Yemens’ Economic Outlook- Spring 2016

The latest MENA Economic Monitor Report - Spring 2016, expects Yemen’s economic and social prospects in 2016 to depend critically on rapid improvements on the political and security fronts.

The country’s economic and social fabric is crippling after one year of conflict. The economy has contracted sharply. Official reporting suggests that the GDP contracted in 2015 by approximately 28%. The escalating conflict since March 2015 has led to widespread disruptions of economic activities and infrastructure destruction. Since the second quarter of 2015, oil and gas exports have come to a halt. Imports have also contracted, except for critical food and energy products. Annual inflation reached around 30% in 2015, and is expected to increase further as the fiscal performance is continuously weakening.

Public finances are under severe stress. The fiscal deficit widened to 11.4% of GDP in 2015 from about 5% of GDP in 2014. Foreign financing of the budget has largely come to a halt, as many development partners suspended their engagement. Where possible, partners moved to emergency and relief operations. Non-hydrocarbon tax collection declined by about 25% compared to 2014. The government had to delay or suspend many public expenditure obligations while servicing wage and interest payment obligations. All premiums on wages were cut. Public investment has come to a complete stop.

The escalated conflict has complicated the management of monetary and exchange rate policy. The 2015 loss in foreign financing and especially in oil and gas exports led to increased pressures on Central Bank of Yemen (CBY) foreign exchange reserves, limiting gradually its space to finance imports while maintaining a stable exchange rate. International reserves declined to less than $2 billion in late 2015 (2 months of imports). Consequently, the CBY stopped in February 2016 supporting imports at the official exchange rate except for wheat and rice. Meanwhile, the government’s reliance on central bank financing of the fiscal deficit has increased domestic debt stock by about 18% of GDP, to an estimated 53% of GDP.

Social indicators were already poor before the 2015 crisis. Yemen has the highest poverty incidence in the Middle East, with about 37.3% of the population living below the poverty line of $2 (2005 PPP) a day per person, and poverty is more widespread and persistent in rural areas. Yemen also has one of the highest malnutrition rates in the world, with almost 60% of children under the age of five having chronic malnutrition, 35% underweight, and 13% having acute malnutrition in 2012.

An alarming humanitarian crisis is unfolding in the face of conflict and war. The civilian death toll is estimated to have exceeded 6000, with about 28,500 wounded. As of end 2015, 2.5 million people were estimated to be internally displaced in Yemen. As in any conflict, the poor are suffering the most: 21.2 million Yemenis or roughly 82% of the population are in need of emergency humanitarian assistance; 14.4 million Yemenis are facing chronic food insecurity, which has increased by 35% since the conflict began; and 19.3 million Yemenis are without safe drinking water or sanitation. According to UN-OCHA, this has led to a sharp increase in malnutrition and disease burden as forced reliance on water from unprotected sources make people, particularly the young, vulnerable to diarrhea and cholera.

Economic and social prospects in 2016 and beyond will depend critically on rapid improvements on the political and security fronts to be able to rebuild the economy. Providing relief and basic humanitarian assistance is needed to the many suffering from the conflict in the short-term. Even in a post-conflict period, the country will depend more than ever on foreign assistance and donor support to recover from this conflict and rebuild confidence, including in its institutions. Restoring peace and political stability is critical for beginning reconstruction and addressing the country’s deep-rooted governance, institutional, economic, social, and environmental challenges.