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Yemen's Economic Agenda: Beyond Short-Term Survival

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The Post-Uprising Economy

With Yemen's National Dialogue process approaching completion, the nation is poised to move to the next stage of its transition. Now is the time for the government to address not only demands for more inclusive political participation, but also the economic aspirations of most Yemenis who have not experienced any improvement in their standard of living since the 2011 popular revolution. Without making progress on the economic front a priority, the democratic transition process risks derailment and its leadership a complete loss of credibility, which could result in renewed conflict. For too long, taking tough economic decisions has been postponed because of political uncertainty, but the status quo can no longer continue if the country is to emerge from its near failed-state status.

Two and half years after youth demonstrators sparked a popular uprising that ousted former President Ali Abdullah Saleh, incremental progress has been made by President Abdrabo Mansour Hadi since he assumed the presidency in February 2012, but little headway has been made to address the underlying objectives of the revolution, many of which were economic in nature. The political class in Sana'a has been entirely consumed with the National Dialogue, a six-month plus process to address the most pressing issues left unresolved by the Gulf Cooperation Council (GCC)-supported transition plan, including southern demands for secession, the Houthi conflict in the north, and the system of government and prospects for a federal state. While a necessary and positive part of the process, the Dialogue also had the unfortunate consequence of sucking the oxygen out of the political space and policymaking environment, thus leaving a great deal of urgent work unfinished.

Focusing on Yemen's precarious economic situation is urgent because most of the current problems can be traced back to weak state institutions and poor economic management that will not be repaired through the Dialogue or a new constitution. As the poorest country in the region with a per capita GDP of $1,500, more than 54 percent of the population under the poverty line, and a young, unskilled, low productivity labor force, Yemen faced grave challenges before the uprising even began.[1] When violent conflict raged throughout the country in 2011, the economy contracted at least 10 percent, fuel and energy costs skyrocketed, major infrastructure projects were halted, and the result was an acute unemployment problem. The transitional government is still struggling to address ongoing humanitarian pressures that are not abating, with 10 million people deemed as food insecure, 24 percent of urban households unable to find sufficient food sources, more than one million children severely malnourished, and 12.7 million people lacking clean water and sanitation services.[2] This September, the United

1 Information from World Bank DataBank and World Bank Joint Social and Economic Assessment, Republic of Yemen, August 2012.
2 UNCHR Factsheet, April 2013, http://www.unhcr.org/4c907a4a9.html.

Nations announced that Yemen is in dire need of additional donor support to deal with the most critical and basic needs of its struggling population.[3]

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With the cessation of active hostilities, Yemen witnessed considerable stabilization by 2013 with GDP growth returning to 2.4 percent, the currency regaining its value (in large part due to a $1 billion deposit from Saudi Arabia), and capital expenditures resuming.[4] The International Monetary Fund gave Yemen a $94 million Rapid Credit Facility in April 2012 that provided emergency assistance and helped stabilize the situation. But the relatively minor improvement in macroeconomic indicators have not translated into new job opportunities or improved quality of life for the vast majority of the population. Now with the dialogue set to conclude in the coming months, the government should turn its attention to addressing the population's economic needs.

Economic Stabilization versus Economic Reforms

What has been glaringly absent from most conversations about Yemen's delicate transition is the need to focus on transforming the economic environment and actually implement the short-, medium-, and long-term plans that were put on paper. In an effort to stop the economic bleeding, the transitional government developed a fairly comprehensive Transition Plan for Stabilization and Development (TPSD), with considerable input from the World Bank, in advance of the Riyadh donors' conference in September 2012. The document outlines priority areas for the government, with the objective of matching donor assistance according to the framework. By design, the TPSD has a short-term orientation and stops short of laying out a full economic agenda for the country to move forward. When pressed on this point, ministers in the transitional government reply that their mandate is limited to implementing the GCC agreement and does not extend to charting a course for Yemen's economic future. But even if the benchmark is the plan set forth in the TPSD, one is struck by how little has been achieved.

The transitional government would attribute the lack of progress to the difficult security environment and the slow disbursement of internationally pledged funds. The Friends of Yemen[5] meetings and donor conferences over the past two years have produced significant financial pledges reaching nearly $8 billion by August 2012, roughly three-quarters of what the Yemeni government sought for its two-year stabilization plan. Yet by September 2013, the government reported that only $2.2 billion has been transmitted, including a one-time $1 billion central bank deposit from the government of Saudi Arabia, which helped stabilize the currency, but had little other tangible impact on the ground. Nearly 80 percent of the pledged amounts have been "allocated," meaning they have been assigned specific projects or initiatives, but allocation on paper means little until it is transferred and projects begin. Yemen will likely remain oriented toward donor assistance for the foreseeable future, but such funds are unpredictable, highly politicized, and may not be forthcoming, as happened with the 2006 Friends of Yemen pledges. Yemenis lament that the wealthy Gulf states, which pledged the

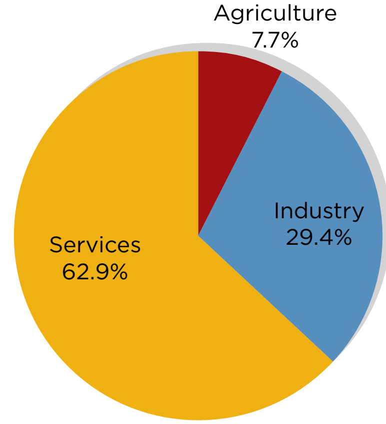
3 "Secretary-General's Remarks at Friends of Yemen Ministerial Meeting," United Nations, September 25, 2013, http://www.un.org/sg/statements/index.asp?nid=7129.

4 International Monetary Fund, *Republic of Yemen: 2013 Article IV Consultation*, report no. 13/246 (Washington, DC: IMF, 2013), 30.

5 The Friends of Yemen forum was first introduced in 2006, then reinitiated in 2010, in order to leverage international support and political, economic, and humanitarian assistance to Yemen. The Friends of Yemen is now co-chaired by the United Kingdom, the Kingdom of Saudi Arabia, and the Republic of Yemen, and has the support of thirty-nine countries and international organizations.

Table 1. Yemen's Economic Data (2012)	
Population (millions)	26 million
Real GDP growth (2012)	2.4%
Nominal GDP (US billions)	$35.4
GDP per capita	$1,500
Fiscal deficit (% of GDP)	6.3%
Energy subsidies(%of GDP)	9%
Unemployment rate (% of total labor force)	35%
Unemployed youth (% of 18-24 years old)	50-70%
Population under poverty line	54%
Food insecurity (millions, of total population)	10.5
Food insecurity (%, of total population)	44%
Malnourished (%, of total population)	31.7%, including 1 million children under age 5

Composition of Yemen's GDP



Sources: IMF, World Bank, UN Data, SEDRC, UNDP, ILO, UNICEF, OCHA, Yemen's Ministry of Public Health and Population.

most and have the most at stake in ensuring their neighbor's stability, have not delivered. On the flip side, Gulf countries and other donor governments complain that the Yemeni government lacks the capacity to prepare and implement projects and have yet to put in place the necessary mechanisms to instill confidence. It appears both sides are correct, and both sides are to blame.

The donor funds are meant to support the laundry list of infrastructure projects and other initiatives detailed in the Public Investment Program (PIP) for 2011-15, developed by the Yemeni government prior to the outbreak of the uprising, but some donors make their own decisions about what is most needed or aligned with their own national priorities. And many of the line items included in the Friends of Yemen pledges are for development projects already underway or humanitarian assistance that is urgently needed but does not address service delivery or unemployment. Compounded with the slow pace of disbursement, it is not surprising that few Yemenis actually feel the impact of the much lauded $8 billion promised by the international community.

Partially in response to demands from the international community, Hadi agreed to create an Executive Bureau to expedite project implementation, provide oversight, and coordinate and streamline donor assistance. Unfortunately, the way the Executive Bureau was designed severely hamstrings its ability to play a strong role and does not empower its director to cut through time-consuming bureaucracy and red tape. The Bureau has been plagued by a tug-of-war among the relevant ministries, donors, and international financial institutions (IFIs) that each want it to serve their own interests. After months of delay, the donors and major political parties finally concluded that they should hire someone outside the country to run this institution. Nearly one year after Hadi agreed to create the Executive Bureau, the office is just now being established and has yet to seriously embark upon its intended mandate. Meanwhile, the government lost valuable time to mitigate the economic situation during a critical period. Although the World Bank and others continue to invest in developing this mechanism, the Bureau is not fully empowered; therefore, it will be constrained in expediting project implementation and reducing opportunities for corruption.

On the positive side, the Ministry of Finance and the Central Bank have done a reasonable job of overseeing some macroeconomic recovery; they have maintained foreign exchange reserves (buttressed by the Saudi deposit), cut interest rates from 20 to 15 percent, and stabilized the

The 2012 Friends of Yemen meeting in New York. Photo credit: UK Foreign and Commonwealth Office.

currency back to its pre-2011 levels.[6] However, a September 2013 Central Bank report indicates that the annual inflation hit a sixteen-month high of 14.5 percent in June, and foreign currency reserves dropped to their lowest level for nearly a year in July.[7] Some indicators improved in November 2013, but there is still a great deal of volatility. Yemen is not in the clear, and its economy cannot afford to coast on autopilot. Even if all the pledged donor funds come through, this will not solve Yemen's economic problem and policymakers will still need to make difficult decisions.

Governing with a Divided Government

For the past two years, all attention within the cabinet, government bureaucracy, parliament, and political parties has been oriented toward the political arena and implementation of the National Dialogue. Throughout 2012 and 2013, the author conducted interviews with analysts, ministers, and representatives from the prime minister's and the president's offices. Although all of the interviewees agreed on the need to focus on economic recovery and employment generation, they acknowledged that the political bandwidth was simply not present. The very structure of the transition government means that ministers and their lead staff were selected not on the basis of their technical competence or experience, but rather due to party positions and relationships with key power brokers. The reality is that the GCC transition agreement set in place a fundamentally divided government—with half of the ministries allocated to the General People's Congress and half to the Joint Meetings Parties (JMP) coalition. The underlying conflict within the government between the former ruling party and the JMP coalition ministers hinders any constructive action toward improving the economic situation.

While the split government allows for political balance and a sense of equity among the major political factions, it has stymied the development of a unified vision for the cabinet to pursue. Hadi is a respected figure, but Prime Minister Mohammed Basindwa has not demonstrated leadership with the cabinet, and the government is viewed as a relatively weak

6 International Monetary Fund, *Republic of Yemen: 2013*, 12.

7 "Yemen Inflation Climbs to 16-month High in June, Reserves Down," Reuters, September 30, 2013.

body whose mandate is limited to implementing what is dictated by the GCC deal. The lack of leadership is felt acutely in the economic sphere.

Yemen is not in the clear, and its economy cannot afford to coast on autopilot. Even if all the pledged donor funds come through, this will not solve Yemen's economic problem and policymakers will still need to make difficult decisions.

The Ministry of Planning and International Cooperation is meant to take the lead on implementing the Mutual Accountability Framework (MAF) that guides the two-year stabilization plan and coordinating with donors, but delays establishing the Executive Bureau have slowed action. Reverting back to what the MAF outlined would be accomplished in the short and medium term paints a dismal picture of how little has been achieved on the economic reforms front. There have been some positive steps worth noting, including the recent adoption in September 2013 of a National Youth Action plan oriented toward job creation and skills development. But for the most part, there is almost no sustained effort to turn plans on paper into action due to lethargic bureaucracy and vested interests.

The Ministry of Finance, the Ministry of Industry and Trade, the Ministry of Planning and International Cooperation, and the General Investment Authority each have an important role to play in coordinating and implementing economic policy. However, due to internal divisions and party rivalries, they are far more concerned with advancing their own loyalists and there is insufficient coordination. In fact, there is a lack of clarity about the specific role and mandate for each ministry, and this leads to conflict between those ministries and other related agencies. As a result, the president has no team of economic advisers to help chart a course for growth and guide economic decisions.

One way around this lack of leadership and coherence is to form an Economic Cabinet, which would include the ministers and deputy ministers from the relevant ministries and agencies listed above, along with five or six outside economists or policy analysts to provide economic guidance and advice. In order to mitigate internal power struggles, the chairperson could be elected from among the external experts and be empowered to set the agenda and call meetings. Forming such an economic council that includes, rather than sidelines the ministers, would provide much-needed, nonpartisan advice to the president on economic policy and could provide some political cover for tough decisions.

Next Steps

The Reform Agenda

The path toward economic reform is not a new topic. There is relative consensus among Yemeni and international experts about the essential components and parameters of a reform agenda: economic diversification, reduction of fuel subsidies, strengthening tax and customs administration and collection, investment in infrastructure and basic service delivery, creating a better operating environment for businesses, and expanding access to financial services. The IMF recently completed its periodic assessment of Yemen's economic profile, and emphasized the danger of its growing budget deficit and the need to reorient the budget toward pro-growth and pro-poor expenditures.[8]

The current discussion in the National Dialogue regarding decentralization and federalism could introduce a new kind of regional economic approach and could impact the arrangement of sharing natural resources and tax revenue in a federal system. However, the basic components of how Yemen's economy must shift will remain unchanged, regardless of the Dialogue's outcome. Presumably, the central government will maintain some key economic planning functions, and Yemen cannot afford to wait until the final parameters of a federal system are determined to start building consensus for these reforms.

8 "The IMF Concluded 2013 Article IV Consultation with the Republic of Yemen," International Monetary Fund press release, July 21, 2013, http://www.imf.org/external/np/sec/pr/2013/pr13291.htm.

First, Yemen should **diversify its economy beyond reliance on hydrocarbon revenue.** This has been noted ad nauseum in the past, but declining production and lower prices mean government coffers have taken a hit, and this makes a shift even more urgent and necessary. Oil production has fallen over the past several years and reserves are expected to be depleted by 2017. Sabotage of oil pipelines hampers the government's plan to increase oil production; in 2012, it was estimated the government lost $1 billion in oil exports due to attacks on pipelines,[9] and the Central Bank reported a $580 million loss in oil revenue from January to August 2013.[10] There is little reason to believe this security threat will evaporate soon. The cyclical pattern of tribesmen attacking pipelines and blocking roads to advance their demands can only be addressed if the government begins to resolve underlying grievances that prompt disgruntled Yemenis to use these tactics as bargaining chips in political negotiation.[11] More importantly, in the long term, available oil and gas resources will not sustain government expenditures. Yemen's economy needs to

9 Mohsin Khan and Svetlana Milbert, "Yemen's Economic Quandary," *MENASource*, Atlantic Council, August 22, 2013, http://www.atlanticcouncil.org/blogs/menasource/yemen-s-economic-quandary.

10 Ali Saeed, "Economists: Government Must Collect Taxes, Better Manage Oil Revenues," *Yemen Times*, November 5, 2013, http://www.yementimes.com/en/1726/business/3092/Economists-government-must-collect-taxes-better-manage-oil-revenues.htm.

11 Charles Schmitz, *Building a Better Yemen*, Carnegie Papers (Washington: Carnegie Endowment for International Peace, April 2012) 3, http://carnegieendowment.org/2012/04/03/building-better-yemen/a67j.

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move into labor-intensive industries to propel sustainable growth and provide sufficient employment opportunities for its population.

Moving away from oil revenue dependence is like breaking a bad habit; it will take time and will be painful, but can no longer be delayed and the government should start aggressively planning for diversification. Growth in other sectors is essential for Yemen's long-term economic prospects, and sustained economic growth will depend upon leveraging and utilizing Yemen's large labor force. In the meantime, increasing the number of Yemenis working in the GCC countries is the quickest and most obvious path to mitigate unemployment and increase remittances. Some may recall the 10-Point Plan initiated by the Yemeni government in 2010 that detailed a plan to move thousands of Yemeni workers to Gulf countries, and as part of the Friends of Yemen process GCC countries committed to accepting Yemeni workers. Since then, security and political issues have stymied these efforts. A comprehensive approach is needed to overcome such obstacles and would benefit both Yemen and its neighbors.

Beyond this stop-gap approach, the government's economic planning should prioritize where opportunities exist for growth and then make the requisite capital and infrastructure investments. Yemen needs to identify and exploit where its comparative advantage lies: the provision of services in areas that need further development, namely construction, retail, tourism, and financial services. The proportion of agriculture in the productive economy has been declining over the years, yet some of this could be reversed or restimulated through crop substitution (away from the frequently used mild stimulant, qat), greater water-use efficiency, and the utilization of new technologies that will increase yield. The fisheries industry, the mineral sector, and port development present opportunities for growth, and Yemen has tremendous potential to develop and expand the tourism sector when the security situation comes under control. The government should engage with international partners and the local private sector to stimulate investment in these sectors; without deliberate guidance and incentives, diversification of the economy is unlikely to happen on its own. In addition, the infrastructure projects planned and funded by international donors should be designed to maximize use of Yemeni labor and begin shifting the economy into more productive sectors.

Second, the **government should reduce fuel subsidies**. This will be an extremely difficult and unpopular move—many vested interests benefit from cheap fuel that is smuggled and resold at higher prices, or used in industries that do not need subsidized prices—yet it is absolutely essential. Subsidies consume more than 30 percent of the government budget, foster corruption, and do little to serve the needs of the most vulnerable.[12] The IMF has been talking with the current and past governments about a medium-term program, and the major stumbling block to date has been the lack of commitment to addressing the problem of subsidies. Recent reports indicate that an IMF deal may come to fruition by the end of 2013, which would likely hold the government accountable for implementing a multi-phase, gradual process of reducing the costly subsidies.

Any subsidy reform program should be accompanied by a cash transfer program to help those truly in need, and many other

12 Ibid, 4.

countries in the region and elsewhere in the developing world are testing out systems and generating best practices. Yemen faces a particular dilemma since the government currently lacks an effective way to target the poor to deliver this compensation. In order to lay the groundwork for subsidy reform, the government will need to develop this mechanism—perhaps through the Social Fund for Development or other government agency—in order to ensure that the poor are not the ones hit hardest from subsidy removal. The process of creating a new voter registry, which will collect information that could subsequently be used to launch a national identification card, could be a critical element in this process. At the same time, the fiscal impact of a cash transfer program should also be taken into consideration.

What subsidy reform really requires—and what Yemen is most lacking—is the political will and leadership to make the case to the public and generate popular support for a measure that would reduce opportunities for corruption and give more targeted assistance to those in financial need. Yemen's government, with the support of international partners, should start a nationwide public outreach and communications strategy to explain why subsidy reform is necessary, how poor families will be compensated, and the timeline for such changes.

Third, **Yemen's government should get its fiscal house in order** and prioritize expenditures appropriately. With oil revenue declining and subsidies and wage payments increasing, the fiscal deficit is increasing at alarming rates. Subsidy reform is part of that equation, but more effective and efficient tax and customs administration and collection is the other part. Tax evasion is a major issue, and most businessmen either underreport profits and underpay taxes, cut deals to pay a reduced rate to tax collectors off-line, or circumvent the process altogether. At the same time, given corruption within the tax authority, it comes as no surprise that reasonable businesspeople would be incentivized to evade taxes. The tax problem is clearly two-sided and both the public and private sector need to be engaged. Due to corruption and mismanagement, the country loses about $4.7 billion in unpaid taxes[13] and at present there are only 3,080 registered taxpayers, an extremely low number for a population of 25 million.[14] In order to improve tax collection and modify the General Sales Tax, the government should actively engage and partner with the private sector to get their buy-in to any changes.

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The current budget passed by the Yemeni parliament in January 2013 was the largest in the country's history, with a notable 50 percent of total government spending for energy subsidies and wages, while expenditures on social services and cash transfers to the poor were cut.[15] When the budget was submitted with an unapologetic gap between predicted revenue and expenditure, the government indicated that international donors would make up the difference in the immediate term. International assistance may fill some of this gap, but the remainder is financed by the local banking sector, which results in fewer resources available for private investment in the local business community.[16] There seems to be little concern about this worrisome trend

13 Saeed, "Economists: Government Must Collect Taxes, Better Manage Oil Revenues."

14 International Monetary Fund, *Republic of Yemen: 2013*, 34.

15 Khan and Milbert, "Yemen's Economic Quandary."

16 Khaled Sakr, "Yemen: Reorienting Public Spending Would Create Jobs, Fight Poverty," interview, *IMF Survey*, http://www.imf.org/external/pubs/ft/survey/so/2013/car073013a.htm.

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in the government, yet this is an unsustainable attitude.

Just as concerning, the budget was developed without significant input or debate about whether it reflects the country's priorities and how it will be financed. There was little if any debate in parliament, no visible public discussion, and minimal media coverage on policy decisions inherent in the budget. The economy is off the political agenda, meaning political parties and civil society groups are not arguing economic policy even though these decisions have the most impact on their constituencies.

Fourth, the fiscal restructuring necessary for Yemen's economy would have a significant impact on the ability to **make investments in infrastructure, such as roads, reliable electricity provision, and access to water and basic services.** Reorienting the state's budget to infrastructure projects and labor-intensive initiatives would not necessarily reduce the deficit, but would go a long way toward empowering Yemenis to achieve economic agency. In addition to reducing subsidies and increasing tax and customs revenue, the Yemeni government needs to address the growing wage bill by eliminating ghost workers and instituting a more efficient and effective civil services system. As of now, the wage bill exceeds 11 percent of GDP, a rate that is high even relative to other countries in the region with bloated public bureaucracies.[17] Even if undertaking a massive reduction in the number of civil service employees is not feasible, since government jobs are seen as a critical means of building political loyalty, cleaning up the rosters and removing ghost workers would be a critical start.

The last major component of Yemen's reform agenda should include **expansion of the financial sector and improvement of the business climate.** Currently, the financial

17 International Monetary Fund, *Republic of Yemen: 2013*, 6.

system is bank-dominated, but banks are reluctant to lend to the private sector because it is too risky; there is no effective insolvency system or judicial infrastructure to ensure property and creditor rights. While bank supervision and regulation should be enhanced, the loan process should be simplified and made far more accessible to potential borrowers outside the elite cohort that currently accesses the banking system. At the same time, increasing the options and availability of financing by expanding the banking sector would help address the gap that large banks may be unwilling to fill and to reduce the cost of financing for small businesses and individuals. Restrictive business regulations and lack of access to finance impede the development of small and medium-sized businesses, which will be the engine of growth and employment in a country like Yemen.

Part of what has led to Yemen's low level of productive growth is the weak capacity of state institutions. Guaranteeing property rights, contract enforcement, effective tax collection, and fair judicial procedures are all essential to creating an environment that facilitates and allows growth and investment. The ability to implement these measures and to enshrine the norm of transparency rests largely in the hands of political leaders who can galvanize the state-building endeavor. This will be a lengthy process and may happen only with generational change. In the meantime, the Yemeni private sector and local nongovernmental institutions and development organizations will have to continue to navigate this reality. Furthermore, it is unlikely that foreign investors will come in large numbers given the precarious security environment. In the near future, therefore, Yemen's economic development will largely rely on the local business community and investors.

In the short and medium term, there is simply no easy answer to the unemployment crisis and neither the local private sector nor the government alone will have the means to create enough jobs to meet demand in the next three to five years. While these reforms are being implemented, Yemen will need to rely on its neighbors to help address the huge gap between available job opportunities and job seekers. Saudi Arabia and other GCC countries committed to accept two million Yemeni laborers as part of the Friends of Yemen process, yet Saudi Arabia's recent move to tighten its labor market and deport two hundred thousand Yemeni workers as of November 2013 only exacerbates Yemen's already bad economic situation and may contribute to further regional instability. Saudi Arabia and other Gulf countries cannot afford to ignore Yemen's economic situation, and should make good on their promises, not to mention that they need laborers who are willing to do the jobs that their own nationals are unwilling to do. One approach is for GCC countries to tie their acceptance of Yemeni workers to institutional reforms related to improving security and the investment climate in Yemen. In particular, the international community could support an arrangement that makes the flow of Yemeni workers to GCC countries contingent on the Yemeni government's ability to make concrete improvements in legal framework. Specifically, the development of a national ID system in Yemen would enable greater transparency and would give greater assurance and confidence to Gulf governments and employers regarding the background and legal status of their employees.

Engaging the Private Sector

Moving beyond the divisive politics, exclusion, and inequality that led to the 2011 uprising will necessitate a new approach to economic development that addresses state weaknesses, actively engages a broader segment of the business community in identifying areas of potential growth to create new jobs, and develops a more productive labor force. Moving forward, establishing mechanisms to gain that kind of input and improving the institutional and legal environment will be essential to leverage the dynamism of the private sector and the energy of a youthful work force.

The political transition underway has not changed the basic reality that engaging in business activity in Yemen requires operating within a system based on corruption and nepotism. Some benefit directly from this, but others are frustrated by wasted time, resources, and cuts in their profits margin because of the inevitable bribes that have to be paid. There are businesspeople who recognize the real costs of operating within the status quo and are fed up with the uneven playing field; they have an incentive to break with the past and forge a political and economic environment based on greater transparency and fair competition. This is the segment of the private sector that needs to be identified, empowered, and incorporated into a vibrant public-private partnership with government and civil society organizations.

As in any other country, the private sector in Yemen is not a monolith and includes a complex web of elite families that have wielded economic privilege and power for generations, newcomers that have emerged in the last three decades, a strong merchant class from the coastal cities, and thousands of small- and medium-sized enterprises, both formal and informal. While most economic activity now takes place in and around Sana'a, for generations Taiz was the center of commercial activity and the coastal cities also have strong trade ties and economic legacies. While there is diversity within the private sector, it is important to note an important political economy analysis by Chatham House that details the control of around ten key families and business groups with close ties to the former president of more than 80 percent of imports, manufacturing, processing, banking, telecommunications, and the transport of goods.[18]

The government needs not only to pay lip service to dialogue with the private sector, but actually empower the business community, provide the necessary infrastructure, and implement legal and regulatory reform that would open up opportunities for more competitive and fair business growth. Of course none of this can be done without ensuring a minimum level of security, which is essential for any kind of economic development or investment, whether foreign or domestic. Moving forward, the government should sustain an open dialogue not just with the stalwarts in the Chambers of Commerce that benefit from the status quo, but with a broader cohort that brings in various segments of the private sector, including small and medium-sized businesses, which represent the overwhelming majority of businesses in Yemen.

There are now clear access points for the government to engage with the business community, but to date the Yemeni government has not had the bandwidth to focus on the economy. The government recently established a special Public Private Partnership unit, yet this has not been fully utilized or activated. Hadi has been consumed with other priorities such as the National Dialogue, military restructuring, and al-Qaeda in the Arabian Peninsula. Prime Minister Basindwa, for his part, has not put forward any economic policies. The TPSD is a good start, but it is not a substitute for real attention from Hadi and the relevant ministers in formulating and implementing an economic agenda for the country. Most political leaders are not focused on the dire economic conditions, or even on the humanitarian crisis which threatens starvation for thousands daily; rather, they are more concerned with pleasing specific interest groups and positioning for upcoming parliamentary elections. After two years, the government is still in a state of crisis management and zero-sum political maneuvering, but this will not be sufficient to lift Yemen from the calamitous fate of a nation perpetually on the brink of collapse. The international community has an important role to play by placing these issues on the front burner and incentivizing Hadi and the current government to prioritize economic reforms.

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18 Ginny Hill, Peter Salisbury, Léonie Northedge, and Jane Kinninmont, *Yemen: Corruption, Capital Flight and Global Drivers of Conflict*, Chatham House, 5.

Conclusion and Recommendations

Assessing the best use of international donor funds and creating mechanisms to implement projects in an effective, cost-efficient way will require tackling the most sensitive political issues. The previous regime and elite insiders benefited from significant distortions in the economy by taking advantage of subsidized fuel and perpetuating inefficiencies in the electricity sector. A small number of families, including that of the former president, have a vested interest in maintaining the status quo and this behavior is hindering the country's economic development. For the Yemeni government to effectively rebuild the economy and restructure the country, these two issues will need to be confronted. In this case, good intentions will not be sufficient, rather strong political will is needed. This pressure can come from both domestic and external actors, including through aid conditionality on the part of the international community.

- **Yemen's government should shift its focus to economic planning, fiscal reform, and implementation of labor-intensive projects** in order to improve economic conditions and address unemployment, particularly among youth. The government can no longer afford to view its economic mandate only as stabilization; real leadership is urgently needed to promote growth and improve living conditions across the country. Delivering results in the South will be particularly important in order to generate some confidence and reduce the likelihood of an outright rejection of the Dialogue's outcomes.

- **Introduce a new government upon the conclusion of the National Dialogue rather than waiting for the next elections and focus its mandate on three areas: improving security conditions, economic performance, and basic service delivery.** Ideally, new ministers would be technocrats appointed based on merit, but if this is unfeasible due to resistance from the political parties, then deputy ministers should be selected based on their technical qualifications and empowered to play a leadership role.

- **Hadi should form an Economic Cabinet and forge consensus on a long-term economic plan** based on the outcomes of the National Dialogue and in consultation with the Yemeni business community. This should be tackled with urgency, even while constitution-drafting and election preparations are underway.

- Yemen's government should activate and empower **a permanent Public Private Partnership body that brings together the private sector and the relevant government bodies** (ministries of finance, international planning and cooperation, and industry and trade). Instead of the ad hoc efforts of the past—or competing initiatives from various ministries reaching out to individual business leaders—this would represent an ongoing, all-of-government effort to engage with diverse segments of the business community to gain their input and buy-in for economic initiatives and reform efforts.

- **The government needs to demonstrate leadership and establish credibility by prioritizing action that will deliver results for the Yemeni population.** The ability of the government to effectively leverage tax revenue depends upon a social contract with the private sector; if there is no basic agreement on the legitimacy of the government, business people will continue to avoid paying taxes. Only when the private sector and private citizens believe the government is working to advance their interests will it be able to implement a more robust tax regime.

- **International partners should press the Yemeni government to deliver reports on concrete progress according to the benchmarks and action items set forth in the TPSD and Mutual Accountability Framework** (developed between the government and the World Bank), specifically regarding economic initiatives and economic reform commitments. Most of the discussion in the Friends of Yemen meetings has focused on the National Dialogue and security issues, with very little attention to the economy.

- **The international community should support Yemen in formulating an IMF program by providing financial and political support for the government to undertake difficult economic reforms**, including but not limited to a gradual, phased reduction of subsidies that would increase direct spending on the country's most vulnerable population. An IMF framework should link international financial assistance to progress on reforms that the Yemeni government itself has determined are priorities. The international community should help the Yemeni government formulate and implement a robust communications strategy that explains how such reforms will directly benefit the Yemeni people and develops buy-in for a Yemeni-led reform agenda.

- **Yemen's partners and international financial institutions should forge a common understanding with the GCC countries that Yemen's economic success is essential for regional stability**, encourage them to quickly deliver pledged funds, provide political support to empower the Executive Bureau, and integrate forthcoming financial contributions within the broader framework of economic reform and diversification plans.

- **The international community should develop a framework that makes the flow of Yemeni workers to the Gulf countries contingent on institutional and legal reforms.** Under the auspices of Friends of Yemen, the G10 countries[19] should put forth a comprehensive plan between the GCC and Yemen, which creates an incentive-based system to encourage reform in exchange for access to Saudi and other Gulf countries' labor markets. In the short term, there is no way that Yemen can absorb the massive number of unemployed, particularly among the youth, and Saudi Arabia in particular has incentive to address a situation in Yemen that has worrisome security implications at home. While Yemen's economy regains some momentum, its neighbors have a great deal to gain with this kind of approach.

- Moving forward, **international actors should utilize political economy analysis in order to understand how economic, humanitarian, and military assistance impacts the local economy and benefits certain elite circles.** International donors should consider how funding decisions and assistance strategies can either enhance or impede good governance and accountability.

19 The G10 is a diplomatic grouping consisting of the five permanent members of the UN Security Council, the GCC, and the EU.

About the Author

Danya Greenfield is the acting director of the Atlantic Council's Rafik Hariri Center for the Middle East. She leads the Yemen Policy Initiative and writes extensively on Yemen, Jordan, and Egypt, as well as US assistance to the Arab world.

She is a democracy and governance specialist with extensive experience in the Middle East and North Africa. Prior to joining the Atlantic Council, she worked at the Center for International Private Enterprise (CIPE) as a program officer, implementing a three-year corporate governance project in the region, and subsequently managing a portfolio of projects in Yemen. Before CIPE, Greenfield worked as a program officer at the International Republican Institute (IRI) from 2003 to 2007 and helped launch several field offices and managed a variety of programs related to elections, political party strengthening, and civil society development in Egypt, Lebanon, Tunisia, Qatar, Jordan, and West Bank/Gaza. Prior to IRI, she participated in a year-long fellowship to study Arabic at the American University of Cairo and worked with the Egyptian Center for Women's Rights.

From 1997 to 2000, Greenfield worked within the NGO and interfaith community in Washington on international policy issues and advocated to increase US international engagement, support foreign aid, and fulfill US financial commitments to the United Nations.

Greenfield holds a master's degree in international relations and Middle East studies from Johns Hopkins School of Advanced International Studies and a bachelor's degree in international relations from Tufts University. She has advanced skills in Modern Standard Arabic and the Egyptian dialect.

About the Rafik Hariri Center for the Middle East

The Atlantic Council's Rafik Hariri Center for the Middle East brings North American and European voices together with experts from the Middle East, fostering a policy-relevant dialogue about the future of the region at a historic moment of political transformation. The Hariri Center provides objective analysis and innovative policy recommendations regarding political, economic, and social change in the Arab countries, and creates communities of influence around critical issues.

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