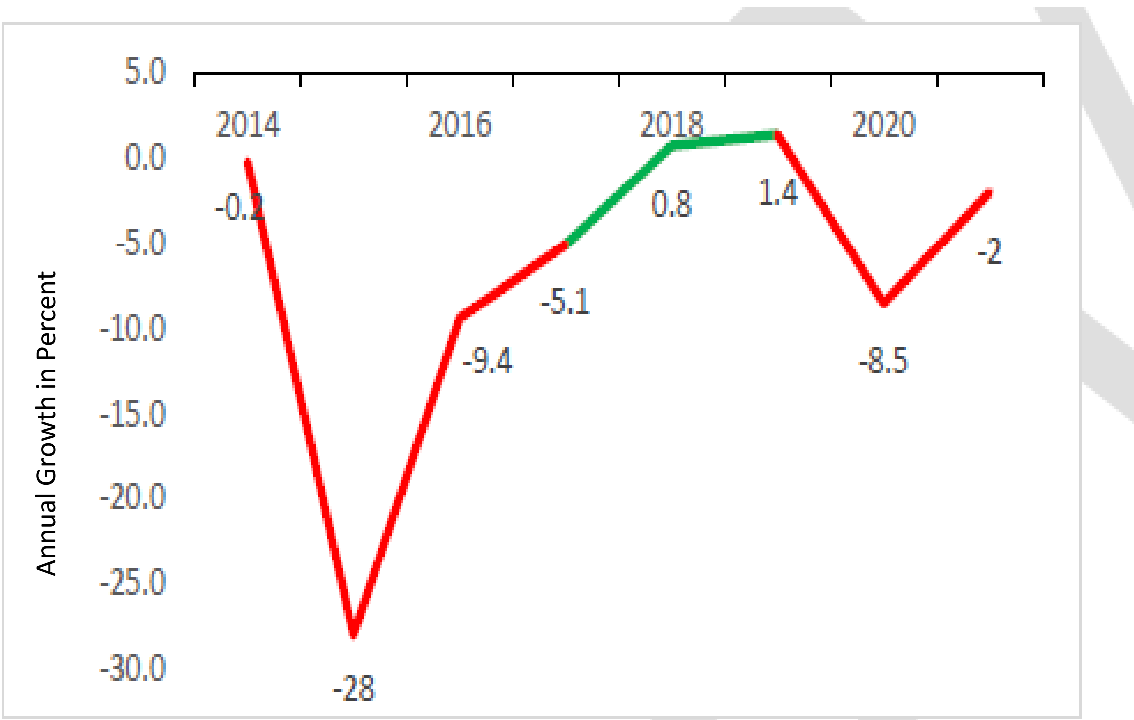
# 1. The Economic Situation

## 1.1. The War and its Impact on the Economy

The ongoing war since 2014 has had a significant impact on the national economy. During the period from 2015 to 2020, the economy has shrunk by 50%, with an average annual decline of 8.1%. GDP decreased from USD 43.2 billion in 2014 to USD 18.9 billion in 2020. Although the economy shrank significantly in 2015-2017, it witnessed a slight recovery in 2018-2019 and grew by 0.8%, 1.4% respectively due to relative stability, the resumption of oil production and the support of the balance of payments with the aid provided by the Kingdom of Saudi Arabia.[2] The economy, however, shrank again in 2020 due to the outbreak of COVID-19 pandemic slowed by 8.5%. In 2021, GDP also contracted by 1%. The per capita GDP decreased from USD1500 in 2014 to USD 582 by the end of 2020,[3] leading to worsening the humanitarian crisis and poverty. Nearly half of the population urgently need humanitarian assistance, and the poverty rate rose, covering almost 80% of the population.

The decline in GDP is due to the impact of the war on infrastructure such as electricity, roads, production, and service facilities, as well as the lack of any effective role of the fiscal and monetary policies given the inherent complexities of the political and security situation.

Figure 1: GDP Growth Rate in Market Prices




[2] Global Economic Prospects, World Bank 2019.
[3] World Bank 2020.

## 1.2. The Deterioration of the Humanitarian Crisis

The ongoing war and deteriorating economic situation have exacerbated the humanitarian crisis. According to the 2021 Humanitarian Needs Overview issued in February 2021 by the United Nations Office for the Coordination of Humanitarian Affairs (OCHA),[4] Yemen represents the world's largest humanitarian crisis. The report estimates that 20.7 million people (66% of the total population) need humanitarian assistance in 2021, and 12.1 million people are in dire need of assistance. According to the report, the number of people suffering from hunger is expected to reach 16.2 million (phase 3 of the Integrated Food security Phase Classification)[5], of whom 5 million face emergency conditions (Phase 4) and 50,000 are already suffering from disaster conditions (Phase 5). The report points out the reasons for the deterioration of the humanitarian crisis in 2021, namely the continuous depreciation of the national currency due to the government's inability to support the import of food commodities, 90% of which are imported; the impact of the Covid-19 pandemic on the flow of remittance; in addition to the disastrous impact of floods and natural disasters on infrastructure and livelihoods, as well as their role in spreading infectious and fatal diseases.

[4] Yemen Humanitarian Needs Overview 2021 (February 2021) [EN/AR1 -Yemen | ReliefWeb

[5] The Integrated Food Security Phase Classification categorizes food needs into five phases: Phase 1: Full Food Security, Phase 2: unstable food security, Phase 3: acute food crisis, Phase 4: Emergency phase and Humanitarian Relief, Phase 5: Famine/Humanitarian Disaster Phase.

### 1.3. Challenges and Economic Trends During 2021

With no signs of the war coming to an end in Yemen, national economy will continue to deteriorate in the short term. The International Monetary Fund (IMF) estimates that the economy shrank by 1% in 2021. IMF predicts that with the continued monetary financing of the budget deficit (estimated at YR 975 billion), the balance of payments financing gap of USD 1.9 billion will lead to reduce imports, thereby exacerbating food insecurity and humanitarian crisis.

The government faces great challenge of stopping the deterioration of the current economic situation and achieving stability. Urgent and effective measures will be needed, including the creation of political and security conditions and the adoption of fiscal and monetary policies to ensure that the budget deficit is reduced to an acceptable level and financed by non-inflationary sources and mobilize foreign exchange fund, whether internal or external, to finance the import of basic commodities. In addition, the Central Bank must be fully responsible for adopting strong and effective controls and measures to control the foreign exchange market and reduce speculations.

## 2. Methodology of the Framework

The framework is based on a series of primary and secondary data collected from multiple sources:

**Secondary data sources:**

Mainly, the preparation of this framework was based on an extensive desk review and analysis on group of reports and data produced by IMF, WB, FAO, METAC, Central Bank of Yemen and Ministry of Finance.

**Primary Data sources:**

*Presentation and Feedback:* to capture strategic and political insights, the framework was individually presented to the Prime Minister and Minister of Finance. Their feedback was received and highlighted whether the proposed reforms are politically and strategically feasible. The feedback also provided additional reforms and proposed more applicable means of reforms implementation.

To diversify and capture more views on the framework, it was severally presented to an ex-governor of Central Bank of Yemen, ex-deputy minister of Ministry of Finance and one businessman and two well-known development and political experts. Feedback received has significantly improved the framework contents and contributed to considering many political and technical aspects.

*Roundtable Discussion:* a group of businessmen and traders were invited to a roundtable discussion to determine the main interventions and reforms the government should put in place to stimulate domestic investment and create a favorable investment environment given the current situation. The discussion enriched the framework contents and underlined many obstacles and constraints that should be addressed for the private sector to effectively contribute to the economic stability.

*Key Informant Interviews*: the framework considered including views at the technical levels. Senior officials in many ministries were interviewed to bring out current institutional capacities against which proposed reforms feasibility was checked.

## 3. Significance of the Framework

In the seventh year of the war in Yemen, economic and living conditions of millions of people continued to deteriorate, resulting in the world's most serious humanitarian crisis. Creating conditions for sustainable economic stability has become a top priority. The government must mobilize all its efforts to stop huge economic, social, and humanitarian losses. The importance of developing a general framework for economic stability lies in the following:

- Documenting the key factors, determinants, policies, and actions to achieve economic stability in one document.
- Launching the process of developing a general framework for economic stability shall ensure that international partners provide the necessary technical and financial support and ensure the maximum use of knowledge, expertise, and best practices to achieve economic stability to ultimately arrive at a feasible version of the framework.
- The framework shall ensure identifying a set of feasible and monitorable reforms.
- A comprehensive framework for short- and medium-term economic stability, which should be implemented immediately, will help to demonstrate the government's seriousness in addressing the current economic crisis to the international community and will therefore enhance the chances of obtaining financial support.

## 4. Vision and objectives

**Vision:**

Stopping and stabilizing economic deterioration through controlling and maintaining inflation at a single digit level.

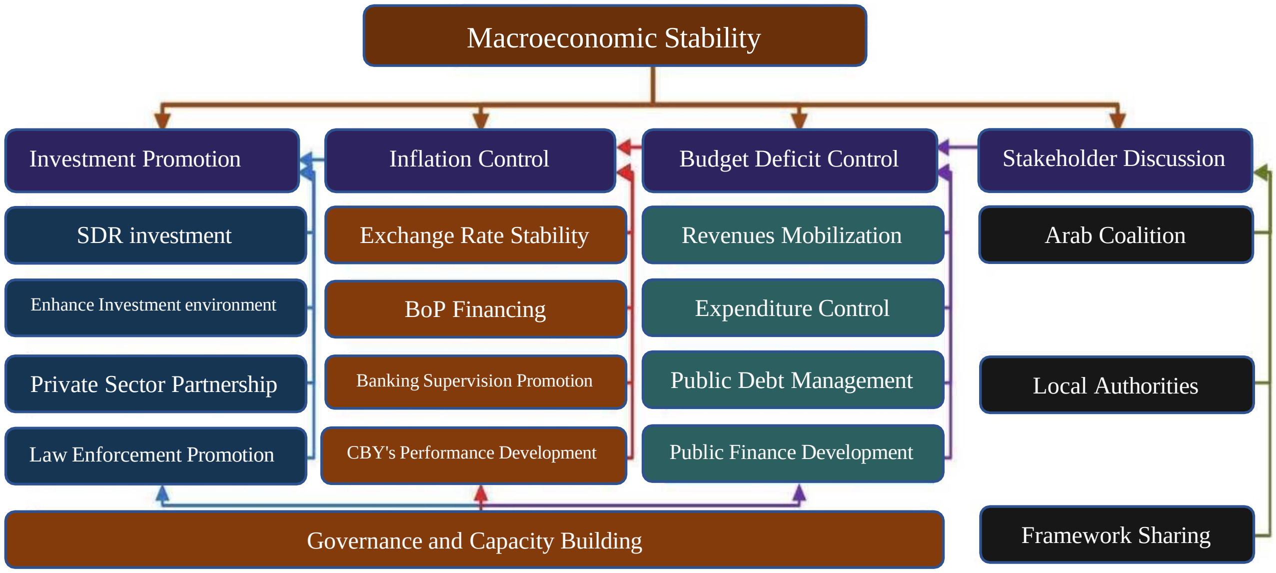
**Objectives:**

The framework calls for the following:

- Creating political and security conditions, as well as a favorable environment for the implementation of necessary reforms.
- Achieving sustainable stability of public finances by reducing the budget deficit to an acceptable level.
- Achieving monetary stability by controlling inflation.
- Creating a favorable environment for providing basic public services and encouraging investment.

Frame components: Figure No. 2: Components of the Economic Framework

*General Framework for Economic Stability 2022-2023*



## 5. Phase 1: Limiting Economic Deterioration (Emergency Interventions)

### 5.1. Emergency Public Finance Intervention

Short-term financial measures aim to develop revenues and reduce spending by taking urgent measures that can be implemented in the short term as follows:

1. Increasing tax revenues by improving tax collection by increasing the level of tax advance payments on all taxpayers and depositing it at the Central Bank; adding more tax staff at headquarters and governorates, improving their technical capacities with focusing on the large taxpayers.
2. Developing customs revenues by improving the collection of customs revenues, standardizing the customs collection procedures at all customs ports, and ensuring that all revenues are deposited in the general government account at the Central Bank.
3. Depositing all central revenues collected in the governorates into the government's general account at the Central Bank.
4. Addressing the problem of duplicate jobs by transferring, as a first step, the salaries of employees of the state administrative apparatus through banks and then starting preparations for a comprehensive survey of all government positions and setting up a regular database.
5. Achieving external debt sustainability through immediate participation in the Debt Service Suspension Initiative (DSSI). There is also a need to establish a coordination mechanism between the Ministry of planning, the Ministry of foreign affairs, the Ministry of Finance, and the Central Bank to improve the efficiency of external debt management.
6. Developing quarterly expenditure plans and realistic public budgets to ensure local participation with the aim of preparing a comprehensive budget of all state income and expenditure.
7. Enhancing transparency and accountability by developing and strengthening the oversight bodies of the Ministry of Finance and independent bodies such as the Central Organization for Control and Accountability and the National Authority for Combating Corruption.
8. Strengthening complementarity between the Ministry of Finance and other government agencies, particularly in information and data exchange, as well as policy coordination.

### 5.2. Emergency Monetary Policy Intervention

Monetary measures aim to stop the deterioration in exchange rates by taking the following monetary and control actions to control the foreign exchange market:

1. Working with regional and international partners to seek the possibility of emergency funding to stop the current deterioration, while developing clear in-take mechanisms to ensure the highest degree of transparency and accountability.
2. Completely stopping monetarizing the budget deficit and taking effective measures to ensure that the existing cash mass is managed efficiently.
3. Improving foreign exchange management procedures and establish an effective and transparent foreign exchange management system.
4. Taking prompt action to utilize the special drawing rights (SDR). This includes effective coordination between the Central Bank and the government to speed up the monetization of SDRs in consultation with potential buyers.
5. Standardizing the different exchange rates into one.
6. Releasing the Central Bank's reserves frozen in banks abroad. The Central Bank should continue its efforts to release frozen reserves at many international banks and institutions.

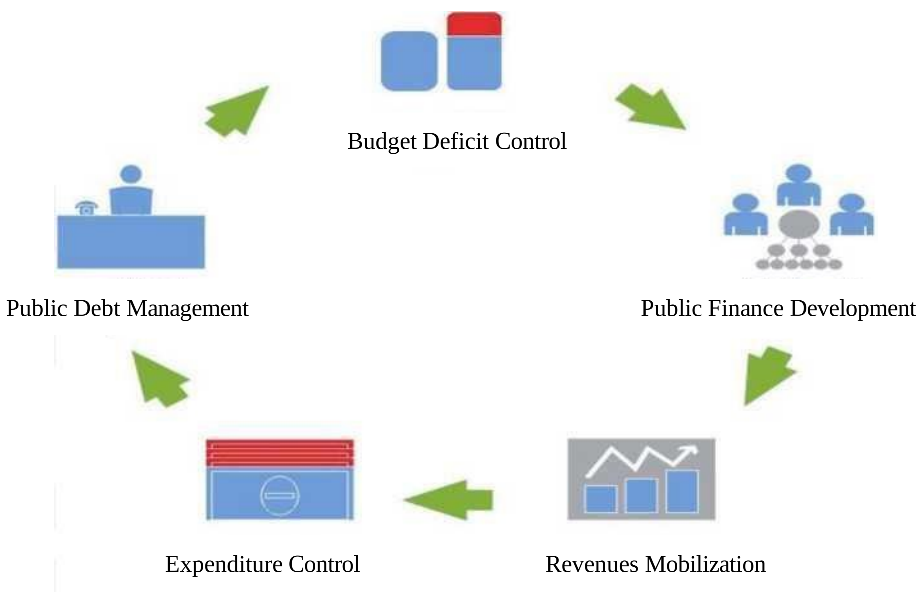
7. Developing and regulating the foreign exchange sector, as well as strengthening supervision through full control of foreign currency sales and purchases and applying strict measures — in cooperation with the security and judicial agencies — on violators in the exchange market. Remittance networks should be promptly subject to control by the Central Bank of Yemen.
8. Taking the necessary measures and procedures to deal with the violations of exchange institutions that open accounts for clients, to ensure that their cash stock is reduced.
9. Closing all accounts of public and government institutions at commercial banks and exchange firms and, instead, opening accounts for them at the Central Bank of Yemen and its offices in the governorates.
10. Taking urgent action to strengthen compliance, provide new opportunities for the banking sector to deal with correspondent banks, and transfer foreign currency to supplement the overseas assets of domestic banks.

## 6. Phase 2: Achieving Economic Stability

### 6.1. Public Finance Stability

This includes a series of reforms that must be carried out by the government, particularly the Ministry of finance, to stabilize public finance. The main goal of these reforms should be to reduce the budget deficit, to reduce dependence on inflationary deficit finance and control inflation. This includes a series of actions aiming to improve the efficiency and capacity of public financial institutions and taken emergency measures to increase revenues, rationalize expenditure and improve the efficiency and capacity of the Ministry of Finance to manage public debt.

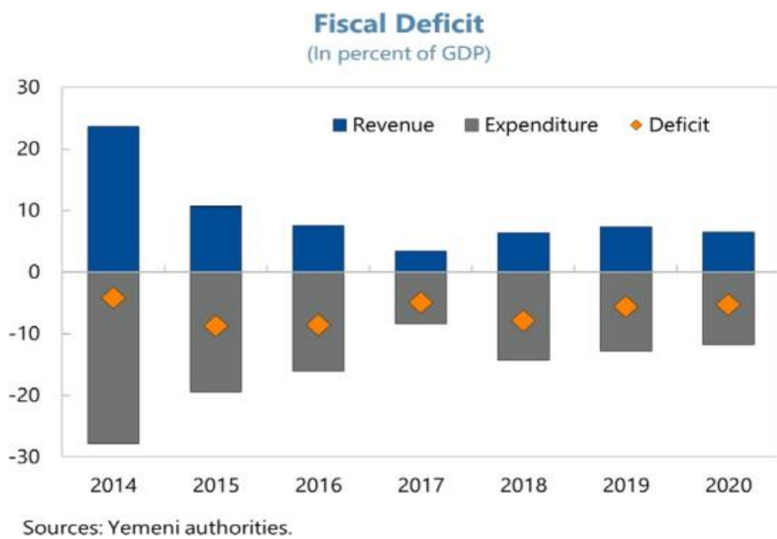
Figure 3: Public Finance Stability Framework




#### *6.1.1. Current Situation of Public Finance*

The war had a disastrous impact on public finances. Revenue slumped significantly compared to the pre-war period. Public revenues accounted for 6.4% of GDP in 2020 compared to 23.6% in 2014. One of the most important factors that led to the decline in revenues is the decline in the production and export of oil and gas, the decline in non-oil revenues due to the control of a large part of those revenues by the Houthi militias, the failure of some local authorities to deposit central revenues in the general account of the government, and the decrease in the volume of external grants. All of this has created a continuing budget deficit that yearly averaged at YR 708 billion.

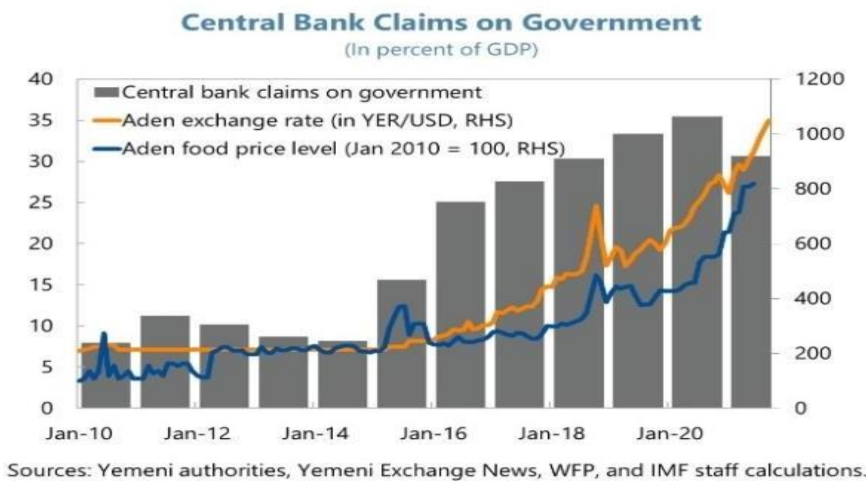
Figure 4: The Current Situation of Public Finance




Source: International Monetary Fund mission, June 2021

Considering insufficient state revenues, the government resorted to financing the budget deficit by printing new banknotes, which led mainly to a deterioration in exchange rates. In June 2021, the cumulative budget deficit was approximately YR 3.36 trillion, 94% of which was financed through monetary financing from the Central Bank and only 6% through public debt bonds. Poor oil revenues, the lack of control over all revenues by the central authorities, coupled with the high wage and salary bills in the military and security sectors, may limit the government's ability to undertake reforms to strengthen public finance indicators. Challenges posed by the conflict, as well as the political and security instability are among the important factors that play a major role in the implementation of effective reforms to improve public finance.

Figure 5: Domestic Public Debt and Exchange Rates




### *6.1.2. Proposed Policies in Public Finance*

**First: Developing non- inflationary resources:**

1. Setting up an automated mechanism for tax collection and learning from the experience of countries in the region.
2. Increasing oil production and exports and resuming LNG exports. Oil and gas revenues are estimated to have decreased by 70% in 2020 compared to 2014, as oil production fell from 172,000 barrels to 50,000 barrels per day. LNG exports have completely stopped, which was estimated over 3 billion USD in 2014.The operation of Block 5 should be accelerated to increase oil production by 25000 barrels a day, in addition to increasing the production of other oil fields and resuming the production and export operations of LNG through Belhaf port. In this regard, careful planning must be undertaken to make up for the deficit of about 1.5 billion in oil derivatives trade balance, which will require nearly doubling oil production.
3. Strengthening the role of Aden Refinery Company in importing oil derivatives, refining locally produced oil, and reducing the role of the private sector in importing oil derivatives. Local and external sources of financing should be sought with the aim of operationalizing the Aden Refinery Company, including issuing foreign currency debt bonds with the aim of resuming operations of the refineries or increasing oil production.
4. Improving the collection of local taxes by reviewing the value and schemes of local taxes.
5. Collecting the revenues of the telecommunications sector and aviation fares. Statistics show that telecommunication revenues are the second largest resource after oil (as per 2014 figures), with an annual revenue of more than USD 300 million. In addition, revenues related to air fares are crucial to increasing national revenues, all of which are collected by the Houthis. The collection of these revenues will reduce the budget deficit and enable the government to continue to pay salaries and provide public services.

**Second: Reducing Expenditures**

1. Addressing the problem of ghost jobs by conducting a comprehensive survey of all government positions, and establishing a regularly updated database, whereby duplicate and ghost jobs are eliminated in all sectors across the country. Moreover, the move towards a full automatization of the payroll for all employees of the state's administrative apparatus — as an urgent step — through biometric system will contribute to the elimination of ghost jobs.
2. Reducing unnecessary expenditure in the energy sector, improving the efficiency of production and revenues collection, and proper planning of all aspects of power sector management. Coordinate with international agencies and development partners to formulate a comprehensive and clear development plan to raise funds for the energy sector, while gradually raising energy prices, in line with the policy of increasing revenues.
3. Continuing to reduce domestically funded capital expenditure while maintaining it at the minimal and necessary level and relying on the expected funding of SDRs for the implementation of priority projects, while cooperating with international partners for any potential funds to strengthen state's ability to provide important projects.
4. Strengthening the procedures for collecting the revenues of public institutions such as electricity and water corporations. The government supports the deficit of public institutions, including electricity and water corporations, at a time when no revenues are collected from those public institutions. Effective collection measures should be taken to collect the revenues of these institutions for the coming years.

**Third: Public debt management**

1. Exploring the possibility of qualifying for DSSI with regional and international creditors and financial institutions.
2. Exploring the possibility of issuing foreign currency debt bonds to finance projects that generate foreign currency profits or those that reduce the demand for foreign currency in the local exchange market.
3. Issuing debt bonds in local currency at no more than 10% of the total expenditure.
4. Developing the public debt management of the Central Bank and the Ministry of Finance (foreign currency bond management) to effectively manage public debt.

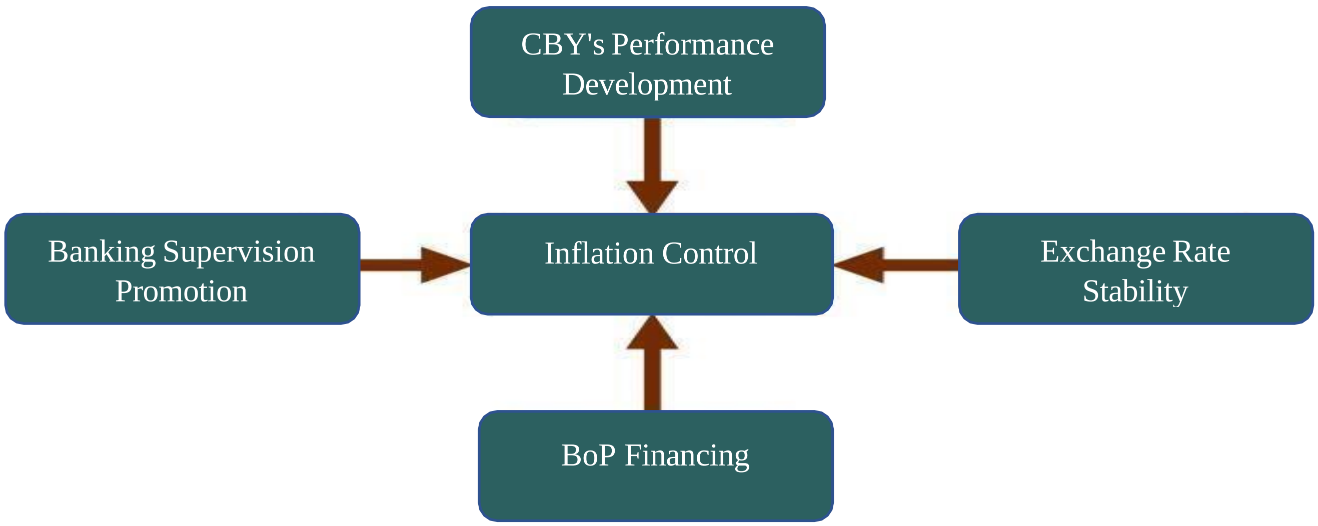
**Fourth: Improving the Performance of Public Finance**

1. Developing a realistic national public budget that ensures local governments participation. This will include developing a comprehensive national budget preparation program, identifying coordination and liaison mechanisms with local governments, and improving the capacity of staff at the local level to plan, prepare, execute and control budgets.
2. Improving the capacity of the Ministry of Finance to prepare and execute and control public budgets.
3. Strengthening the liquidity management capacity of the Ministry of Finance.

## 6.2. Monetary Stability

The following are a series of emergency interventions that the monetary authorities must adopt to reduce inflation by controlling the exchange rate. They include actions to ensure exchange rate stability, strengthening banking control, reducing the balance of payments deficit, and improving the institutional capacity of the Central Bank.

Figure 6: Monetary Stability Framework

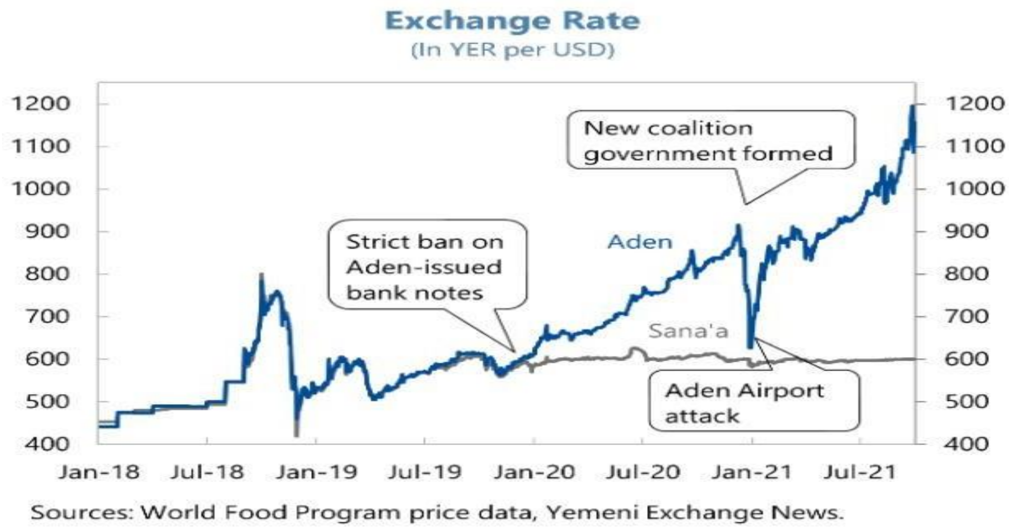



### *6.2.1 The Current Situation of Monetary Indicators*

**Exchange Rates:**

During the war years, the local currency value has depreciated to its current lowest level. The exchange rate increased from 215 YER / USD in 2014 to 1700 YER/ USD in November 2021, and then decreased to around 1000 YER/ USD in the last week of December 2021 following the announcement of a new board of directors of the Central Bank. In 2021, foreign exchange rates increased drastically, and the purchasing power of domestic currency decreased. In addition, the FAO world food index increased by 27% between October 2020 and October 2021, which indicates a rise in the price of basic food and the deterioration of living conditions in Yemen.

Figure 7: Exchange Rates




Over the past years, many of the reasons for the continued rise in exchange rates have emerged. The continued balance-of-payments deficit, the coverage of the fiscal deficit through cash financing (deficit financing), as well as weak control over the exchange market are the most important factors affecting exchange rates. The ban on using the new banknotes in Houthi-controlled areas has led to creating two prices for the local currency (the price of the old edition and the price of the new edition) and led to a rise in the exchange rates of the new edition, which is used only in areas under the control of the legitimate government. The gap between exchange rates of the local currency gradually widened to reach 100% in September 2021. However, from September 2018 to December 2019, several factors contributed to the stability of exchange rates, including the USD 2 billion deposit, provided by KSA and was allocated to support the import of basic commodities, oil grants, the USD 200 million cash grant to the Central Bank, and increased exports. The Central Bank was provided with sources of foreign currency to finance the import of basic commodities, which helped achieve a relatively stable exchange rate.

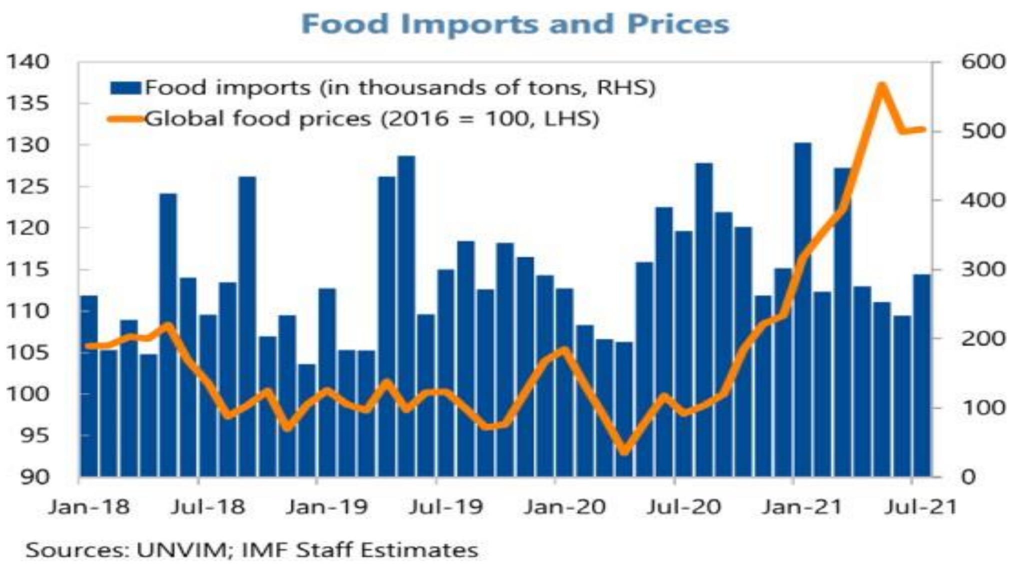
**Inflation**:

In 2020, the overall price level curve shows an upward trend of 35%, compared with 10% in 2019. With the significant deterioration in the value of the local currency during 2020 and further in 2021, the value of the food basket in the areas under the control of the legitimate government increased to YR 123,000 in November 2021 compared to YR 56,000 in December 2020, an increase of 120% in 2021.[6] High foreign exchange rates are not the only factor contributing to the high inflation rates. A range of other factors play a major role in raising inflation rates, including high costs of transportation, production, and insurance, as well as high global prices, shortages of fuel supplies, currency devaluation, and taxes. Factors contributing to the high inflation rate also

[6] FAO. 2021.
https://app.powerbi.com/view?r=eyJrIjoiMmMwYzE0OWEtMDFkYS00ZGM 4lTgwYmItMjBjN2M5OWM5ZDAzIiwidCI6IjE2M2FjNDY4lWFiYjgtNDRkMCQ 4MWZkLWQ5ZGIxNWUzYWY5NiIsImMiOjh9&pageName=ReportSectionc5 e63b280e6b753Q62d2

include the long period of import of goods, dual customs, difficulties, and weak infrastructure of inland transportation routes.

Figure 8: Food Imports and Prices.




**The Balance of Payments**

Statistics from the International Monetary Fund (IMF) show that the balance of payments deficit increased — as a proportion of GDP — from (—0.7%) in 2014 to nearly (—3.4%) in 2020, with the external financing gap projected to increase to nearly (—10%) in 2021—2022 with an annual deficit of USD 1.9 billion. In the same vein, the decline in oil exports from USD 3.3 billion in 2014 to nearly USD 711 million in 2020 created a trade deficit of nearly USD 1.4 billion, which calls for adopting policies aimed at reducing this deficit and mobilizing resources to strengthen the balance of payments and thereby stabilize exchange rates.

### *6.2.2 Monetary Policy Framework 2022-2023*

**First: Promoting Exchange Rate Stability**

1. Reducing the printing of banknotes to finance the budget deficit and developing preliminary cash management policies and measures that allow the Central Bank of Yemen, in coordination with the Ministry of Finance, to estimate the budget deficit. An annual monetary plan should be developed in which the ceilings on monetarizing the budget deficit should be set through a general monetary policy framework that aims at an acceptable inflation rate. Those plans must be discussed with the Ministry of Finance in advance before the beginning of the fiscal year and the amount of monetarizing the deficit should be approved. On the other hand, oversight, forecasting, transparency measures in monetary management and spending methods must be improved. Moreover, institutional coordination between fiscal and monetary policy should be strengthened through the formation of joint committees between the Central Bank and the Ministry of Finance.

2. Strengthening foreign exchange management by ensuring effective and efficient exchange rate management: adopting efficient and transparent exchange rate management policies and practices designed to appropriately reflect the supply/demand conditions of foreign exchange market and ultimately eliminate incentives for market behavior that tends towards more speculations. In this regard, the Central Bank's interventions should be reflected in the following:

- Adopting an auction system for sale and purchase of foreign currencies in accordance with best practices and standards. The auction system would contribute to the stability of exchange rates, show indicators of actual market trends in addition to contributing to the consolidation of exchange rates and efficiency in foreign exchange management.
- Developing LCs procedures and mechanisms funded through the deposit by KAS in a manner that promotes more effective and cost-effective / time-effective trade financing activities and apply them in any future interventions.
- Reviewing the oil derivatives financing mechanism and establishing a comprehensive and effective framework covering all relevant supply and financing procedures to achieve maximum effectiveness.

3. Consolidating foreign exchange rate. According to the International Monetary Fund, consolidating foreign exchange rates is a prerequisite condition for any economic reform to improve the efficiency and confidence of exchange rate management. Currently, there are multiple exchange rates in play. In addition to the general budget rate, different prices are given for the Saudi deposit, oil derivatives, the price of the governorates' share in the oil sales, customs exchange rate in addition to market exchange rates, which is not stable by itself. All exchange rates should be consolidated in the medium term and the expertise of the International Monetary Fund (IMF) should be utilized in this area.
4. Withdrawing the money supply and returning it to the banking sector and strengthen confidence in local currency. The banking liquidity crisis that began in 2016 has weakened people's confidence in the banking sector. Exchange companies stepped in as the alternative solution to facilitate financial transactions, which opened accounts to facilitate financial transactions in violation of the Exchange Law. With the expansion of banknote printing, a large part of the cash supply remains outside the banking sector, particularly with exchange companies and firms, which is used in speculative operations. Effective measures should be taken to withdraw the money supply by taking the following actions:

- Applying the necessary control procedures — stipulated by law — and obligating exchange companies to supply their liquidity to commercial banks and retain the necessary liquidity pursuant to the provisions of the law.
- Closing all these current accounts with exchange companies and depositing their balances in the banks.
- Strengthening confidence in the banking sector by ensuring the rapid provision of services, facilitating the transfer of foreign exchange balances to feed their external funds/assets, as well as supporting remittances and paying salaries through banks.
- Issuing bonds to recover part of the money supply.
- Linking all import permits of the list of the most imported goods with cash deposits to banks.

**Second: Improving the Balance of Payments**

1. Releasing Central Bank's reserves frozen by banks abroad. Reports indicate that nearly USD 450 million frozen in the post-war period in Europe and Asia. These reserves should be released to help the Central Bank reduce exchange rate deterioration. Despite the continued efforts of the Central Bank of Yemen over the past three years, only recently have those efforts begun to bear fruit. Similar efforts — perhaps political efforts — should be made to release the funds of local banks abroad and strengthen Central Bank reserves.
2. Using Special Drawing Rights: according to the recent allocation of the International Monetary Fund (IMF) for 2021, Yemen received an allocation equivalent to USD 655 million. At this stage, these funds should be used to strengthen the reserves of the Central Bank by accelerating the negotiations on the sale of special drawing rights and identifying the areas in which they must invested.
3. Strengthening communication with donors, development partners and brothers in the Gulf Cooperation Council to strengthen the reserves of the Central Bank of Yemen to contribute to the stability of exchange rates. During the war, all efforts to support the state budget or the Central Bank of Yemen stopped — to some extent. In the six years of war from 2015 to 2020, only USD 180 million -- the Saudi oil grant in 2018, and a central bank deposit and grant of USD 2.2 billion in 2018, were received, which contributed significantly to stabilizing exchange rates in the year 2019. International efforts — to obtain grants or deposits on concessional terms — should be combined to support Central Bank's reserves and to improve the management mechanisms of those funds — and to learn from past experiences — to use these funds to the utmost extent to stabilize the local currency.
4. Redirecting all organizations' funds and funds from abroad through the Central Bank of Yemen — the head quarter in Aden, in accordance with a clear banking/ exchange mechanism. Remittances from international organizations directly support the balance of payments of approximately USD 1.2 billion annually, all of which are transferred and exchanged through certain commercial banks under the control and administration of the Central Bank in Sana'a at a lower exchange rate. The use of this exchange rate has eroded the share of beneficiaries of such transfers in areas under the control of the legitimate government and contributed to more division in the banking sector. To enable the Central Bank of Yemen – Aden – as a legitimate body with the authority to manage the country's monetary policy — based on ensuring that such transfers are effectively used to promote trade, strengthen controls on such transfers and ensuring that humanitarian assistances are exchanged with a fair exchange rate on the other. Negotiation must continue with United Nations organizations and other international organizations to transfer all funds through the Central Bank of Yemen to guarantee the rights of all parties and promote the best use of these funds to consolidate/ stabilize exchange rates.
5. Reducing the trade deficit by increasing oil production, resuming LNG exports, and adopting policies aimed at reducing the import of unnecessary or locally produced goods that are of relative importance to the country's imports (e.g., iron). A study should be prepared detailing commodity imports that can be reduced.

**Third: Strengthening Banking Control**

1 Developing and regulating the exchange sector and strengthening control and supervision by taking the following strict measures in dealing with manipulators in the exchange market:

- Closing all unlicensed exchange firms and not issuing any new licenses. License fees, warranty amounts and licensing mechanisms should be reviewed, considering the global best practices, and aiming to reduce the unjustified widespread of exchange firms.
- Controlling all exchange sales and purchases operations and obliging exchange firms to comply with the provisions of the law regarding selling surplus of foreign exchange and not retaining liquidity, which must be deposited to banks.
- Strengthening control and oversight on the operations of transfer networks.
- Controlling operations taking place in the exchange sector and transfers to and from Houthi-controlled areas and taking strict actions against offenders.
- Reviewing the value of fines currently imposed by the Central Bank on exchange firms, and taking deterrent actions against offenders.
- Strengthening anti-money laundering and terrorist financing measures in the exchange sector and dealing with any suspicious operations.

2 Activating the role of banks. Measures should be taken to improve the capacity of banks in areas controlled by the legitimate government and strengthen their role in pushing the wheel of the economy forward. The following actions should be taken:

- Strengthening the role of commercial banks in Aden.
- Strengthening AML and CTF measures, controlling the currency exchange and transfer operations.

## 7. Governance and Building Capacity

**Central Bank Institutional Building/ structure**

1. Promoting communication channels and the exchange of information between the Central Bank and the government, which is achieved by providing the government with needed reports.
2. Providing the Central Bank with the programs necessary to strengthen its operations.
3. Improving the capacity of specialists in research and statistics.
4. Enhancing Central Bank governance.

**Institutional Structure of the Ministry of Finance and Tax and Customs Authorities**

1. Improving Ministry of Finance staff capacities in budget planning, execution, and control. This requires first to hire more staff to fill the current gab for Ministry of Finance to perform its main functions more effectively and efficiently.
2. Strengthening tax administration's capabilities to mobilize more revenues along with providing essential systems and staff.

3. Building the organizational structure of the Ministry of Finance as well as providing the necessary systems and software.

Institutional Building of Other State Institutions

1. Strengthening the role of the Central Organization for Control and Accountability and the Supreme National Authority for Combating Corruption and providing appropriate technical support to carry out their work in monitoring the work of government institutions in accordance with the laws in force.
2. Strengthening the role of the Supreme Economic Council.

## 8. Encouraging Investment and Improving Public Service Provision

To prevent further deterioration and promote economic stability, in addition to the financial and monetary policy reforms plan, the government should focus on reforms in the investment context and the good use of SDRs. Government measures should aim to enhance food security and access to commodities at affordable prices as well as improving public services — mainly electricity — in the short to medium terms. Such measures should also include adopting investment promotion objectives to encourage economic growth through a long-term strategy aimed at comprehensive reforms in the post-conflict investment milieu. In this context, three main points will be addressed:

1. **Best SDR investment**: In August 2021, Yemen acquired its share of IMF Special Withdrawal Rights that are roughly equivalent to $655 million. SDRs may not fix the structural deficiencies of the national economy in the long run but using this allocation wisely and in a transparent manner will undoubtedly contribute to supporting the economy.
   - Formulating an effective investment vision that enables this allocation to be used in interventions and projects that contribute to the stability of basic commodity prices and support economic priority projects that promote economic growth.
   - Developing a set of measures and procedures to ensure retrieving the value of used allocation from funded investments.
   - The management module of absorbing the SDRs allocation can be then consider as a start point for developing modules for absorbing fund during the reconstruction phase.

**2. Improving public services:** Focusing on improving public services, particularly power services, is crucial to promoting stability and stimulating growth. The provision of public services has been severely affected by the war, which had a negative impact on all the aspects of peoples' lives. A comprehensive strategy to improve the power sector should be adopted. However, given the limited public resources to finance power investments, sources of funding should be explored, such as investing part of SDR allocation in the power sector, strengthening the public private partnership practices and measures, or working with international institutions (such IFC) or other development partners to support the power sector.

**3. Creating a Favorable environment for Investment:** In the years that followed the outbreak of the war, many obstacles that seriously affected the business environment emerged in Yemen, such as economic downturns, currency collapse, lack of infrastructure, political and security instability, weak state authority and judicial problems are all major factors that contributed to the flight of capital and thereby depriving the country of investments that could have been used to build key projects. Given the multiplicity of factors affecting the investment environment, priority should be given to improving the business environment of existing investments, promoting the participation of the private sector, and easing obstacles as much as possible. In the long run, a favorable investment environment must be created to attract new investments.

In the short- medium terms, focus should be on the following reform priorities to enhance investment environment:

- Lifting any restrictions on the import of all equipment, tools and spare parts for factories and investment projects.
- Stopping any illegal collections of taxes or royalties.
- Creating a Favorable environment for Investment: activating the role of the General Investment Authority from the interim capital of Aden and fully strengthening its role in enforcing the 2011 Law of Investment and reintroducing the Single Window system that was in place before 2015.
- Finding comprehensive solutions to the real estate/ land hostilities, as well as creating favorable political and security conditions for investors.
- Exploring the option of creating an attractive investment environment, e.g., establishing industrial zones (on the borders for instance).
- Strengthening the partnership between the public and the private sectors through the activation /drafting of laws, developing memorandums of understanding, and holding direct meetings with the aim to solve the problems facing the sector and establishing joint committees. Focus should be on strengthening partnership with the private sector as regards public service projects or related projects that reduce unemployment rates.
- The Government should establish a unit to manage partnership with the private sector and learn from the experiences of some countries in this respect.
- Strengthening communication with donors who have previously committed to the implementation of certain projects, motivating them to re-implement these projects and developing a general framework for mutual accountability with them.

**Proposals to Use SDRs in Investment**

**Transportation Sector:**

Recent reports indicate that " transportation and insurance costs contribute toa about 50% of the cost of one KG of. Therefore, following are measures of high priority: 1) allocating part of the SDRs to rehabilitate the ports of Aden and Mukalla, together with introducing reforms in the management of those ports; 2) allocating funds to establish the Commodity Import Guarantee Fund, which will reduce transport and insurance costs and contribute to reducing the cost of food commodities; 3) maintaining, rehabilitating and reconnecting vital roads and bridges, which requires limited funding with the aim of reducing in-land transportation costs based on feasibility study.

**Telecommunication Sector:**

The telecommunications sector is critical to accelerating the process of economic growth, as well as being a key resource of the state budget. The sector has a good infrastructure, namely a wide network of fiber optic lines, which can be utilized to invest upon. Fiber optic lines in liberated areas need to be expanded and an allocation of nearly USD 50 million is needed to improve the efficiency of this sector. Building infrastructure for the provision of 4G services will also strengthen the role of the government in the field of telecommunications. In this regard, the government should strengthen its control of the telecommunication sector.

**Electricity Sector:**

The electricity sector is a top priority, requiring solutions to the energy problems that have been going on for years. Part of the SDRs should be allocated to invest in energy savings alternatives, maintenance of power plants or any other priorities set by the Ministry of Electricity.

**Oil and Gas Sector:**

Exploring the possibility of investing in this sector to increase oil and gas production and thus provide resources for the state budget. In this context, it is important to operationalize the Aden Refinery Company and Yemen Oil Company in refining, importing, or distributing oil, which requires taking decisions to invest in these two companies and strengthen their role due to the positive impact it will have on all aspects of economic life.

## 9. Creating Favorable Political and Security Conditions

1. Fully implementing the Riyadh agreement and supporting the government to carry out its work from the interim capital of Aden.
2. Any economic reforms program should be fully supported by consolidating all state institutions and authorities and should be directly and effectively supported by the Presidency of the state. Local authorities should also be involved by organizing discussions with local authorities with a view to improving security conditions and meeting the requirements of economic reforms at the local level.
3. Sharing the framework with all relevant parties with the aim of mobilizing the necessary support to achieve its goals.

4. Holding direct discussions with the Coalition on easing and eliminating restrictions on exports and imports of goods; supporting and stimulating investment opportunities and reaching out to international partners to support the provision of the technical and financial resources needed to complete the objectives of this framework.

## 10. Expected Difficulties and Risks

1. The continuation of the war exacerbates the problem of the budget deficit and reduces the chances available to the government to finance that deficit.
2. Failure to obtain additional financial support from regional and international partners will reduce the chances of controlling the current deterioration in the economic situation.