Yemen Monthly Economic Update[1]

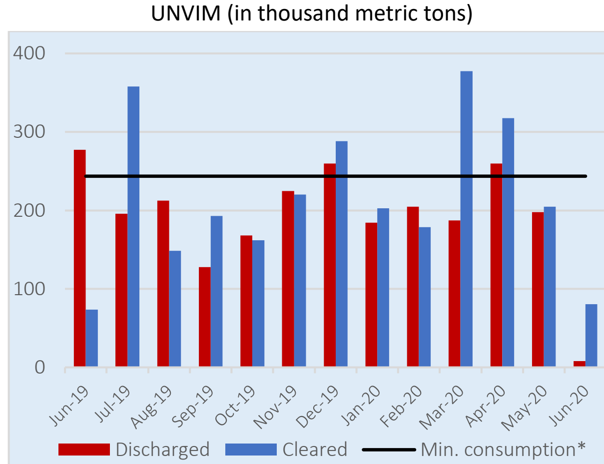
JUNE 2020

The country's socio-economic conditions are deteriorating, affected by the COVID-19 outbreak, downsizing of humanitarian operations, and currency volatility. Severe fuel shortages in the northern governorates jeopardize COVID-19 responses and delivery of humanitarian assistance.

In June, a severe fuel shortage hit Yemen's northern governorates, including Sana'a, disrupting COVID-19 responses and humanitarian operations. The suffocating fuel crisis has affected all aspects of life, threatening access to food, hospital operations, water supplies, which are fuel-dependent and crucial to suppress the virus transmission and to save lives. Reportedly, black market operators are selling fuel products at significantly high prices, sometimes three times or more than the official price.[2] The Yemen Petroleum Company (YPC) in Sana'a attributed the supply shortage to the detention of fuel vessels, despite being inspected and cleared to enter the Hodeidah Port by the United Nations Verification and Inspection Mechanism (UNVIM). Before entering the port, vessels have to receive a final approval from the Government, which ensures importers' compliance with fuel import regulations (Decrees 49 and 75). According to the YPC, as of June 30, 22 ships carrying 500 thousand metric tons of imported fuel products (about 1.5 months consumption needs), already cleared by the UNVIM, were awaiting the Government's approval to discharge.[3]

UNVIM data show a marked decline in the volume of fuel imports discharged through the Hodeidah and Saleef Ports in June against the cleared volume (Figure 1). The Government claimed that the fault lies with the *de facto* authorities for breaking the UN-sponsored agreement on public salary payments. Since November 2019, taxes and customs fees levied on commercial fuel importation through the Hodeidah, Saleef and Ras Issa Ports had been set aside in a special account with the Central Bank of Yemen (CBY) Hodeidah branch and earmarked for salary payments to state employees nationwide, in accordance with the Hodeidah Agreement. The pooled funds, supplemented by transfer from the Government in Aden, were supposed to be left untouched until the warring parties agreed on the mechanism for salary payments and coverage of the

Figure 1. Volume of Fuel Imports Cleared and Discharged via UNVIM (in thousand metric tons)



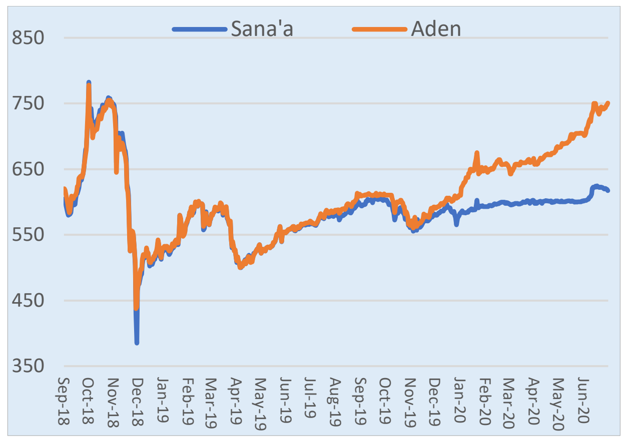
* minimum consumption is for diesel and gasoline products in the northern governorates.
Source: UNVIM and Yemen Petroleum Company (Sana'a).

[1] Prepared by Naoko C. Kojo (Senior Economist) and Amir M. Althibah (Research Analyst) of the Global Practice for Macroeconomics, Trade and Investment, based on information available up to July 7, 2020 and inputs provided by Sharad Tandon (Senior Economist).
[2] According to *FAO-FSIS & MoPIC-FSTS Market Bulletin (#59)*, fuel prices (mostly petrol and diesel) on the parallel market recorded a sharp increase by 308% compared to the national average in May 2020.
[3] http://www.ypcye.com/Show_News.php?id=700 In the first week of July, four ships carrying less than a week of fuel consumption needs, were allowed to enter the port for offloading.

payroll. In April 2020, the *de facto* authorities withdrew funds from the special account to pay half month salaries to civil servants in the northern governorates. The *de facto* authorities stated that the decision to withdraw funds from the special account was made after considerable delays in implementing the agreement.

In early June, depreciation of the Yemeni rial gathered pace in the southern governorates, prompting the CBY (Aden) to impose measures to curb currency speculation. During the first two weeks of June, the rial depreciated by 7 percent from YR 700 to 750 against one US dollar in the southern governorates, amid dwindling foreign reserves, and anticipation of increased monetization of the fiscal deficit (Figure 2). Concerns about falling remittance inflows, growing political uncertainties, and downsizing of humanitarian operations may have also added downward pressure on the rial (Box). Accusing "currency manipulators" of the currency deterioration, on June 9 the CBY (Aden) launched an extensive campaign to curb speculation. Several circulars have been issued, instructing exchange bureaus to trade the rial at a specific exchange rate, while supervision of money exchangers and local money transfer networks (e.g., Kuraimi Express, Al-Najm Transfers) have been tightened significantly.[4] The CBY (Aden) stressed that non-compliant money traders, unlicensed operators and those suspected with speculations, including banks, would be subject to legal measures, including license withdrawal, heavy fines and judiciary processes. On June 13, the Southern Transitional Council (STC) announced confiscation of containers carrying an estimated YR 80 billion (US$109 million) newly printed banknotes from the Aden port on their way to the CBY (Aden), claiming that this was a necessary action to prevent a further circulation of new banknotes and thereby protect the value of the rial.[5] The Government condemned STC's action and demanded the handover of the YR 80 billion confiscated unissued banknotes.[6]

Figure 2. Parallel Market Exchange Rates
(Daily Average, YR/US$)



Source: Data collected from Informal exchange rate markets and staff estimates.

The pace of rial depreciation slowed in late June, but this is likely be short-lived. On June, in protest against the "arbitrary" measures imposed by the CBY (Aden), the Money Exchange Association of Aden announced a closure of all exchange bureaus in the city. In response to the Association's criticism, the CBY (Aden) issued a statement early July, reiterating the legality of its enforcement measures.[7] As of end-June, the rial was trading at about YR 750-755 per US dollar while the strike of exchange companies

[4] According to the official website of the CBY (Aden), the rate was set at YR 180 for purchase and YR 181 for sale against the Saudi Arabia rial (equivalent to YR 684 for purchase and YR 690 for sale against the US dollar). In mid-June the parallel market exchange rates were estimated at about YR 197 per Saudi rial and YR 748 per US dollar on average.
[5] https://stcaden.com/news/12129 The US dollar value is calculated based on the average parallel exchange rate of the rial that prevailed in Aden during June (YR 735/US$).
[6] The notes were eventually handed over via the Coalition forces in July. The seizure of currency and its resolution will be covered in the July edition.
[7] https://www.cby-ye.com/2020/07/%d8%a8%d9%8a%d9%80%d9%80%d9%80%d9%80%d9%80%d9%80%d8%a7%d9%86/

remained in place, which has caused paralysis of the exchange process and transfers. Although the CBY's campaign and the closure of money exchangers may have arrested the rial's free fall, this is unlikely to have a lasting effect unless the root causes of the currency depreciation are addressed. Downward pressures on the rial are likely to continue. Given Yemen's heavy reliance on imports, depreciation of the currency is expected to have a knock-on impact on the prices of imported commodities, eroding households' purchasing power.

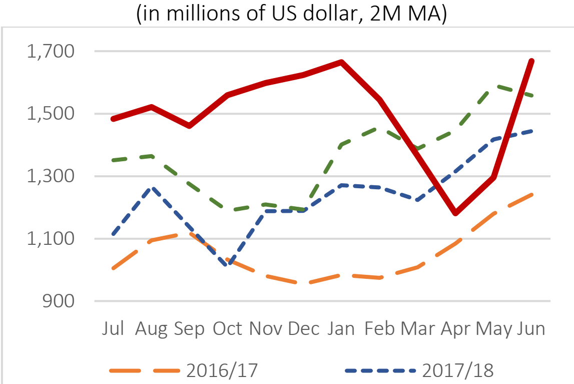
Box. Are remittance inflows to Yemen falling? An Update.[a]

There are mounting concerns that remittance flows to Yemen have declined significantly, as the economies of the Gulf Cooperation Council (GCC) countries, the main source of remittances to Yemen, is dragged by the sharp decline in oil prices, production cuts and stringent measures to contain COVID-19. The lack of reliable information on the volume of remittance receipts may have contributed to rising uncertainty about the availability of foreign exchange and in turn may have encouraged speculation on the exchange rate.

The economic prospects for the GCC economies remain uncertain. However, there is emerging evidence that remittance outflows from the GCC, through the formal financial sector channel, have remained resilient to the economic slowdown caused by the COVID-19 pandemic, consistent with historical observations. Saudi Arabia's balance of payments data suggest that outward remittances from the country increased by 5 percent in the first quarter of 2020 (2020 Q1), compared with the same period in 2019. Similarly, the United Arab Emirates reports a 7.8 percent increase in remittance outflows during 2020 Q1 year on year. Outward remittances from Qatar in 2020 Q1 remained at the same level as a year earlier. Despite these positive developments, there are concerns that remittance inflows via informal channels (e.g., through workers crossing the border) may have been affected negatively by the closure of border with Saudi Arabia due to the pandemic. Reduced opportunities to send money through informal channels may have shored up financial transfers from the GCC through the formal financial system.

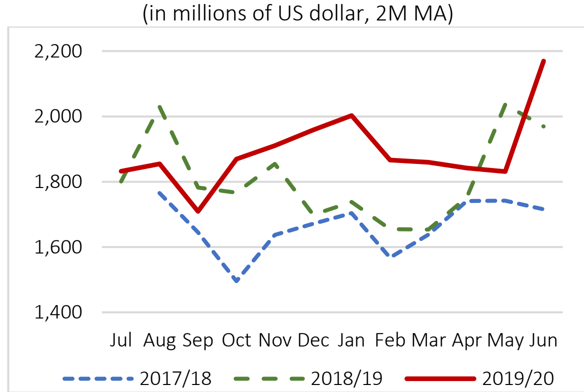
Encouraging evidence is also reported by recipient countries. Monthly data released recently suggest that workers' remittances to Bangladesh and Pakistan—both of which, like Yemen, receive a predominantly large share of total inward remittances from the GCC countries—are recovering strongly, reversing the downward trend witnessed earlier in 2020 (Figures B1 and B2). Remittance inflows to Bangladesh rose sharply to US$1.8 billion, a 21 percent increase from May. Workers' remittances to Pakistan increased by 32 percent in June compared with May, recording a historic high of US$2.5 billion. Pakistan's central bank attributes the significant increase in June to the easing of lockdown in the host countries, which allowed overseas Pakistanis to transfer funds, which they were unable to send earlier. Strengthened incentives, introduced in both countries in 2020Q2 to encourage money transfer by expat workers through legal channels, may have also contributed to the marked recovery of inward remittances to Bangladesh and Pakistan.

Figure B1. Bangladesh Wage Earners' Remittance
(in millions of US dollar, 2M MA)



Source: Bank of Bangladesh.

Figure B2. Pakistan Workers' Remittances
(in millions of US dollar, 2M MA)



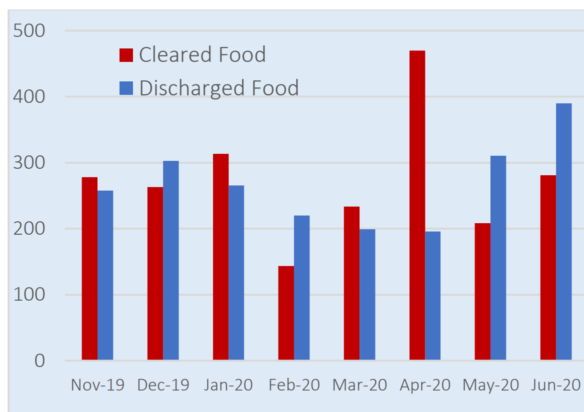
Source: State Bank of Pakistan

a/ See *Yemen Monthly Economic Update, May 2020*,World Bank.

Increased volatility of the rial was also observed in the northern governorates after months of relative stability. During the first two weeks of June, the rial declined from YR 602 to YR 625 per US dollar—the largest fluctuation since the ban on new banknotes was tightened in December 2019, likely triggered by the sharp depreciation in the southern governorates. Concerns about reduced remittance inflows and downsizing of humanitarian operations were also present in the northern governorates, which may have contributed to increased currency volatility. To restore currency stability, the CBY branch in Sana'a stepped up its supervision while tightening access to foreign exchange. On June 15, the Payment Committee in Sana'a announced the sale of SR 40 million (about US$10.7 million) to finance essential food imports in the northern governorates.[8] On July 6, a circular was issued, prohibiting exchange bureaus from selling foreign currency directly or indirectly to merchants and importers of four sectors (including those of petroleum products and basic food items), whose foreign exchange needs are covered by the Payment Committee of the CBY branch in Sana'a. These measures have helped to ease market jitters, allowing the rial to appreciate.[9] By the end of the first week of July, the rial returned to about YR 596-598 per US dollar in Sana'a. The exchange rate gap between the northern and southern governorates continued to widen during June, reaching nearly YR 134 (about 30 percent) at the end of the month, compared with YR 103 (17 percent) at end-May.

In an encouraging development, the volume of food imports through the Hodeidah and Saleef ports continued to recover in June. According to data from the UNVIM for Yemen, the volume of monthly food imports discharged at the Hodeidah and Saleef ports in June increased by nearly 26 percent from previous month, as the cargos inspected and cleared by the UNVIM in the previous months were allowed to enter the ports to off-load (Figure 3). The total amount of food discharged via Hodeidah and Saleef in the first half of 2020 was 11 percent lower compared to the same period in 2019.

Figure 3. Volume of Food Imports Cleared/ Discharged via UNVIM (in thousand metric tons)



Source: UNVIM.

Food prices spiked sharply in the southern governorates in June. According to the latest *FAO-FSIS & MoPIC-FSTS Market Bulletin*, the national average cost of Minimum Food Basket (MFB) rose to YR 41,950 (about US$63) in June, 4 percent above the MFB in May (Figure 4). The national average MFB increased by 15 percent since the beginning of 2020.[10] Food price increases were particularly pronounced in the southern governorates, driven likely by the large depreciation in the rial. The MFB cost increased, month to month, by 18 percent in Aden, 13 percent in Lahji, and 11 percent in Dhalee, raising concerns about the impact on households. In sharp contrast, the MFB cost declined markedly by 7 percent in Sana'a and remained stable in most of other northern governorates during June, despite the acute fuel shortages. The *Bulletin* reports that ongoing

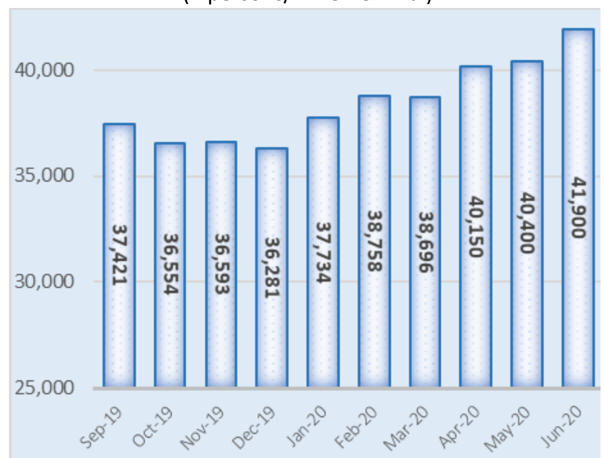
[8] https://www.saba.ye/ar/news3099664.htm

[9] The Payment Committee in Sana'a oversees demand and supply of foreign exchange in the northern governorates to avoid excessive volatility of the exchange rate.

[10] *FAO-FSIS & MoPIC-FSTS Market Bulletin June 2020 (#59).*

COVID-19 related movement restrictions continued to impact export potential of vegetables and fruits to neighboring countries, leading to significantly increased supply of these products locally. Prices of vegetables and fruits went down. Yet this was not reflected in the MFB, as vegetables and fruits, along with many other food commodities consumed by households, are not included in the MFB.[11] Food prices are expected to rise further in the southern governorates, as the official prices of petrol and diesel were adjusted upwards in July.[12]

Figure 4. Average Monthly Cost of Minimum Food Basket (7 persons/in Yemeni rial)



Source: FAO-FSIS & MoPIC-FSTS Market Bulletin June 2020 (#59).

While Yemen continues to grapple with COVID-19, many aid agencies scaled down humanitarian operations due to funding shortfalls. Since the first officially confirmed case was reported in April, COVID-19 has spread rapidly across Yemen with deadlier consequences.[13] Yemen's capacity to fight the virus is severely constrained by the erosion of health facilities due to 5 years of violent conflict, shortage of medical equipment and supply, poor health conditions (malnutrition, diarrhea, lack of access to clean water and basic sanitation), and a total lack of fiscal space. The mobile Vulnerability Analysis and Mapping (mVAM) conducted by the World Food Programme (WFP) finds emerging signs that access to medical care is declining and the capacity of health centers is becoming overwhelmed, particularly in Aden, where the reported spread of COVID-19 is more prevalent.[14] The downsizing of humanitarian operations came at the worst time. Since mid-April, 31 of 41 critical UN operations have closed or downsized for lack of funding, with significantly reduced number of people receiving life-saving aid. Delivery of water, sanitation and hygiene (WASH) assistance necessary to suppress the spread of the virus and other diseases was significantly cut down in June due to the lack of funding, which was compounded by increased cost of fuel.[15]

Public sector salary payments remained irregular in the southern governorates in June. Disbursement of salaries was frequently delayed, and the geographic coverage was uneven. Salary payments appear to have been made regularly to civil servants in the central ministries in Aden, including the Revenue Authorities. Since December 2019, no public sector workers in the northern governorates have received

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[11] The MFB consists of wheat flour, dry weight beans, vegetable cooking oil, sugar and Iodized salt.

[12] The retail prices of petrol and diesel increased by 70 percent 27 respectively, according to *FAO-FSIS & MoPIC-FSTS Market Bulletin June 2020 (#59).*

[13] *Yemen Humanitarian Update Issue 6 (June 2020)*, OCHA.

[14] The finding is based on monthly mobile phone surveys conducted during May-June 2020. Since July 2015, the WFP has been performing remote phone-based data collection and food security monitoring in Yemen through the mVAM approach. Survey respondents are contacted through a call center and asked to respond to a short series of questions on household food consumption, coping and access to food assistance. Beginning in March 2020, the survey covers approximately 4,200 respondents each month, and each survey reaches just over 140 respondents each day of the month.

[15] *Yemen - Humanitarian Dashboard (January – June 2020)*, Wash Cluster.

regular salaries from the Government.[16] With the sharp drop in global oil prices, government oil revenue (oil exports and taxes on cheaper imported fuel) has declined in 2020. The diversion of government revenue to the STC's so-called "self-rule" accounts with the Al Ahli Bank has further disrupted public financial management by the Government and made regular salary payments difficult.[17]

[16] During 2019, the Government made partial salary payments to a limited number of civil servants in the northern governorates working in judiciary, health and higher education. These payments have been suspended since December 2019 when the ban on new banknotes were tightened by the *de facto* authorities in Sana'a.

[17]During April-May, the *de facto* authorities in Sanaa disbursed half of January 2018 salaries to civil servants in the northern governorates, drawing resources from the special account with the CBY branch in Hodeidah. For further information, see *Yemen Monthly Economic Update, April* and *May 2020*, World Bank.