

# RESTORING CENTRAL BANK CAPACITY AND STABILIZING THE RIAL

## BACKGROUND

The primary reason Yemen is experiencing the world's largest food security emergency is that millions of people cannot afford to buy the food available in the local market. The ongoing conflict has spurred myriad factors contributing to this crisis, such as general economic collapse and widespread loss of livelihood, restricted naval and air access to the country and internal transportation challenges that are inflating costs for importers. Imports and international trade have also been stifled financially: Yemeni commercial banks have been facing difficulties in transferring foreign currency banknotes abroad due to the air restrictions on Sana'a airport, while American and most European banks have closed the accounts Yemeni commercial banks held abroad due to compliance concerns regarding obligations to international money laundering and counter-terrorism financing standards.

In addition to these factors, the depreciation of the rial has severely impacted purchasing power in Yemen. Prior to the current conflict, the exchange rate was at YR 215 to US\$1. By mid January 2018, the rial was trading at YR 530 to US\$1 (before the \$2 billion Saudi deposit was announced). For in-depth analysis on the the depreciation of the YR and the major contributing factors, see the Sana'a Center for Strategic Studies' (SCSS) October economic bulletin: [Renewed rapid currency depreciation and diverging monetary policy between Sana'a and Aden](#).

## INTRODUCTION

As part of the "Rethinking Yemen's Economy" initiative, more than 20 of the leading socio-economic experts on Yemen converged for the second Development Champions Forum on January 14-16 in Amman, Jordan. Among the urgent topics of discussion was the deterioration of the value of the Yemeni rial (YR), the magnifying impact this is having on the humanitarian crisis, and the need to re-empower the Central Bank of Yemen (CBY) as the steward of the rial and the economy generally. This policy brief is an outcome of those discussions, and the recommendations it includes collectively underline the need for the CBY to function in a more coherent, assertive manner – whereby its various branches operate as a united entity that is able to draft and implement monetary policies for Yemen as a whole. This paper includes further input from the Development Champions following the announcement by Saudi Arabia on January 17 of a \$2 billion deposit to the CBY.

This policy brief was prepared by the Sana'a Center for Strategic Studies, in coordination with the project partners DeepRoot Consulting and CARPO – Center for Applied Research in Partnership with the Orient.

## Recommendations to the Central Bank of Yemen (CBY)

- Carry out the CBY's full legal mandate, in accordance with Law 14 of 2000 and the amendments of 2003. This includes managing any and all Government of Yemen foreign currency accounts.
- Regulate domestic currency printing and monitor distribution so as to ensure the optimal balance between easing the cash liquidity crisis and creating further downward pressure on the rial's value. The guiding metric in this equation should be per capita purchasing power relative to basic commodities, which the CBY should seek to maximize.
- Establish specific coordination mechanisms with Yemeni banks, money exchangers and large private sector actors regarding currency stabilization. The primary immediate need for such coordination relates to the CBY's deployment of the \$2 billion deposit announced by Saudi Arabia; coordination between the CBY, banks, money exchangers and private sector actors should seek to magnify the stabilizing impact of these foreign currency reserves and their ability to facilitate basic commodity imports, while simultaneously minimizing the rate at which the CBY expends these reserves.
- Enact monetary policies, legal procedures and coordination mechanisms with Yemeni banks and large private sector actors to curb the ability of currency exchanges and speculators in carrying out coordinated currency market manipulation. Identified violators of the set policies and procedures should face legal action, including the possible imposition of sanctions.
- Begin providing commercial banks with the interest due on treasury bills in order to boost market liquidity and to encourage banks to pay interest on their customer deposits. Given the large proportion of Yemeni bank assets held in treasury bills, interest paid on these would inject significant liquidity into the banking sector, in turn empowering banks to regain customer trust.
- CBY leadership must relocate permanently to Yemen. Current circumstances in Yemen represent a challenging operating environment; however, CBY leadership operating from abroad – as is currently the case with senior management largely based in Amman and Riyadh – is insufficient for effective central bank management. A properly functioning central bank is not possible without the physical presence of CBY leadership on location in Aden.
- Draft and circulate monthly, quarterly and annual reports amongst domestic, regional and international stakeholders that include the balance sheets of banks operating in Yemen and data that maps the level of liquidity in the local market in order to enhance transparency.
- Re-activate the Financial Information Unit of the CBY:
  - Although the new FIU will be located in Aden, it should seek ways to carry out its responsibilities throughout the country, including Sana'a, to maximize effectiveness.
  - The FIU should resume its regular meetings and coordination with the Middle East & North Africa Financial Action Task Force (MENAFATF), among other organizations, to ensure that Yemeni bank processes and practices are in compliance with international standards.
  - Yemeni banks were largely forced to close their accounts abroad because of the compliance risk these posed for foreign banks. Reactivating the FIU would be a positive step toward reducing that compliance risk and allowing Yemeni banks to reopen accounts abroad.

## Recommendations to the Government of Yemen (GoY)

- Refrain from holding foreign currency accounts outside of the CBY, as per Yemeni law. (Currently the GoY holds an account at Ahli Bank in Saudi Arabia, where revenues from oil exports have been deposited until recently).
- Improve government revenue collection mechanisms – such as those related to taxes, customs duties, and oil and gas revenues – and ensure that these funds are deposited in government-held accounts at the CBY. Effective anti-corruption measures should also be considered among the primary means to improve government revenue collection.
- Draft and circulate private monthly, quarterly and annual economic reports amongst domestic, regional and international stakeholders to enhance transparency. In particular, this should include data concerning government revenues and expenditure. The national budget should also be shared with the Yemeni Parliament when it reconvenes.
- Refrain from covering governmental expenditures through inflationary means, such as printing domestic currency in the absence of economic expansion.
- Cancel previous instructions that insisted on the collection of state revenues in cash, which pulled cash from local banks and reduced liquidity. Instead, enforce the use of cheques in the collection of state revenues. The use of cash in state revenue collection also leads to heightened levels of government corruption and increases the risks of doing business, given the highly insecure environment.
- Re-activate the National Committee to Combat Money Laundering and Terrorism Financing. The operations of this committee have been suspended since the onset of the conflict. Reactivating this committee would be a positive step toward reducing Yemen's compliance risk.
- Form an advisory team to assist the government with fiscal and economic policies, in coordination with the CBY.
  - The advisory team should consist of representatives from state institutions, prominent economists and representatives from all major sectors of the economy.
  - This team can also act as an advisory council on Yemeni socioeconomic affairs for the GoY, and regional and international stakeholders.
- Given the significance of natural resource revenues for Yemen's GDP and government expenditure, the GoY must look to increase oil and gas production and exports in view of reaching pre-conflict levels.
- Engage actively with the Saudi government to explore options for waiving or at least reducing taxes/fees that the Yemeni diaspora are obligated to pay in Saudi Arabia, thus enabling the Yemeni diaspora to send additional remittances to Yemen.

## Recommendations to the Saudi-led coalition member states and the international community:

- Mobilise additional foreign currency deposits from GCC countries to support the CBY in stabilizing the YR, facilitating imports of basic commodities and facilitating the resumption of basic public service delivery.
- Assist Yemeni banks in providing trade finance facilities to Yemeni importers purchasing basic commodities abroad.
  - Allow the resumption of flights to transfer Yemeni commercial banks' foreign currency banknotes to their accounts in Manama, Bahrain.
  - Accelerate the establishment of the Trade Finance Facility for Food Imports that the World Bank Group announced in April 2017.
- Provide technical support and capacity-building assistance to the CBY to allow it to fulfil its mandate as a central bank.
  - This capacity building and technical support should include training, consultancy teams and/or advisers to help improve internal processes and systems. For example, the installation and use of modern IT systems would help the CBY manage the national budget, international transactions and other central bank duties.
- The coalition members that control access to Yemen's Red Sea ports should not grant oil importation clearances unless the importer submits all the appropriate documentation regarding the mechanism of payment for the shipment (for example, documentary credit, commercial transfer, etc).
  - This will serve two purposes: it will help rein in the leverage money exchangers exert over the currency market and help deter illicit oil shipments.
- The international community should increase pressure on the Houthi authorities in Sana'a to stop political interference in the work of the banking sector.
  - For example, the Houthi leadership in Sana'a recently ordered more than 1,200 accounts of both individuals and institutions frozen. Such moves create distrust in the banking sector and encourage the exit of cash from the banking system.

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\*Note: This document has been produced with the financial assistance of the European Union and the Embassy of the Kingdom of the Netherlands to Yemen. The recommendations expressed within this document are the personal opinions of the Development Champions Forum participants only, and do not represent the views of the Sanaa Center for Strategic Studies, DeepRoot Consulting, CARPO, or any other persons or organizations with whom the participants may be otherwise affiliated. The contents of this document can under no circumstances be regarded as reflecting the position of the European Union or the Embassy of the Kingdom of the Netherlands to Yemen.

## Development Champions

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# ABOUT THE “RETHINKING YEMEN’S ECONOMY” INITIATIVE

This two-year project, which was launched in March 2017, is an initiative to identify Yemen’s economic, humanitarian, social and developmental priorities in light of the ongoing conflict in Yemen and to prepare for the post-conflict recovery period. The project aims to build consensus in crucial policy areas through engaging and promoting informed Yemeni voices in the public discourse, and to positively influence local, regional and international development agendas.

The project has four components: (1) in the Development Champions Forums, Yemeni experts and professionals in social and economic development will identify key issues for intervention and provide recommendations towards tackling these issues; (2) in the Research

Hive, the project consortium will – based on the issues and recommendations of the Development Champions – conduct research and identify best practices and lessons learned from international experiences to create knowledge capital for the Rethinking Yemen’s Economy initiative; (3) in the public outreach component, the consortium will implement consultation workshops with local stakeholders, including the private sector, youth and civil society organizations; moreover, campaigns through both traditional and social media outlets will be conducted to engage the wider Yemeni public; (4) and through regional and international engagement the consortium will inform stakeholders of project outcomes and aim to motivate and guide the international community’s policy interventions to the greatest benefit of the people of Yemen.

## Implementing Partners

The project is implemented by a consortium of the following three partners:



**The Sana’a Center for Strategic Studies (SCSS)** is an independent policy and research think-tank that provides new approaches to understanding Yemen and the surrounding region, through balanced perspectives, in-depth studies and expert analysis. Founded in 2014, the SCSS conducts research and consultations in the fields of political, economic, civil and social development, in addition to providing technical and analytical advice regarding key issues of local, regional and international concern.  
[www.sanaacenter.org](http://www.sanaacenter.org)



**DeepRoot Consulting** is a dynamic social enterprise passionate about Yemen’s development. DeepRoot aims to help international development actors, the private sector, local civil society organizations and the Yemeni Government anchor their interventions in a deep understanding of Yemen’s national and local contexts, and international best practices. Our leadership team and advisory board has decades of combined experience working in Yemen and internationally in the public, private and nonprofit sectors.  
[www.deeproot.consulting](http://www.deeproot.consulting)



**The Center for Applied Research in Partnership with the Orient (CARPO)** is a Germany-based organization whose work is situated at the nexus of research, consultancy and exchange with a focus on implementing projects in close cooperation and partnership with stakeholders in the Middle East. The CARPO team has long-standing experience in the implementation of projects in cooperation with partners from the region and a deep understanding of the Yemeni context.  
[www.carpo-bonn.org](http://www.carpo-bonn.org)

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