Yemen Monthly Economic Update[1]

MAY 2020

In May, political volatility continued, while socio-economic conditions deteriorated further, affected by the COVID-19 outbreak, rising food prices, and downsizing of humanitarian operations, especially in the northern governorates.

COVID-19 is spreading rapidly across Yemen, adding further strains on the country's already stretched health care capacity. Only 50 per cent of health facilities in Yemen are currently fully functioning, and those that continue to function lack basic equipment such as masks and gloves, oxygen and other essential supplies for the treatment of COVID-19. The private sector health care system is underdeveloped, and equally suffers from the shortages of medical supplies and trained health workers. The country's capacity to deal with increasing cases of COVID-19 is further compromised by the increasing cases of other infectious diseases. The Government has called for the formation of a joint committee to coordinate efforts to confront COVID-19 throughout Yemen, while liaising with the international community to raise funds to respond to the pandemic.

Following its self-declared autonomy in the southern governorates in April, the Southern Transitional Council (STC) moved during May to organize its relationship to some economic and social service government institutions in Aden. On May 11, the STC announced a Supreme Economic Committee with up to 27 expert members.[2] The Committee, which reports directly to STC leadership, is assigned by the STC to provide supervision and guidance on economic management to government institutions in Aden. Other key responsibilities include the preparation of reform agendas to address issues with public services delivery (electricity, water, health care) and improve overall efficiency in the public sector. In addition, task teams have been formed to monitor government financial flows.

Reportedly, several revenue-collecting government institutions in Aden have deposited public revenue into the so-called "self-rule" accounts with the Al Ahli Bank, in response to the STC's request. According to the public statement by the STC, major economic institutions such as the Customs, Tax Authority, Aden Refinery Company, Port of Aden, and Authority of Aden Free Zone are among those reported to have complied with the request.[3] It is not clear if the STC has gained oversight over oil exports, the central source of government revenue. The STC stated that the measure was intended to enhance transparency of the use of public resources, fulfill payroll obligations, and rationalize the recourse to money printing to finance the deficit, but not to overrule the existing budget framework.

The Government labeled the STC's move as "a rebellion against government institutions in Aden", and ordered to close the STC's accounts with Al Ahli Bank. The Government asserts that many institutions (including Customs and Tax Authorities, Aden Refinery Company, Oil Exports and Yemeni Economic Corporation) are still depositing revenue to the Central Bank of Yemen (CBY) in Aden, which enabled salary

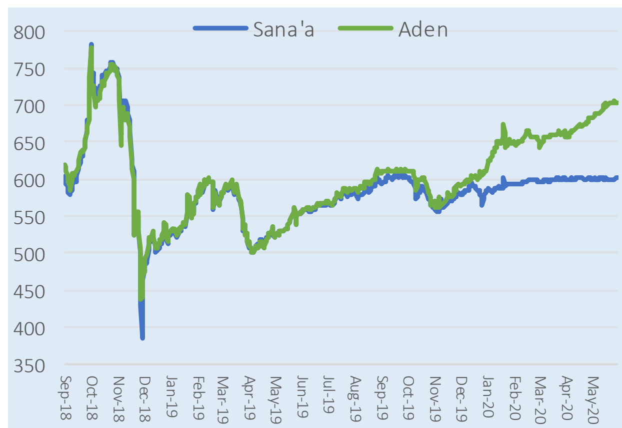
[1] Prepared by Naoko C. Kojo (Senior Economist) and Amir M. Althibah (Research Analyst) of the Global Practice for Macroeconomics, Trade and Investment, based on information available up to June 8, 2020.
[2] Per decree 21 of 2020; https://en.stcaden.com/news/9165
[3] https://stcaden.com/news/11876

payments to government workers. Nonetheless, sources suggest that public sector salary payments remain irregular and partial across Yemen. In southern governorates controlled by the Government, stagnation of salary disbursements was first reported in early 2020.

Meanwhile in Sana'a, the *de facto* authorities implemented a series of legislative economic reforms aiming to improve the business environment in their controlled territory (the northern governorates). On May 3, 2020, the *de facto* authorities issued Laws No. 5 to No. 8 (2020), ratifying amendments to the Custom Tariff Laws, General Sales Tax Law and Income Tax Law.[4] The legislative revisions are part of the economic measures under the Economic Revival and Recovery Strategy 2019-20, announced in January 2020.[5] The amendments provide tax exemptions to support small businesses, strengthen local production of medicine, and facilitate renewable energy investment to reduce reliance on imported fuel products. During April-May, half of January 2018 salaries were disbursed to civil servants in the northern governorates, drawing resources from the special account with the CBY branch in Hodeidah.[6]

In mid-May, the parallel market exchange rate of the Yemeni rial crossed the YR 700/US$ mark for the first time since November 2018 in the southern governorates. The rial continued to depreciate moderately by about 3.7 percent per US dollar during May, compared with 1.9 percent in April, amid dwindling foreign reserves and anticipation of increased monetization of the fiscal deficit (Figure 1). In early June, however, the modestly declining trend changed dramatically. During the first week of June alone, the rial fell by more than 3 percent, from YR 701/US$ to YR723/US$, possibly triggered by the unmet expectations for the donor pledging event held on June 2.[7] Reportedly, the CBY in Aden instructed exchange bureaus to suspend currency trading, accusing "currency manipulators" and "corrupt money exchangers" of the depreciation of the local currency.[8] The exchange rate of the rial remained stable at YR 600-602 per US dollar in the northern

Figure 1. Parallel Market Exchange Rates
(Daily Average, YR/US$)



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

[4] https://www.saba.ye/ar/news3095918.htm; https://www.saba.ye/ar/news3095917.htm; https://www.saba.ye/ar/news3095913.htm https://www.saba.ye/ar/news3095909.htm

[5] For further information, see *Yemen Monthly Economic Update, January 2020.*

[6] Further information is available in *Yemen Monthly Economic Update, April 2020.*

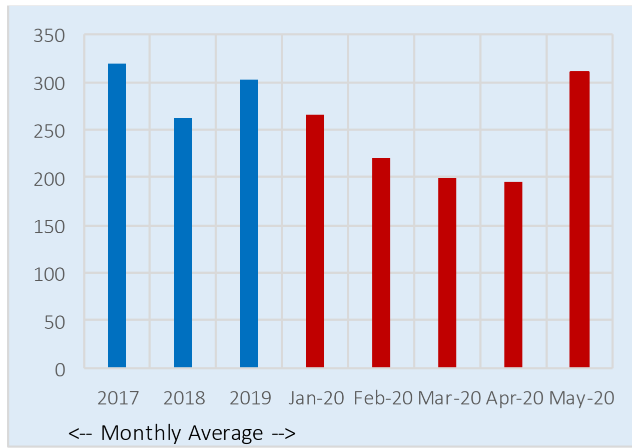
[7] On June 2, a high-level donor pledging event was organized by the Kingdom of Saudi Arabia (KSA) and the United Nations (UN) to raise additional funds to support humanitarian emergency responses in Yemen around 54 percent of the total requested by the UN for Yemen 2020 Humanitarian Response Plan (HRP) Extension to assist 19 million people with life-saving aid between June and December 2020.

[8] Sources suggest that the CBY (Aden) instructed exchange bureaus to either suspend currency trading, or trade at the exchange rate prevailed in May (YR 700 – 705/US$). On the following day, most exchangers complied the CBY's instruction to purchase US dollars at the prescribed rate, but refused to exchange the rial to hard currency or traded under the table to avoid the risk of being blacklisted for non-compliance.

governorates due to the monetary measures implemented in December 2019.[9] The wedge between the two parallel market exchange rates reached YR 100 or 17 percent at end-May. Going forward, downward pressure on the rial is expected to intensify given the bleak prospect for remittance inflows, especially from the neighboring countries, and the absence of external financial support (See Box). Demand for foreign currency is expected to soar, driven by the recovery of trading activity in China (a major trading partner for Yemen) and post-Ramadan stock replenishments by Yemeni importers.[10] Given Yemen's high dependence on imports, depreciation of the rial would have a knock-on effect on the prices of imported commodities, with dire economic and humanitarian consequences.

While the volume of food imports through the Hodeidah and Saleef ports recovered in May, there remain concerns over food security in Yemen, especially in the northern governorates. According to data from United Nations Verification and Inspection Mechanism (UNVIM) for Yemen, the volume of food imports discharged at the Hodeidah and Saleef ports increased to a level comparable to the annual monthly average for 2019 (Figure 2). The discharged imports in May are mostly cargos that were inspected and cleared by the UNVIM in April but were unable to enter the port for discharge. During the first 5 months, food imports through Hodeidah and Saleef amounted to only 77 percent of food imports for the same period in 2019. Besides delays in entering the port, the decline in the discharged volume of food imports in the northern governorates could be explained by a couple of factors, including shortages of foreign exchange, COVID-19 related sluggishness in trade activity, and a possible downsizing of humanitarian assistance in the northern governorates (see below), which led to reduced food imports by humanitarian agencies.[11] The volume of new food imports cleared in May through UNVIM declined by nearly 56 percent from previous month (nearly 32 percent below the monthly average cleared in 2019).

Figure 2. Volume of Food Imports Discharged via UNVIM*
(monthly average, thousand metric tons)



Source: UNVIM.

[9] For further information, see *Yemen Monthly Economic Update, December 2019.*

[10] According to data released by the National Bureau of Statistics of China, exports (in value) from China bottomed out in April, growing by 3.5 percent year on year (y/y), after sharp contractions in February (-17.2 percent y/y) and March (-6.6 percent y/y).

[11] Russia's wheat export ban remains in place. Yemen imports a large quantity of wheat from Russia. See *Monthly Economic Update, March 2020*, for details.

Box. Are remittance Inflows to Yemen Falling?

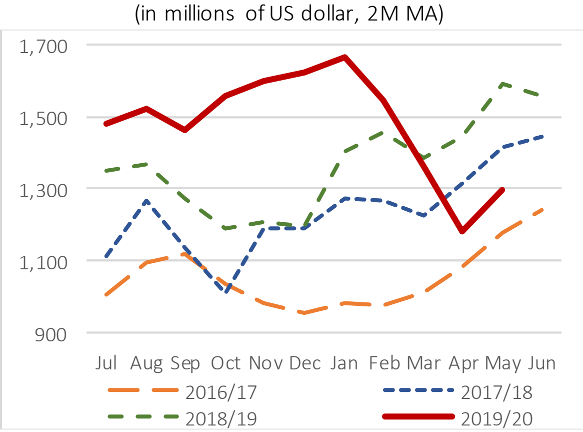
Financial transfers from Yemeni migrant workers overseas have become an important part of their households' disposable income in Yemen since the current conflict began 6 years ago. Given the significant COVID-19 related economic downturn worldwide, there are growing concerns that employment opportunities and wages for Yemeni migrant workers may be hit hard, leading to a sharp contraction of remittance inflows to Yemen, especially from the neighboring Gulf Cooperation Council (GCC) countries, the dominant source of inward remittances for Yemen.

Are remittance inflows to Yemen declining due to the economic fallout of COVID-19? Evidence is not yet available to confirm this. Indeed, obtaining reliable information on remittance flows is notoriously difficult in many countries. While balance of payments (BoP) statistics capture remittances (the sum of compensations to employees and personal transfers) that are channeled through a formal financial system, transfers channeled through informal channels (hawala or physical transit across the borders with Saudi Arabia) are not recorded in BoP statistics. In Yemen, obtaining remittance information, let alone any other economic statistics, is even more challenging due to the fragmentation of capacity. What is available is partial and on an annual basis only. In other words, there are no reliable, high frequency data at present to confirm whether inward remittances to Yemen have declined in 2020 because of COVID-19.

Historical observation suggests that remittance flows to developing countries tend to be relatively resilient to economic shocks. For instance, in the aftermath of the global financial crisis in 2008, remittance flows to developing countries (Sirkeci, et al. 2012)[a] Defying expectations, inward remittance flows to most south Asian countries (Bangladesh, Maldives, Nepal, Pakistan and Sri Lanka) did increase 2009 and continued to grow in 2010, due to strong remittance flows from GCC countries, the predominant source of remittances to South Asia. Estimates suggest that inward remittances to Yemen also withstood during the global financial crisis and beyond.[b]

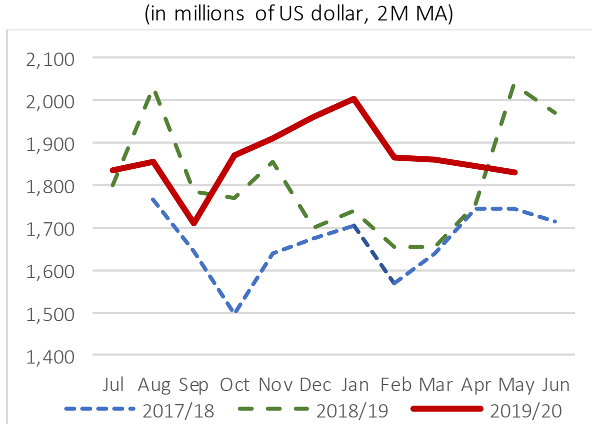
Will remittances to developing countries remain resilient again this time? It is too early to tell, but available evidence is not too assuring. As of end-May 2020, high frequency data are available only for Bangladesh and Pakistan, both of which receive nearly 60 percent of their total inward remittance flows from the GCC. Data from the Bank of Bangladesh suggest that wage earners' remittances through the formal financial system plunged in the first months of 2020, before recovering slightly more recently (Figure B1). Inward remittances to Pakistan also exhibit a downward trend in 2020. Yet the decline here is not as dramatic as in Bangladesh (Figure B2), and the total amount of inward remittances during January-May 2020 (US$9.3 billion) is still larger than during the same period in 2019 (US$9.1 billion) and 2018 (US$8.4 billion).

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

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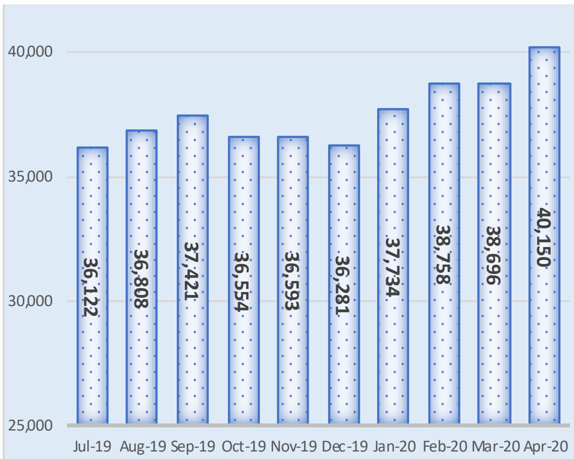
a/ Sirkeci, Cohen and Ratha, eds. (2012), *Migration and Remittances during the Global Financial Crisis and Beyond*.
b/ World Bank staff estimates based on IMF balance of payments data.

Figure 3. Average Monthly Cost of Minimum Food Basket (7 persons/in Yemeni rial)



FAO-FSIS & MoPIC-FSTS Market Bulletin April 2020 (#57).

Food prices rose markedly in April, posing a threat to the already dire humanitarian conditions. According to the latest *FAO-FSIS & MoPIC-FSTS Market Bulletin*, the national average cost of Minimum Food Basket (MFB) in Yemen increased by almost 4 percent to YR 40,150 per month (about US$64) in April from YR 38,696 (about US$62) in March (Figure 3). The price increase in April was driven by increased demand for food commodities during Ramadan, security conditions, and COVID-19 related movement restrictions, which raised transport cost of perishable food prices.[12] Retail prices of imported food commodities hiked at an accelerated pace in April, driven possibly by the combination of reduced food imports and downsizing of humanitarian assistance that began in mid-April in the northern governorates.[13, 14] Higher price increases were observed in Aden, Marib, Lahj, and Sana'a, where devastating rains and flooding in April destroyed crops, food stock and livelihoods. Food price levels are generally higher in the southern governorates, on average, than in the northern governorates, likely reflecting the wedge between the two exchange rates. Going forward, there are concerns that sweeping swarms of desert locust may significantly damage agricultural crops, exacerbating food insecurity. The World Food Programme (WFP) is currently conducting a mobile Vulnerability Analysis and Mapping (mVAM). The results, expected in late June, would shed light on the impact on households and vulnerable population.

[12] According to the *FAO-FSIS & MoPIC-FSTS Market Monitoring Bulletin (March 2020)*, traders are taking longer routs to deliver foods at a greater cost, in order to avoid COVID-19 related movement restrictions strictly enforced on most direct intra-governorate routes.

[13] Among imported food items, sugar exhibited the highest price increase during April (9.5 percent), followed by cooking oil (8.9 percent) and non-basmati rice (5 percent). Retail prices of all monitored imported commodities (wheat, rice, cooking oil, sugar and beans) except for beans increased by over 10 percent year on year.

[14] According to the *OCHA Yemen Situation Report (June 2020)*, since mid-April 2020, more than 30 core UN programs have been downsized or closed due to the lack of funding.