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Achim Wennmann¹ and Fiona Davies²

About this report

This report provides an update to a previous [2020 publication](#) on the economic dimensions of the conflict in Yemen, commissioned by the European Union (EU), UNDP and UNOCHA. The update was commissioned by the EU. It represents a preliminary stocktaking after 7 interviews with interlocutors representing different constituencies within Yemen and the international community, as well as the review of relevant documents. Interviews were conducted in the period 20 September to 12 October 2021.

The report is structured into four sections. The first section recaps the main findings and recommendations from the 2020 report. The second section reflects on overall observations from interlocutors on the continuities and changes in the economic dimensions of conflict over the past fifteen months since interviews were conducted in 2020. The third section provides an updated view on opportunities for engagement on economic dimensions of the conflict in view of strengthening economic development and resilience in Yemen. The final section offers recommendations to the international community on approaches to strengthening economic de-escalation in Yemen.

1. Recap of 2020 report findings and recommendations

The 2020 report synthesised responses from 20 interviews. The findings highlighted that:

- The economy is a critical aspect of the conflict in Yemen. Incompatibilities over control of resources represent a major reason for the armed conflict, including grievances associated with wealth sharing and marginalisation, and have also accentuated political conflict over the control of institutions. Various conflict actors instrumentalise the economy to consolidate their own political position, while control over revenue generating assets and institutions managing the economy has been a driver of conflict dynamics.
- The private sector operates within the realities of a divided Yemen. In spite of the de-facto existence of two currencies and banking systems, many economic transactions nonetheless take

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place across Yemen's internal divisions and international borders, albeit at significantly increased costs.

- A small number of powerful individuals have deeply entrenched economic interests in the status quo. These actors have positioned themselves to benefit from the economic blockade of Northern Yemen, the fracturing of central banking, the creation of two currencies, and the new patterns of territorial control. However, there are constituencies within the trading and banking community that still believe in the value of a neutral economy that can help bring the country together.
- The characteristics of the economies controlled by different conflict actors vary considerably, and their economic interests in the peace process are influenced accordingly.

Four interventions were identified as having the greatest immediate impact in stimulating private sector activity, neutralising the war economy and relieving the humanitarian situation. These four interventions were:

- Opening up the port of Hudaydah and Sana'a airport, to solve the brunt of the supply problem of key goods, especially in Northern Yemen, while also helping lower prices and dismantling a key element of the war economy.
- Re-establishing a neutral and unified Central Bank of Yemen and a single currency, to provide a more stable macroeconomic situation to enable imports and exports, reduce the cost of doing business across the country, stabilize consumer prices and help rehabilitate the financial sector.
- Opening roads and enabling unimpeded mobility internally, to facilitate trade, lower cost of consumer goods and increase the security of traders and their products.
- Predictable payment of salaries for public servants, to stabilize household incomes and boost local demand – although to meet this objective, it was noted as essential that salaries are not funded through money creation.

The report concluded by noting that without sufficient agreement on the shape of the future political system, Yemen might face continued fracture into disparate economic zones whose gate-keepers negotiate the terms of access to their respective economy space – creating de-facto governance entities – while the formal trappings of statehood are subject to contestation. The result might be a Yemen trapped in a 'no war, no peace' scenario that serves the interests of a limited set of stakeholders within and outside Yemen, and that perpetuates an international humanitarian presence for the years to come.

2. Update on the economic dimensions of the conflict in Yemen

The 2021 interviews confirmed that the economy remains a key dimension of the conflict in Yemen. Political actors maintain a war mentality and are engaged in active combat that includes territorial, political and economic dimensions. Zero-sum mentalities remain strong in the public communications of the conflict parties. The role of powerful gatekeepers with monopolistic control over specific economic sectors has largely been consolidated.

The fuel market has emerged as a new front line in the war economy over the past year. Several interlocutors suggested that the efforts of the Kingdom of Saudi Arabia (KSA) and of the Internationally Recognized Government (IRG) of Yemen to inflict revenue losses on Ansar Allah by blocking the entry of fuel shipments into Hodeidah port have backfired. Ansar Allah has found alternative ways of extracting revenue from fuel trucked overland from the South, reportedly exerting greater control over the entire supply chain in the process. The brunt of the fuel blockade has been born by ordinary people living in Northern areas, through increased fuel prices and higher cost of living.

The status quo of a fractured and distorted economy has become increasingly normalised over the past year, and ambition on near-term measures to unblock the economy appears to have reduced

commensurately. Private sector actors have adapted to the realities of operating in an economically divided Yemen, while acknowledging the significant additional costs involved. International community efforts on the economy are increasingly focused on reducing the cost of the status quo and facilitating private sector actors to operate more efficiently within it, through measures such as a bond on war insurance and consolidated inspection mechanisms. These efforts illustrate the type of pragmatic engagements, motivated by the objective of reducing the cost of living for the ordinary person, that are possible in the current constellations - but in the absence of accompanying efforts to resolve the economic fractures and eliminate current barriers that are part of the economic dimensions of Yemen's war, they could also inadvertently serve to perpetuate the current status quo.

Perceptions of the capacities of different conflict actors have evolved over the past year, and it is widely acknowledged that there is considerable asymmetry in the way the state functions in different parts of Yemen. Ansar Allah is considered to have demonstrated a capacity to learn by doing, and to innovate despite their international isolation. It has demonstrated that it is open to seeking advice from trusted third parties as it develops policy in order to progressively expand and improve its governance roles and performance. It has also shown an ability to adopt strategies that protect its own economic interests. Examples include taxing rather than dismantling the gatekeepers that control trade flows into the North, ongoing measures to prevent the importation of inflation into its territories by banning use of newly-printed IRG banknotes, initiatives to promote domestic production and non-interference with the activities of institutions such as the Social Fund for Development.

Several interlocutors also raised questions over the capacity of the IRG as a governing entity given its limited control of territory and people, even in areas nominally under its control. The IRG's continued leverage derives from its control of the international entry points into Yemen and its status as the internationally recognized partner for the international community. In the face of limited de facto territorial and administrative control, the IRG has increased effort to bolster its position around its international recognition. Its influence over areas controlled by the Southern Transition Council (STC) is also said to be becoming increasingly limited.

3. Opportunities for engagement on economic issues

Opportunities for engagement on economic issues have shifted over the past year, in line with the increasing 'normalisation' of the status quo of a fractured and distorted economy. Certain economic dossiers reportedly have potential for near-term progress. These include resolving the standoff over fuel imports into Hodeidah port and using accompanying revenues for payment of salaries, consolidating inspection mechanisms, and putting up a war insurance bond to reduce the cost of war insurance premiums. However, these dossiers are largely focused on opportunities within the context of the status quo, rather than achieving a major shift in the position of conflict actors on economic issues.

The potential for addressing larger economic dossiers appears increasingly out of reach at present. For instance, removing the blockade of Hodeidah port and Sanaa airport entirely seems difficult in the absence of conflict resolution, and efforts are instead focused on easing restrictions. Interlocutors also concur that efforts to reintegrate the Central Banks are no longer really being discussed, rather efforts focus on adapting to new realities. Progress on dismantling the greatest economic barriers and distortions is apparently unattainable without a significant shift in the political positions of Ansar Allah, the IRG, or other key parties to the conflict; however, prospects for such a shift do not seem high given the current tendency of adaptation to the economic status quo, coupled with a battle for territorial control in key resource-rich areas such as Marib and the interests associated to regional players to keep Yemen weak and divided, as noted in the 2020 interview report. Significant pressure from international actors would be needed to resolve the current conflict dynamics.

There are widely divergent views on Ansar Allah's interests and incentives. Some interlocutors suggested that war is more beneficial to Ansar Allah than peace, and they are not interested in development. However, others pointed to policies they have put in place to promote local enterprise and production (e.g. zero tax on micro-enterprises and solar panels, limiting import licenses to 80% of the normal quota so that importers have an incentive to promote local production). Likewise, while some interlocutors suggested that Ansar Allah has no incentive to compromise, because it has found a way of operating successfully within the current economic constraints, others suggested that they want to be considered legitimate internationally and to attract external expertise and investment.

The wide range in views on Ansar Allah's interests generated a diverse range of suggestions on possible leverage points for economic engagement with them. These included:

- Removal of all restrictions on Red Sea ports (although one interviewee suggested even this was no longer a major priority, because the Ansar Allah have found ways of managing the status quo);
- Gaining external legitimacy and external investment (although one interviewee suggested this wasn't possible/advisable until there is some kind of peace agreement);
- Access to learning/expert advice (but it would need to be from a party that Ansar Allah considers neutral); and
- Dismantling the role/reach of the IRG in the Northern economy.

The diversity of opinion on Ansar Allah's interests and incentives indicates the importance of establishing a more direct understanding of their economic priorities and objectives prior to proposing concrete measures on economic de-escalation.

For the IRG, the assumption is that its incentives continue to revolve around maintaining its status as the internationally-recognised government for Yemen, and deriving benefit from the advantages bestowed by internationally-recognized sovereignty. For the STC, proving itself as a more credible economic actor than the IRG is considered an important motivation.

Events over the past year have indicated that private sector actors can play a role in acting as a mediator between the parties and unlocking current barriers on economic issues - but to the extent that these actors are also the gatekeepers, this approach also carries the risk of further entrenching their existing power.

4. Recommendations for the international community

The recommendations for strengthening economic de-escalation occur within the current status quo of a fractured and distorted economy that is becoming increasingly normalised. Within this context, the international community should consider a two-pronged approach that, on the one hand, seizes incremental and localized opportunities within the status quo realities, and on the other hand, opens spaces for high-level diplomacy to affect the way economic dimensions will be addressed within a bigger political settlement. Economic de-escalation requires both approaches to be advanced together in order to prevent counterproductive outcomes such as a further entrenchment of the status quo, and the acceptance of a closed-access, monopoly-based economy as a trade-off for a political deal.

With respect to the first dimension, the interviews reveal that several international actors have found space for localised economic engagement at various levels in Yemen, such as the ports of Hodeidah and Aden, road rehabilitation projects, or economic peacebuilding at regional levels. Some international actors have also started to be cognizant of the importance of balancing their efforts between the two parties of the UN-led peace process, and other relevant stakeholders to prevent the perception of bias and create incentives for future collaboration; despite tending to be institutionally constrained to work with recognized political entities, and at technical levels. These efforts should be built on, focusing on issues that are economically important and relatively bi-partisan.

With respect to the second dimension, most interlocutors appear to share an assessment that there is currently no appropriate dialogue space to address the politics of economic de-escalation. International economic actors have confirmed their focus is at the technical level, deferring responsibility for the political level to UN Members States, the UN Resident Coordinator (UNRC), and the UN Special Envoy (UNSE). Interviewees suggested an emerging arrangement between the UNRC and UNSE whereby the UNRC focuses on the economic dimension from the perspective of food security (or humanitarian perspective). However, the question remains as to whether a wider coalition of actors (international, regional and domestic players or private sector actors) could support this dialogue space and endow it with the necessary leverage for brokering agreements on unlocking the economy of Yemen, in support of UN efforts.

In addition, there are likely to be limitations to the effectiveness of this dialogue space in the absence of a fuller understanding of two significant issues: the economic objectives and priorities of Ansar Allah, and the increasing asymmetry in the way the economy functions in different areas of Yemen. These priorities and asymmetries need to be better recognised and understood in order to shape the dialogue and proposals on economic de-escalation accordingly. Understanding the economic objectives and priorities of Ansar Allah requires a more direct engagement with policy-makers working with the De Facto Authorities.

Finally, several interlocutors confirmed that the Yemen conflict features in several political discussion including not only the UN-led process, but also conversations between the KSA and Iran facilitated by Iraq, discussions facilitated by Oman, and discussions initiated by the US Special Envoy. However, an assessment of these efforts in view of their contribution to economic de-escalation was not possible on the basis of the current set of interviews. A better understanding of the implications of these different discussions for the economic dimension of the conflict in Yemen might provide an outlook on the pathways for a transition from humanitarian assistance to economic development, or on the resilience of entrenched stakeholders with a partisan interest in a fractured and distorted economy.