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The Economic Dimensions of the Conflict in Yemen: Final Report

Fiona Davies and Achim Wennmann
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Executive Summary

1. Introduction

This report provides a synthesis of the views of different stakeholders on the economic dimensions of the conflict in Yemen. The research focused on the following themes:

- Economic interests of Ansar Allah, the various constituents of the PLC and, to the extent relevant, their affiliated interests.
- Asymmetry in the way the economy functions in different areas across Yemen.
- Degree of the IRG's financial vulnerability without full international recognition.
- Existing internal divisions within each party to the conflict, in relation to the economy.
- The sources of leverage to push the economic file.

The authors conducted interviews with Yemeni stakeholders and members of the international community in October 2022, attended the Yemen International Forum (June 2022) and the Yemen Track II conference (November 2022), and presented preliminary findings in Amman (13-15 December).

2. Overall observations

- A new feature of Yemen's conflict in the economic domain is the trend towards 'economic balkanization' within PLC-controlled areas. This new feature emphasises how control over territory and cities, and associated revenue generation and patronage opportunities, have become central political aims of the various parties within the PLC. It to some extent mirrors the economic approach of AA in the territory under its control in recent years.
- Individual PLC actors also advance their resource extraction through engagement with international partners, reflecting the economic value of international recognition and associated access to financial assistance.
- The competition between PLC and AA has nurtured a new round of economic warfare. The PLC aims collectively to limit AA's ability to benefit from international engagement, by reiterating its position that it is the sole legitimate representative of Yemen internationally. Meanwhile, AA is using the means at its disposal to prevent PLC access to revenue from natural resource exports, by launching drone attacks on oil and gas installations and shipping.
- The consequence of 'economic balkanization' and the new round of economic warfare is a negative equilibrium. All actors are consolidating control over revenue sources to bolster their own power and legitimacy within the specific territories under their control. Economic warfare targets critical economic infrastructure with the intention to affect opportunities for revenue generation. These efforts emphasize 'zero-sum' mentalities and a 'winner gets it all' logic, harkening back to the notion of control over a central state as the 'big prize'.
- The focus on controlling revenue sources is also linked to the parties' desire to assert a certain performance legitimacy viz-a-viz their populations. As the active conflict and related insecurity have declined in many parts of Yemen, people's expectations for the payment of salaries and delivery of basic commodities and services (for example, fuel and electricity) have increased. These dynamics therefore emphasise the importance of adequate financing and adequate governance capacity for delivery, elements which the parties to the conflict lack to a greater or lesser degree.

3. Overview of economic interests

3.1. Ansar Allah

- AA aims to run a government system that has limited exposure to external influence. To support this strategic autonomy, AA is continuing the progressive consolidation of economic activities in areas under its control. It has created a centralised resource mobilisation system and is implementing programmes to boost local production and limit dependence on imports.
- While AA's economy is closed in governance terms, the economy is permeable to trade with the rest of Yemen and in the region.
- AA's economic strategies appeared to have created relative economic stability. Areas controlled by AA have a relatively effective taxation system and stable macro-economic situation, although AA's economic governance has coercive features.
- To date, AA has managed to project a skilful bifurcation of its responsibilities within its territories – presenting itself a state actor when it comes to revenue collection, but not when it comes to expenditure and service delivery. The sustainability of this bifurcation has come under increasing pressure now that there is no longer an active war context.

3.2. Presidential Leadership Council

- The PLC does not yet have a unified economic interest or vision for the economy, beyond revenue generation and exchange rate stabilisation. Although these issues are a priority, progress on revenue generation in particular is hampered by lack of trust and co-ordination between its constituent elements.
- Different players within the PLC seeking to control their own revenue bases for their own ends, in particular, payment of their own forces and public officials. They primarily exert revenue control on a geographic basis, rather than over particular revenue streams.
- The IRG is dependent on international recognition for its survival as a political unit. Maintaining a monopoly on international recognition is therefore a key economic interest. The IRG would not have political, economic, or military authority if it were not for the assistance provided by and recognition received from the international community, particularly the Saudi-led coalition.

3.3. KSA and UAE

- The way in which KSA and UAE provide financial support to the PLC has tended to reflect their own individual interests. KSA and UAE reportedly often prefer to support specific actors within the PLC who are allied to their interests, rather than the PLC as a whole, feeding into the creation of economic fiefdoms and territorial control of resources.
- A feature of KSA and UAE economic interest in Yemen is that it is increasingly projected in a manner that is autonomous from 'Western' international actors.

3.4. Yemeni private sector

- The private sector struggles with ever-increasing costs of doing business in Yemen.
- The private sector has an interest in the success of the peace process dossier on salaries and public sector revenue, given that improved purchasing power would lead to increased demand for essential food items and services.

- The private sector also has a clear interest in a predictable and secure operating environment. Predictability and security may be of greater priority to private sector actors than a particular governance structure countrywide.

4. Asymmetries in the way the economy functions

- The overall division of Yemen's economy is still perceived to be divided along the primary fault lines of AA and PLC territorial control, involving two currencies and taxation systems. Fragmentation is starting to extend beyond two zones into multiple territorial fiefdoms within the PLC-held areas.
- Private sector actors operating across both territories face increased operating costs associated with currency exchange and double taxation, both between AA and PLC territories, and within PLC territories. Traders enable continued movements of goods but at a higher price.
- Despite the existing asymmetries in the economy, there are also commonalities, especially with respect to the structure of the private sector. Powerful trading houses with links to long-standing elite and political connections continue to dominate private sector activity. Yemen's oligopolistic private sector structure has not been fundamentally altered by the fragmentation of its economy.

5. Internal divisions within each party to the conflict

- The AA movement it not homogenous, but is largely able to contain the tensions between the various different groupings.
- The individual interests of PLC actors remain in tension with one another, and prevent effective delivery of security objectives, as well as revenue generation and management.
- From the Southern Transitional Council (STC) perspective, not all actors currently within the PLC belong to what they understand as the 'south'. Their definition of the 'south' is based on the territories that previously belonged to the People's Democratic Republic of Yemen prior to 1990.
- The private sector can have the potential to influence the conflict. Some larger corporate actors, including new entrants, have developed a business model that relies entirely on their links to individual conflict actors. They might behave as spoilers if the territorial control of these conflict actors comes under threat.
- The majority of business actors should not be considered as potential 'spoilers', however. For these actors, peace represents a welcome return to greater profit and an expansion of market demand.

6. Sources of leverage to push the economic file

6.1. The international community

- The formulation of Security Council Resolution 2216 (2015) prevents more systematic international community engagement with AA in terms of dialogue on economic issues. This blockage on dialogue with AA was considered by several interviewees to be unhelpful, as it increases scope for a distorted characterisation of their actions with respect to the economy, limits understanding of their economic needs and objectives, prevents the provision of capacity support and inhibits discussion on solutions to the current economic distortions.

- The international community could increase its credibility with some Yemeni actors if it takes greater steps to speak out against, or take action on, economic mismanagement and corruption by conflict actors in Yemen, especially by the IRG.
- The international community could increase its leverage over the economic file by strengthening its own coordination.

6.2. Regional actors

- Although regional actors – including the KSA and UAE – are viewed as wanting to be seen to be taking action to address the economic file and to take credit for the successes achieved their support is considered unreliable, and not always co-ordinated with other international actors, which makes it hard to fully harness its potential leverage capacity.

6.3. The Yemeni private sector

- The leverage of the private sector builds from the fact that it is closely entwined with the prevailing realpolitik.
- On certain issues, the private sector may be better placed to conduct economic dialogue with AA than the international community.

7. Concluding observations: Opportunities for the peace processes

- Current trends towards 'economic balkanization' are operating as a zero-sum game. There may be opportunities to transform this negative trend into a more positive framework that recognises and co-ordinates the devolution of economic power. However, such an avenue for change requires an economic truce, prioritizing trust-building and deconstructing enemy pictures and narratives by Yemeni and international actors.
- Within a de facto economic system of increasing regional economic autonomies, international actors should engage with all relevant economic actors, providing capacity development and policy support as appropriate, with a focus on enhancing co-ordination between them.
- Finding compromise on the sharing of income from natural resources is a new frontier for disarming Yemen's economic warfare. To advance discussion on income sharing from natural resources, there is a need to expand understanding about existing sharing mechanisms.
- Developing scenarios for Yemen's future economy could be a valuable starting point for overcoming current zero-sum mentalities. Such a process must be inclusive of inputs from AA, the PLC, private sector actors as well as technical experts relevant to specific issues.
- The UN-led peace processes should shift gear towards a more pro-active agenda setting roles in the economic domain. This could build on better linkages across the political, security and the economic tracks.

1. Introduction

This report is a synthesis of key observations on the economic dimensions of the conflict in Yemen in the period May to December 2022. The work is an independent study commissioned by the United Nations Development Programme (UNDP) and the European Union (EU) through the European Resources for Mediation Support (ERMES) to further analyse the economic drivers of the Yemeni conflict and potential opportunities for peace by researching the economic factors and interests that influence the conflict dynamics. The research also provides an input to the Office of the United Nations Special Envoy for Yemen on the economic aspects of the political process.

Building on two previous reports for 2020 and 2021, the current report covers the following focus areas under the Terms of Reference for this assignment:

- Economic interests of Ansar Allah, the various constituents of the PLC and, to the extent relevant, their affiliated interests.
- Asymmetry in the way the economy functions in different areas across Yemen.
- Degree of the IRG’s financial vulnerability without full international recognition.
- Existing internal divisions within each party to the conflict, in relation to the economy.
- The sources of leverage to push the economic file.

Key foundations for this report include 11 conversations conducted between 14 and 25 October 2022 that were focused on the economic dimensions of the conflict in Yemen and on understanding the perspectives of Yemeni stakeholders. The report has also been informed by conversations during the Yemen International Forum (Stockholm, 17-19 June 2022) and the Yemen Track II conference (Amman, 8 November 2022), as well as by feedback received on the draft report (Amman, 13-15 December 2022).

This report is a synthesis of multiple views and opinions expressed during the interviews and in the cited publications. These views are presented in the report in order to provide, to the extent possible, a full spectrum of views on the economic dimensions of the conflict in Yemen as a contribution to finding pathways towards a more peaceful Yemen. As the authors interpreted these views and opinions to draft this synthesis, they have focused on what is ‘new’ in contrast to the 2020 and 2021 reports, acknowledging an ever-richer resource base on the economic dimensions of the conflict in Yemen.

The authors would like to recognize the important assistance provided by Emilian Berutti, Maëlys Glück, and Claudia Wiehler in preparing this report, including background research and support for the interview process.

2. Overall observations on the economic dimensions of the conflict

The research for this assignment on the economic interests in the conflict in Yemen occurred within an **overall context of a transition from all-out war towards an evolving 'no war, no peace' situation.** The significant reduction in violence and insecurity across Yemen since April 2022 represents 'good news'. However, conflict dynamics continue to interact with many other forms of crises in terms of food security, public health, and environmental challenges across Yemen. In particular, after a brief respite, conflict between the various parties for control over the economy continues unabated.

In the political sphere, this assignment occurred in the **context of the newly established Presidential Leadership Council (PLC**), whose formation was brokered by the Kingdom of Saudi Arabia (KSA). The PLC is the executive body of Yemen's internationally recognized government (IRG), formed by a presidential decree on 7 April 2022 to seek a comprehensive political solution to the Yemeni civil war. It is headed by Rashad Muhammad Al-Alimi and has a membership of eight members uniting different political tendencies and military actors in Yemen who oppose Ansah Allah (AA). The formation of the PLC occurred a few days after the United Nations Special Envoy for Yemen brokered a truce between IRG and AA. The truce lasted until October 2022, when conditions for its renewal were not agreed between the parties. Although the UN-sponsored talks between the parties have lost momentum, KSA maintains a separate bilateral negotiations track with AA.

A new feature of Yemen's conflict in the economic domain is the trend towards 'economic balkanization' within PLC-controlled areas. This new feature emphasises how control over territory and cities, and associated revenue generation and patronage opportunities, have become central political aims of the various parties within the PLC. It to some extent mirrors the economic approach of AA in the territory under its control in recent years. Achievement of 'economic balkanization' has a coercive component, with PLC actors using the militias under their control to advance their economic interests in their territories. These interests are primarily centred on resource extraction.

Individual PLC actors also advance their resource extraction through engagement with international partners, reflecting the economic value of international recognition and associated access to financial assistance. This constellation of interests has shaped a situation whereby PLC actors aim to maximise their own individual benefits from international engagement at the expense of other PLC actors. Specifically, the Southern Transitional Council (STC) has used its membership in the PLC to advance engagement with international actors in view of obtaining financial assistance or other types of support.

The competition between PLC and AA has nurtured a new round of economic warfare. The PLC aims collectively to limit AA's ability to benefit from international engagement, by reiterating its position that it is the sole legitimate representative of Yemen internationally. Meanwhile, AA is using the means at its disposal to prevent PLC access to revenue from natural resource exports, by launching drone attacks on oil and gas installations and shipping. This has prevented the IRG from earning revenues from oil and gas exports, which constitute the majority of their domestic income and are estimated to amount to USD 1.6 billion on an annual basis. Conversations with members of the international community suggests that the IRG has informed Commercial Banks who are headquartered in AA-controlled territory that they will be cut off from the SWIFT system if they do not comply with the reporting requirements of the internationally-recognised Central Bank of Yemen based in Aden. This has been interpreted by interlocutors as an act of retaliation by IRG against AA for the bombing of oil installations. Disconnection from the SWIFT system would carry significant economic costs for the financial transactions in areas controlled by AA.

The consequence of 'economic balkanization' and the new round of economic warfare is a negative equilibrium. All actors are consolidating control over revenue sources to bolster their own power and legitimacy within the specific territories under their control. Economic warfare targets critical economic infrastructure with the intention to affect opportunities for revenue generation. These efforts emphasize **'zero-sum' mentalities and a 'winner gets it all' logic**, harkening back to the notion of control over a central state as the 'big prize'.

Security and governance imperatives are a driving force behind economic balkanization. All parties to the conflict need revenue to pay their fighters and public servants. They focus on consolidating their control over revenue sources in order to do so. These competitive dynamics are shaping distrust between the leaderships of AA and the PLC, as well as within the PLC, and could make it very hard to advance discussions on a national wealth-sharing mechanism, both as part of the economic track of the peace process and within the PLC economic committee.

The focus on controlling revenue sources is also linked to the parties' desire to assert a certain performance legitimacy viz-a-viz their populations. As the active conflict and related insecurity have declined in many parts of Yemen, people's expectations for the payment of salaries and delivery of basic commodities and services (for example, fuel and electricity) have increased. The authorities can no longer point to ongoing hostilities as an excuse for non-performance, as they could do prior to the April 2022 truce. These dynamics therefore emphasise the importance of adequate financing and adequate governance capacity for delivery, elements which the parties to the conflict lack to a greater or lesser degree.

Economic balkanization is shaping the emergence of a 'governscape' in Yemen. Economic and social relations still knit Yemen together across lines of territorial control, and so the process of 'economic balkanisation' is not necessarily nurturing a series of semi-independent sub-states. Rather, it is shaping Yemen into what is called a 'governscape' (see Box 1). By exhibiting features of an emerging 'governscape', Yemen joins other conflict and post-conflict environments such as Syria, Libya, Myanmar and Afghanistan which are marked by shared or divided sovereignties at different levels and across different sectors. These characteristics of multiple sovereignties test the limits of the effectiveness of international community engagement. However, they also offer several opportunities for elite bargaining processes towards a political settlement, especially around wealth sharing which known to be at the heart of political settlement negotiations (see also section 6.2 below).[1] Even though these approaches bear the risk of strengthening elite controlled economies, they offer the prospect of opening more structured political processes that progressively extract violence and coercion from economic and political interaction.

Box 1: What is an emerging 'governscape'?

A 'governscape' is a landscape "with different constellations of authority and governance that form and spread unevenly within and beyond national boundaries."[2] 'Governscapes' have "irregular geographical reach and intensity of authority and governance, which do not coincide with national boundaries" and they build on the notion that "what constitutes legitimate rule can differ according to the position and perspective from which they are viewed". 'Governscapes' are also always 'emerging' given their inherent dynamism and change over time.[3]

3. Overview of economic interests

3.1. Ansar Allah

AA controls the main population centres of Yemen and therefore also many profitable markets in Yemen.[4] Economic objectives and priorities of Ansar Allah (AA) are framed by the group's *National Vision* published in 2019.[5] The *National Vision* sets out AA's central aim to govern Yemen through pre-conflict institutions and government structures[6], albeit overseen by a "shadow" or "parallel" state in the form of *mushrifeen* (supervisors) that directly supervise local-decision making processes.[7] AA supervisors in local councils "possess real authority at the neighbourhood, district and governorate levels".[8]

AA's *National Vision* identifies various economic challenges as barriers to achieving their governance objectives, including factors such as the destruction of economic infrastructure and the inflation of public debt. The *National Vision* suggests several economic mechanisms to tackle the economic challenges, including by diversifying the economy from extractive resources and towards the agricultural and marine sectors.[9]

AA aims to run a government system that has limited exposure to external influence.[10] "The Houthis operate a "walled garden" economy, security networks and governance that function well […] because they are separated from the rest of the country by front lines and different transport routes."[11] AA's *National Vision* says that "One of the priorities of the modern Yemeni Government is to preserve the independence, sovereignty and unity of Yemen and protect it from any (foreign) hegemony, trusteeship, dependence or occupation, and to build balanced relations with Arab and Islamic countries and all other countries of the world based on mutual foundations, interests and benefits while remaining committed to all responsibilities towards our Arab and Islamic nation and the world."[12]

To support its strategic autonomy, AA is progressively consolidating economic activities in areas under its control. AA has created a centralised resource mobilisation system. In this system, AA "is controlling local businesses through a consistent process of economic interference, including: (1) direct takeover of profitable enterprises; (2) creation of monopolies under its direct control or issuance of onerous regulatory demands against competitors; and (3) payment demands – through an internal customs area and collection of taxes. This means that [… AA] has multiple revenue streams to fund the war in addition to any rent earned through black market practices."[13] AA has also created new central institutions to control external aid flows to the local level and to monopolise revenue mobilisation and collection efforts. These institutions include the Supreme Council for the Management and Coordination of Humanitarian Affairs and International Cooperation and the General Authority for Zakat. Consequently, “there has been a re-formalisation of the de facto operations of the local authority system, accompanied by attempts to increase central oversight and control and, albeit less systematically, to improve services and the functioning of formal institutions.”[14]

AA is implementing programmes to boost local production and limit Yemen’s dependence on imports. AA have “adopted regulatory measures which penalise the formal private sector if it fails to invest in local production – part of a suite of policies aimed at developing the kind of self-sufficiency needed to weather a long period of exclusion from international legitimacy”.[15] An AA decree issued early in 2021 requires food import companies to procure 20% of their total stock from domestic producers. In response, importers have set up a company, al-Talal, with capital of about $1.6 million. When they import food, they deposit 20% of the monetary value of the import contract with the company. Part of that deposit is invested with individual farmers, who agree to a forward contract to produce a particular crop. These arrangements apply to crops such as spices, legumes, and garlic, but not to cereals.

While AA’s economy is closed in governance terms, multiple interlocutors confirm the permeability of the economy to trade in the rest of Yemen and in the region. Several large commercial actors maintain operations and value chains across the entire territory of Yemen and are focusing especially on the north because this is where most Yemeni live, and hence where the biggest markets are, especially for basic goods and consumer items.

AA’s economic strategies appeared to have created relative economic stability, particularly as compared to the territories controlled by the PLC. Areas controlled by AA have a relatively effective taxation system and stable macro-economic situation, although some interlocutors highlighted the coercive features of AA’s economic governance. Especially, humanitarian actors report exposure to rent seeking attitudes of AA as well as efforts to manipulate the delivery of aid towards their political interest. Fuel shortages, which had been crippling economic activity in areas controlled by AA, have been largely alleviated since the commencement of the truce in April, a situation that has continued even though the truce has formally expired.

During the first two truces, AA focused on removing obstacles to expansion of the economy, including on opening ports and the airport. Their insistence on salary payments from oil and gas revenues to pay its fighters and public officials was a stumbling block in the third truce negotiations in September 2022, which were not successful. Salary payments remain a major item under discussion in subsequent bilateral talks with the Kingdom of Saudi Arabia (KSA). AA’s focus on accessing oil and gas revenues reflects a desire to use Hodeidah port revenues to meet other expenditures, as well as a view that oil and gas revenues are ‘national’ in nature, and should benefit all parties in Yemen, not just the ones considered by the international community to be ‘legitimate’.

To date, AA has managed to project a skilful bifurcation of its responsibilities within its territories – presenting itself a state actor when it comes to revenue collection, but not when it comes to expenditure and service delivery. The sustainability of this bifurcation has come under increasing pressure now that there is no longer an active war context, as returning fighters expect recompense for their efforts in the form of salary payments. The truce scenario of no war, but no peace, therefore, puts AA under a degree of internal political pressure which it is seeking to manage through its position on salaries in the truce discussions.

Its recent actions to prevent crude oil exports from Hadramawt and Shabwa by conducting drone strikes underscores the seriousness with which it is attempting to advance its position on receiving a share of oil and gas revenues to enable payment of salaries. Interlocutors also suggested that AA was not ready for another truce because they are not ready to start providing services in the absence of a war status, which has to date served as an excuse to justify their limited service delivery.

The economic impact of the truce has reportedly not been uniformly positive in AA areas. Although fuel shortages have eased, the truce has also reportedly had a negative economic impact on civilians as the need for informal payments increased, according to some observers. AA fighters focused their efforts on revenue generation during the truce, with a specific focus on obtaining payments at checkpoints from civilians. This underscores the internal pressure faced by AA to find resources for payment of its fighters.

One other shift with respect to AA's economic interests relates to co-ordination. Whereas in the past AA expressed an interest in co-ordination over monetary and banking issues, in order to ease the adverse effects on the economy in their territories, this interest has diminished over time. AA has largely been able to establish effective mechanisms for insulating the economy in the areas under their control from the problems affecting the economy in areas under PLC control, particularly with respect to exchange rate instability and inflation. The economy in areas under AA control has become a 'closed economy' in terms of governance. Consequently, **AA places limited value on co-ordination, and is instead seeking to find its own solutions to challenges such as limited availability of domestic currency** (physical bank notes), for example by accelerating the use of electronic payments. However**, its demand for a share of national oil and gas revenues in order to pay salaries may also reflect a need for foreign exchange, thus signalling that the economy under AA control is not entirely self-sufficient.**

3.2. Presidential Leadership Council

The PLC does not yet have a unified economic interest or vision for the economy, beyond revenue generation and exchange rate stabilisation. Although revenue generation is a priority, its efforts to consolidate and increase revenue generation are hampered by lack of trust and co-ordination between its constituent elements. Different players within the PLC seeking to control their own revenue bases for their own ends, in particular, payment of their own forces and public officials. Unless a single unified mechanism can be established for the payment of all PLC-affiliated forces, the likelihood of co-ordination over revenue collection and revenue sharing between the various PLC elements is felt to be limited.

There has been an increase in local autonomy in PLC territories. "The overall trajectory […] has been towards increased local autonomy – and while important variations exist between governorates, changes everywhere follow a similar trajectory in terms of decision-making, revenues and local services."[16] These gains in autonomy by local councils and governorates are closely correlated to their ability to generate *ad hoc* local revenue streams. Considering the high dependence of the Yemeni economy on its extractive sectors, Marib, Shabwa, and Hadhramaut have leveraged their economic resources to receive greater spheres of autonomy vis-à-vis the IRG.[17]

Different elements within the PLC primarily exert revenue control on a geographic basis, rather than over particular revenue streams. One example of this is the revenue accruing to Tareq Saleh as a result of his economic control of Taiz. However, in some cases, geography and revenue streams coincide. For example, Marib, Hadramawt and Shabwa receive revenues from petroleum resources generated in their governorates. The Southern Transitional Council (STC) is able to collect informal port revenues on the back of its territorial control of Aden port. Al Mahra governorate collects and retains customs revenues from goods crossing the border from Oman.[18] This Balkanisation of revenue lends itself to PLC actors trying to create their own economies in the territories under their control.

The IRG is dependent on international recognition for its survival as a political unit. Maintaining a monopoly on international recognition is therefore a key economic interest. The IRG would not have political, economic, or military authority if it were not for the assistance provided by and recognition received from the international community, particularly the Saudi-led coalition. This factor is particularly significant given that AA attacks on oil installations have reduced income from natural resources for the IRG with several actors noting the risk of an an implosion in IRG finances without continued financial assistance from the KSA (see also Box 2).

Box 2: The economic value of international recognition for the IRG

The UN-brokered truce indicates that the IRG and actors associated to the former Hadi government, replaced by the PLC, are dependent on the international community for their economic survival.[19]

The Kingdom of Saudi Arabia (KSA) and the United Arab Emirates (UAE) are the IRG's political, military and economic guarantors, making this relationship the primary economic interest.[20] In military terms these functions were illustrated by the intervention to prevent the takeover of Marib in early 2022. IRG forces relied significantly on support from UAE-backed forces.[21] Without these, it would have been possible that the IRG would have lost control over the city and its economic capacities, thereby handing a significant economic advantage to AA.:

The viability of the IRG economy is dependent on financial support from the Saudi-led coalition. The Central Bank of Yemen (CBY) Aden is dependent on Saudi and Emirati money to supply foreign exchange to importers and stabilise the exchange rate. Without this funding, the IRG's control over the new YER would loosen even more, resulting in growing inflation rates. "The revised letters of credit system that CBY Aden began implementing from November 2018 onwards was based on the USD 2 billion deposit that Saudi Arabia provided in March 2018. CBY Aden issued letters of credit underwritten by funds allocated from the Saudi deposit and used them to facilitate the import of five basic commodities – wheat, rice, sugar, milk, and cooking oil. The USD 2 billion deposit and the additional financial support that Saudi Arabia provided to the Government of Yemen (GoY) and CBY Aden helped stabilise the value of the riyal."[22] The currency inflation and the economic mismanagement of the IRG are only running at a minimum because of the liquidity aid received from its Gulf partner countries. The announcement of a further USD 3 billion from the Saudis and the Emiratis in the follow-up of the Riyad consultations of 2022 indicates the high dependency of the IRG on their support to sustain its economic zone, especially its FX rate.[23] In November 2022, KSA and UAE provided an additional USD 1 billion by to GoY through the Arab Monitoring Fund.

Without the support from the Saudi-led coalition, the IRG would not be able to leverage the economy vis-à-vis AA. The Saudi-led coalition has damaged the import capabilities of

AA through its enforcement of UN Security Council Resolution 2216, which calls upon “all Member States, in particular States neighbouring Yemen, to inspect all cargo to Yemen” if the State concerned has reasonable grounds to believe that the cargo contains embargoed goods. The Saudi-led coalition has also enforced the IRG’s own import restrictions on goods such as fuel. “Barring a brief three-month hiatus between October and December 2020, IRG has permitted only limited and occasional commercial fuel imports via Al Hodeidah.”[24] These controls were enforced by the Saudi-led coalition up until the April 2022 truce agreement which enabled a more consistent supply of fuel into Hodeidah port. Equally, control of the waterways by the Saudi-led coalition has resulted in “Shipping fees [that] remain much higher in 2020, due in large part to delays caused by the Saudi-led coalition’s inspection and clearance mechanisms.”[25]

3.3. KSA and UAE

The way in which KSA and UAE provide financial support to the PLC has tended to reflect their own individual interests. KSA and UAE reportedly often prefer to support specific actors within the PLC who are allied to their interests, rather than the PLC as a whole. By focusing on individual actors, some observers noted that they have fed into the creation of economic fiefdoms and territorial control of resources. It was noted that Islah actors sponsored by KSA control oil and gas production, while the UAE and its affiliated Yemeni forces control the Belhaf gas processing facility. In some cases, it was observed that splits within the PLC may even help further the economic interests of the KSA and UAE – for example, Hadramawt’s demands for autonomy may be beneficial for UAE and KSA ambitions for access to the Arabian Sea. Nonetheless, the recent $1bn grant provided by KSA and UAE through the Arab Monetary Fund for economic stabilisation of the Government of Yemen[26] signals a willingness to provide financial backing to the PLC as a whole to ensure its viability. However, this does not necessarily imply that KSA and UAE’s will cease to provide support to individual actors within the PLC in parallel.

A feature of KSA and UAE economic interest in Yemen is that it is increasingly projected in a manner that is autonomous from ‘Western’ international actors. This is evidenced by KSA opening an additional peace process space which resulted in the formation of the PLC as well as its ongoing bilateral negotiations with AA following the failure of UN-brokered truce negotiations**.** ‘Western’ international actors have reportedly limited leverage to shape KSA engagement.

3.4. Yemeni private sector

The private sector struggles with ever increasing costs of doing business in Yemen, which reportedly make local manufacturing uncompetitive. All Yemeni parties to the conflict face a clear incentive to control their own economies, in order to capture and manage revenue streams that enable them to pay for the costs of war. This approach is to the detriment of the private sector as territorial fragmentation of the economy prevents entrepreneurs from taking their businesses to scale and consolidates the grip of established conglomerates on the economy. Some private sector actors are trying to develop a vision for strengthening domestic productive capability and supply chains in the face of these challenges, but most others are focused on day-to-day survival and problem solving.

Larger private sector actors in Yemen identify a number of priorities for economic stabilisation. These include improving the functionality of the banking sector to facilitate imports, exports, and investment; removing blockages related to ports and roads to enable free flow of goods and services; and increasing consumers' purchasing power, especially for essential food items and services. The latter point emphasizes private sector interest in the success of the peace process dossier on salaries and public sector revenue, given that this purchasing power would be dedicated to buying essential food items and services. Overall, these priorities are embedded in the commitment of large corporations to market-based solutions to economic recovery.

Large Yemeni corporations also have a clear interest in a predictable and secure operating environment. On the one hand, this interest is related to establishing a predictable regulatory environment, on the other hand it is related to ensuring payment of contractual obligations by different governing entities. Yemeni corporations still consider such contracts to be commercially valuable, and delays in payments for goods and services are a major concern. They therefore have an interest in the stability of revenue to governing entities and the transparency of public expenditure management so that contractual dues are paid. Large Yemeni corporations may attach greater priority to the achievement of predictability and security than to the re-establishment of a unified government. From the private sector view, there can be predictability and security within a reality of Yemen shaped by multiple governing entities, a perspective which diverges from the international community's priority of unifying Yemen under a single government.

Large Yemeni corporations are not likely to try to prevent the entry of new private sector actors into their sectors of the economy, but they may draw the line at any actions that interfere with their government contracts, some interviewees suggested. Several large corporations have privileged relationships with different government entities across the territory of Yemen. There is little appetite to open government contacts to competition and in case the issue of opening the allocation of public sector resources to economic competition would become part of the economic track, this would likely generate pushback from larger private entities. A similar dynamic might occur in case government entities and the international community would push for a large-scale import substitution policy as an economic priority for reconstruction and climate change adaptation in Yemen.

4. Asymmetries in the way the economy functions

As is already well known, macroeconomic asymmetries shape two de facto economic zones in Yemen. According to the UN Panel of Experts, “The conscious and systematic fragmentation of the economic system and institutions of Yemen by the Government of Yemen and the Houthis alike has resulted in the emergence of separate central banks, customs and revenue authorities, financial intelligence units and telecommunications authorities, as well as separate economic, trade, banking, tariff and tax laws and policies in the two regions ”.[27] These sub-economies were reinforced when the IRG placed an embargo on fuel entering AA-controlled Hodeidah port in 2019, and AA banned the circulation of the new Yemeni Riyal (YER) in its territories in early 2020.

Interviews confirmed that the overall division of Yemen’s economy is still perceived to be divided along the primary fault lines of AA and PLC territorial control, involving the two currencies and taxation systems. Private sector actors operating across both territories face increased operating costs associated with currency exchange and double taxation.

Traders enable continued movements of goods but at a higher price. Transfer fees for traders and cross-border economic flows can amount to fees worth 100% of the commodities’ real market valuation.[28] “Groups on each side of the conflict benefit from trade.”[29] But “Road transportation fees increased by 208% between December 2013 and the end of December 2020 due to a lack of security, road damages, informal payments at checkpoints and long detours.”[30] And disruption to road transport in rural areas through the conflict harms local communities’ local development and economic resilience.[31]

The phenomenon of double taxation is not just limited to economic activity within the two main areas of territorial control. It is increasingly becoming a feature of economic activity between different PLC territories, as each PLC actor seeks to bolster its own access to revenue though taxation or controlling economic assets. Thus, goods coming over the border from Oman to Hadramawt face taxation in both Al Mahra and Hadramawt. Goods coming through Aden port are subject to formal taxation by the IRG, and informal taxation by actors affiliated to the STC. Attempts by the IRG to assert its legitimacy through revenue collection are likely to add to economic costs for the private sector in the short-term, as the IRG does not have the means of control to eliminate informal revenue collection by other PLC elements.

Fragmentation is starting to extend beyond two zones into multiple territorial fiefdoms. Yemen’s “local governance […] has gone from a highly centralised system, in which ultimate de-facto authority rested with the President, to a situation of growing fragmentation and divergence.”[32] One line of research suggests that “there are now, broadly speaking, seven different Yemens: the AA-controlled northern highlands, Hodeidah and the Red Sea coast, Taiz, Marib and al-Jawf, Aden and the South, Hadramout, and Mahra and Socotra. These geographical blocs have distinct histories, different political and sectarian inclinations, and, in some cases, different languages. As the war has fractured the country, what was once a single state is now in seven pieces.”[33]

Box 3: Marib's financial autonomy

Marib's autonomy derives directly from the deal it cut during the 2013-2014 National Dialogue Conference, whereby it is entitled to 20% of the income generated from extractive industries in the governorate.[34] According to some estimates, "oil production in Marib is now about 8,000 barrels per day. At average prices for 2021, this oil is worth approximately $17 million per month or $200 million per year on the international market".[35] While Marib is entitled to 20%, some interlocuters suggest that it doesn't remit any revenue from extractives to the Central Bank in Aden, meaning it retains these revenues in their entirety.

The "steps towards autonomy in Marib were taken in close coordination with President Abdrabbuh Mansur Hadi and the Saudi-led coalition."[36] The governate provided governance mechanisms to its citizens, detaching itself from the broader trend of economic collapse and political dysfunctionality. Thus, Marib has capitalised "on its unique economic, demographic and security advantages" to achieve a degree of political and financial autonomy that far exceeds any other governorate in Yemen.

Economic asymmetries are evident between the borderlands and the rest of the country. Some borderlands have suffered acutely as a result of the conflict - this is particularly the case for the Eastern borderlands between AA controlled territories and KSA. They have lost the economic activity previously associated with thriving border markets, and are now militarised and mined. Their suffering has reportedly become a magnet for the mobilisation of anti-coalition fighters. Western borderlands between PLC controlled territories and KSA have fared somewhat better, as economic activity has shifted from the Western side. The border with Oman in Al Mahra has benefited from significant Omani investment over a long period and relative security. It is not clear that any existing parties to the conflict have an interest in making the case for economic revival of the borderlands, but it was noted that improvement of economic conditions in the Eastern borderlands might stop communities from sending their sons to the frontlines.

Increased asymmetries in the way the economy is managed across Yemen mask commonalities in the structure of the private sector which are a continuing impediment to broad-based economic development. Powerful trading houses with links to long-standing elite and political connections dominate private sector activity. The purpose of the banking sector is mainly to serve these trading houses, a number of whom have ownership stakes in the banks. Politically-connected new entrants into the private sector may disrupt the role of pre-existing elite actors, but they do not disrupt the overall elite dynamic. The elites are generally able to withstand the economic costs arising from the fragmentation of Yemen's economy, and to navigate their way through the conflict context. Small and medium enterprises are the most vulnerable actors within the private sector, as they have no constituency or community that advocates on their behalf, and no access to finance. They have limited ability to absorb increasing tax rates or the multiplication of other levies arising from the fragmentation of Yemen's economy. Overall, it is important to underline that even if it is possible to reduce asymmetries and thereby to reduce the cost of doing business, this would not fundamentally affect Yemen's oligopolistic economic structure dominated by about two dozen powerful entrepreneurs and their associated networks.

5. Internal divisions within each party to the conflict

The AA movement has multiple internal divisions, including differences in interests between urban and rural areas, Hashemites and non-Hashemites, pro-Iranian and tribal groups, and Zaidi and GPC affiliates. Nonetheless, AA is reported to have internal mechanisms which enable it to contain the tensions between the various different groupings, and prevent them from spilling over into conflict.

Achieving PLC unity against AA is proving difficult. The individual interests of various PLC actors remain in tension with one another, and prevent effective delivery of security objectives, as well as revenue generation and management. Interlocutors also noted that the generalised formulation of the PLC-controlled territories as the 'south' and the AA-controlled territories as the 'north' is misleading, because it masks significant differences in perspectives about what is 'south' and what is 'north'. These differences in perception are amongst some of the greatest drivers of the internal divisions within PLC (in addition to the access to revenues noted above).

From the STC perspective, not all actors currently within the PLC belong to what they understand as the 'south'. Their definition of the 'south' is based on the territories which previously belonged to the People's Democratic Republic of Yemen prior to 1990. The STC does not appear to consider areas such as Taiz and Marib, which currently fall under PLC control, to be part of the 'south', as these areas were previously part of the 'northern' Yemen Arab Republic prior to unification. It is not clear that the STC shares a common economic or governance vision with these 'northern' PLC actors, a situation which is likely to complicate attempts to overcome current economic fragmentation in the PLC territories considerably.

Within the 'south' defined as the territories which belonged to the People's Democratic Republic of Yemen prior to 1990, continuation of geographic and tribal splits dating back to the 1960s has been observed. Notably, there are splits between the areas which supported the rebellion against colonial control (Lahj, Al Dhale) and subsequently attained political dominance in the People's Democratic Republic, and those that supplied the colonial forces and were closer to President Saleh after unification (Abyan, Shabwa). These splits reportedly continue to play out in current efforts for control over lucrative business sectors (e.g. fuel importation and money exchange) in the southern economy.

Just as it is important not to assume that the PLC is synonymous with the 'south', it is also important **not to assume that all PLC members were on-board with the proposals made by the Office of the UN Special Envoy with respect to the most recent truce negotiations.** In particular, the STC reportedly did not agree with the truce offer to pay salaries in areas under AA control, nor the framing assumption of negotiations within the context of a unified Yemen.

The private sector, although not a party to the conflict, can have the potential to influence the course of the conflict. It is multifaceted with respect to its potential to act in a peace-enhancing way or as spoiler. Some larger corporate actors, including new entrants, are reported to have developed a business model that relies entirely on their links to individual conflict actors. These businesses align themselves to conflict actors who will provide them with business opportunities based on their territorial control. Loss of that territorial control will in turn damage their business viability and might pose a significant enough threat for them to behave as spoilers.

The majority of business actors should not be considered as potential 'spoilers', however. Many businesses have no reason to prefer a continuation of a conflict situation which increases their operating costs and reduces their growth prospects. They view themselves as having a philanthropic as well as business motivations, and on occasion, subsidise the costs of goods in the market in order to support struggling consumers. For these actors, peace represents a welcome return to greater profit and an expansion of market demand.

6. Sources of leverage to push the economic file

6.1. The international community

The formulation of Security Council Resolution 2216 (2015) prevents more systematic international community engagement with AA in terms of dialogue on economic issues. Resolution 2216 reaffirms the UN Security Council's support for "the legitimacy of the President of Yemen"[37] and demands that the Houthis "withdraw their forces from all areas they have seized, including Sana'a, and, cease all actions that are exclusively within the authority of the legitimate government of Yemen." This wording clearly signals that AA is not considered a legitimate political actor in Yemen. In consequence, AA is frequently spoken of by the international community, but rarely spoken to, because to engage with them in any formal way would be to recognise their legitimacy. This blockage on dialogue with AA was considered by several interviewees to be unhelpful, as it increases scope for a distorted characterisation of their actions with respect to the economy, limits understanding of their economic needs and objectives, prevents the provision of capacity support and inhibits discussion on solutions to the current economic distortions. The reality as perceived by these interviewees is that AA has done a better job of managing the economy in areas under its control than the IRG. Interviewees also observed that the IRG makes strenuous efforts to ensure that the international community to stay committed to the UNSC Resolution 2216 because it is a central pillar of recognition of their monopoly on 'international recognition' (see also Box 2 above).

The international community could increase its credibility with some Yemeni actors if it takes greater steps to speak out against, or take action on, economic mismanagement and corruption by conflict actors in Yemen, especially by the IRG, according to several interlocutors. Instead, in their view, the international community's interest in promoting accountability and sound financial governance appears to be subordinated to the overriding objective of removal of AA, thereby damaging the international community's credibility when it comes to promoting sound economic management and the resolution of the current economic conflict.

Several members of the international community are reflecting on changing their attitude to the STC since it is now part of the PLC and IRG. These reflections stand in contrast to the approach to AA, which continues to be considered 'non-legitimate'**.** As a result of being part of the PLC, the STC has embarked on an international engagement strategy, emphasising its transition from a non-state armed group to being part of an 'internationally recognized government'. The international community might gain new leverage on the economic file by studying how engaging with STC on capacity building and other technical support can translate into opportunities for economic revival and stabilization in PLC controlled areas.

The international community could increase its leverage if it would strengthen its own coordination. Despite ongoing efforts of donor coordination, interlocutors describe the results so far as weak and as being characterized by significant tensions behind the scenes, especially when it comes to defending mandates and resources. It was also noted that lack of co-ordination between international actors, combined with a weak understanding of economic priorities at the sector level, leads to duplication and ineffective targeting of donor resources to economic recovery. Given the number and diversity for the international presence, several interlocutors have also noted that international actors should be aware of how their support can become instrumentalized in the support of conflict actors, especially associated to the IRG. Given the IRG's dependence on its international recognition as its primary source of income (see Box 2 above), strategic coordination of the international community could become a leverage point viz-à-viz the IRG.

6.2. Regional actors

Regional actors – including the KSA and UAE – are viewed as wanting to be seen to be taking action to address the economic file and to take credit for the successes achieved. However, interlocuters describe regional support as unreliable, and not always co-ordinated with other international actors, which makes it hard to fully harness its potential leverage capacity. This is especially relevant in the context of the multiplication of peace process spaces beyond the UN process, as well as bilateral power-based and check book diplomacy approaches. It remains to be seen whether the recent $1bn grant provided by the KSA and UAE to the IRG through the Arab Monetary Fund represents a sustained shift in their engagement modality.

6.3. The Yemeni private sector

Several large corporations in Yemen have significant local footprints across the entire territory of Yemen. This horizontal footprint through local dealers and traders as well as vertical relationships from the local to traditional and provincial elites has given some private entities a significant leverage over the economy. The connectedness has allowed these corporations to remain in business and keep the economy alive during the years of conflict.

The leverage of the private sector builds from the fact that it is closely entwined with the prevailing realpolitik. There is a distinct and detailed knowledge base on the integrated fabric of business, political, and clan relationships in Yemen, and how they have evolved over the last century. The private sector is not fully independent of the political sphere, giving connected business actors the leverage to advance their interests or to broker political deals.

AA reportedly prefers to listen to local business actors rather than the international community. This suggests that on certain issues, the private sector may be better placed to conduct economic dialogue with AA than the international community. Recent progress towards resolution of the Safer oil tanker, which is anchored in an unstable condition in the Red Sea, was in part made as a result of private sector engagement with AA. It was also noted that AA demonstrates a capacity for learning, and a willingness to adapt its policies if presented with reasonable justifications that do not challenge its core ideological tenets.

7. Concluding observations: Opportunities for the peace processes

The report covered a period where Yemen has taken steps away from all-out war to a 'no war, no peace' situation, but its economy has become increasingly balkanized. The economy is moving beyond a mere bifurcation towards a trend of splintering into different fiefdoms controlled by different de-facto governing entities of PLC actors and AA. Economic interactions are embedded in a low trust environment shaped by long history of division and grievances between different entities. The escalation of economic warfare in the natural resources and banking sectors illustrate this point. The private sector faces increasingly higher costs of doing business, especially as all PLC parties and AA focus on the consolidation of revenue. But there is also a lot of pragmatism that reflects an ability of Yemeni stakeholders to adapt and 'get things done' despite a very complicated operational environment, and with a high degree of ingenuity.

7.1. Reshape current trends towards 'economic balkanization' into a more positive framework of co-ordinated economic regionalization

Current trends towards 'economic balkanization' are operating as a zero-sum game. There may be opportunities to transform this negative trend into a more positive framework that recognises and co-ordinates the devolution of economic power. From an economic standpoint, delegating taxation authority over certain economic activity would be nothing uncommon**,** including a tax on local economic activity. But there are also 'national' resources and taxes for which a certain sharing formula should be found. This includes for instance in the case of Yemen, the income from natural resources and from taxes or duties related to international trade. Getting a better understanding on what taxes can be devolved and what should be at national level, and what transparency measure are necessary for trust building and compliance, could shape a pathway away from 'economic balkanization' based on ad-hoc and opportunistic taxation, to systematized and harmonized taxes.

However, the benefit from such opportunities is predicated on an increased degree of trust. This is a kind of trust that builds on a pragmatic realization amongst all parties that managed coexistence is more beneficial to all then the continuation of warfare. A first step to get there is to **deconstruct the 'winner-takes-it-all' and 'warfighting' mentality.** There should also be a certain common prioritization by all de-facto authorities and international donors to invest revenue in health, social and education services and the reconstruction of critical economic infrastructure to ensure food security and expand economic opportunity. These efforts would aim on the one hand, to shift human resources from the security actors into other state services, and on the other hand to start building a relationship between authorities and the people.

7.2. Reset the international community's engagement on the economy

The international community's engagement in the economic domain in Yemen is framed by a narrow definition of 'the parties to the conflict' as embodied in UNSC resolution 2216. Its characterisation of the conflict being between two parties, one of whom is legitimate, and the other not, stands in contrast to the multiple actors that are involved in Yemen's economy, both internationally, regionally and at local levels.

UNSC resolution 2216 seeks the re-establishment of a status quo of a unified Yemen in territorial and governance terms as envisaged in 2015. This objective has proved unachievable to date even through military means. Local, regional and international actors appear war weary, especially as further insecurity in a major energy producing region is not in the interest of many countries – especially European countries – given a global context of radical uncertainty and other priorities, such as dealing with the war in Ukraine, global food security, pandemics or climate impacts. As perspectives evolve into the direction of negotiation and stabilization, rather than war, the framing of resolution 2216 presents an obstacle to conflict resolution, and especially so in the economic domain. AA and STC control two of Yemen's primary markets. It is not feasible to resolve current economic distortions and expanding economic opportunity without engaging with them.

With a growing international interest in and on-the-ground-tendency towards stabilization, international actors should review their own positions on engagement in the economic domain. Within a de facto economic system of increasing regional economic autonomies, international actors would benefit from engaging with all relevant economic actors, providing capacity development and policy support as appropriate, with a focus on enhancing co-ordination between them.

Enabling more direct engagement with AA and STC is also a strategy for preventing radicalisation. Opening a space to transform these political and military actors into capable governing entities would aim at improving the security and economic situation and public service delivery. As the 'hot' conflict appears to ebb away, such a transformation should also be in the interest of de-facto governing entities, even though it is clear that these actors would also need to demonstrate positive change, and step back from the use or threat of violence and coercion to advance their aims.

Operationally in the immediate term, resorting to private diplomacy could assist the transition from 'economic balkanization' to greater economic co-ordination. 'Private diplomacy' is an activity conducted by specialized mediation outfits with unique relationships with non-state actors. With respect to the disarming the economy of Yemen, private diplomacy actors should explore the trappings of a new economic future. This can occur though technical capacity building efforts for all actors and accompaniment for 'on the job' learning. While representatives of governments or international organizations are ill suited for these engagement, private diplomacy actors could lead the way, in connections with the UN-led process and the negotiations led by KSA.

7.3. Advance engagement on income sharing from natural resources

Finding compromise on the sharing of income from natural resources is a new frontier for disarming Yemen's economic warfare . Currently, AA and PLC are bound up in a negative, downward spiral where neither party benefits from oil and gas revenues. AA invokes their commitment to 'unity', emphasizing that income from natural resources should be shared because it is a national asset. In the absence of a solution, it uses coercive means to limit the export of oil and gas on which IRG financing is very dependent. On the PLC side, the IRG invokes its status of being 'internationally recognized' to not share income with AA, whilst Marib reportedly has the latitude to retain its revenues instead of sharing them with the Central Bank of Yemen (Aden).

To advance discussion on income sharing from natural resources, there is a need to expand understanding about existing sharing mechanisms, and their respective advantages and disadvantages for the case of Yemen. Issues around control and sharing of income are a recurrent feature of peace processes (see Box 4). For many years, the UN Mediation Support Standby Team maintains competences in this domain.

Fighting for the control and distribution of income from natural resources was at the heart of the war, in particular in relation to the battles for Marib, so it might be only too obvious that it is at the heart of any political settlement. Gaining clarity on the 'what' is being shared, and 'how' and 'when' and 'by whom' and 'to whom' will be an important exercise. A starting point could be an assessment of Yemen's future production possibilities in its oil and gas sectors (i.e. responding to the questions 'how much is left'). Designing agreement on income sharing in Yemen is a complex endeavour given the fault lines along politics, tribes and faith, but finding agreement on the sharing of income from natural resources might pave the way for finding agreement on governance given the importance of this income for covering the costs of Yemen's governance system, of course providing there is enough oil and gas left for the effort to be worthwhile.

Box 4: Lessons learned from incomes sharing from natural resources in peace processes[38]

Resource-sharing agreements can open up three different avenues for peace processes. First, income-sharing arrangements can resolve (one of) the key motivators of a conflict if they they can address disputes over the ownership and access to natural resources and their revenues. Second, income-sharing arrangements can provide the perspective of future gains that exceed the gains from the conflict economy, for example if the conflict prevents an efficient resource exploitation. This vision of a post-conflict future increases the costs of continued conflict. If successful, a thriving post-conflict economy can lower the incentives to return to conflict. Third, a clear regulation of resource wealth in the post-conflict state can prevent conflict parties from using resource revenues to re-mobilize.

There is "no single best way" to advance income sharing arrangements as part of a peace processes, but there are some lessons learned on how to approach them.

Timing: While resource provisions might seem less urgent than political or humanitarian provisions, it can be useful to negotiate them at the beginning – assuming that economic questions can be more easily resolved than identity or power-sharing questions. An early negotiation success on wealth-sharing can build confidence and provide an incentive to agree in other domains as well.

Depoliticize resource issues: Resource management and wealth sharing discussions can be advanced by framing them in technical terms. However, natural resources are never purely economic issue but can also have a significant identity and political components, as well as influencing what is affordable in terms of the governance structure of the state. So, while a separate technical negotiation on income sharing is possible, given the significance of income from natural resources, a link to the political process should be maintained.

Capacity building: Framing the discussion in technical terms comes with high demands for the capacity of the negotiating parties and mediating third parties. The conflict parties need similar levels of technical expertise as well as information on the available resource. For this, it can be helpful to bring in an independent expert for a detailed technical assessment.

Separation of ownership and wealth-sharing: In cases where the question of resource ownership is highly contested, it can be expedient to postpone this question while still negotiating wealth-sharing. Development agreements can be concluded which allow the exploration and exploitation of a resource until the question of ownership is resolved.

7.4. Develop scenarios for Yemen's future economy

Developing scenarios for Yemen's future economy could be a valuable starting point for overcoming current zero-sum mentalities.. Most Yemeni actors, whether conflict actors or private sector entities, are bound up in managing day-to-day challenges and do not necessarily have the mind-set to plan for the medium and long term. However, there are ongoing initiatives that a vision and scenario development processes could building on. AA has articulated an economic vision for 2030 and a private conglomerate, Hayel Sayed Anam group, is initiating a process of thinking about lasting exits to food insecurity in Yemen. Other efforts are led by the GoY Ministry of Planning and International Co-operations (MOPIC) and the Yemen Development Champions. The STC is also starting to think about its economic vision.

There is opportunity to develop a process design that sequences substantive inputs for scenario and vison building. This design must be inclusive of inputs from AA, the PLC, private sector actors (including large firms and SMEs) as well as technical experts relevant to specific issues. On the one hand such efforts take stock of the existing spectrum of views and materials, including those from the international community,[39] while developing 'realistic' *political* scenarios for the economy, including a spectrum of governance scenarios for the evolution of the Yemeni economy. Political realism can be infused into such vision building process by drawing primarily on approaches rooted in political economy rather than exclusively on economics.

Scenario building relates the de facto economic potential of Yemen to a system of governance that can ultimately sustain itself. All other options lock Yemen into long term aid dependence. Aligning congruence between Yemen's economic potential and its form of governance would be a critical strategic element for Yemen's stability, and a starting point could be the development of a transparent evidence base of scenarios for Yemen's economy. The vison building process in the 1990s for a post-Apartheid economy of South Africa might offer ideas for such scenario building in Yemen (see Box 5). Of course, this process of scenario building occurred when there was an acknowledged incoming government entity, and it involved far fewer players in comparison to Yemen. A key question for Yemen's peace process is when might it be appropriate to embark on a scenario building exercise? And who should be involved? What are the roles of the international community in these processes? What breadth of local ownership is necessary for an 'inclusive enough' vision on the economy?

Box 5: Economic scenarios for a post-*Apartheid* South Africa[40]

In the early 1990s, in a quiet mountain location in the Cape of South Africa, several prominent South Africans met to formulate economic scenarios. The question was how could a peaceful transition be accomplished, and especially, how could the society pay for the sorts of state policies that were likely to be needed to redress the economic inequalities resulting from apartheid? The discussions produced four scenarios:

- *Ostrich*: the white minority government would 'stick its head in the sand' and try to avoid a negotiated settlement, i.e. a continuation of the racism, violence, economic stagnation and international isolation of the 1980s.
- *Lame Duck:* there would be a prolonged transition with a constitutionally-weakened transitional government, and continuing economic decline, that would satisfy no-one.
- *Icarus:* a dominant, 'constitutionally-unconstrained' ANC-led government would emerge on a wave of popular support and seek, with good intentions, to deliver on its mandate, implementing a huge and unsustainable public spending programme – which would crash the economy.
- *Flight of the Flamingos:* the transition would be politically just, but economically pragmatic in the government's political-economic management, looking for steady institutional change, funded by gradual economic growth and improvement; there would be strict and consistent fiscal discipline, with clear messages of stability and confidence to investors and the marketplace generally.

The evident risks of *Icarus* made an impression on the economic leaders in the ANC, who realised that they would bear the political and economic cost for a crashed economy. With no formal agreement, *Flight of the Flamingos* became the effective policy of the incoming government. The question for Yemen is, if it is possible to arrive at a set of scenarios that are on the one hand grounded in real possibilities and potential political compromise.

7.5. Relationship between the UN's peace process tracks

Several opportunities arise for exploring linkages between the security, economic and political tracks of the formal UN-led peace processes under the UN Special Envoy. These might position the UN-led peace processes in a **more agenda-setting role with a more proactive shaping of propositions with all relevant parties**. With respect to a linkage between the security and economic track the following paragraphs develop a rationale for a proactive agenda setting process.

As dynamics for an all-out war appear to ebb, maintaining large military or militia formations will become an ever more difficult problem for the variety of conflict parties. The priority placed by the parties on salary payments reflects an interest to find a (short term) solution for this problem, also in order to maintain motivation and morale of fighters and contain discontent among the population.

To shape demobilization dynamics, focusing economic rehabilitation efforts on troop catchment areas as well as expanding entrepreneurial and training offers could offer a next step by providing positive incentives for returning to civilian life. Such an effort might be particularly relevant for armed actors based on voluntary recruitment patters. In the case of involuntary recruitment, economic incentives might not work, as fighters are restraint by threats to themselves or their families in the case of their departure from the armed actor.

The following three domains might offer prospects when more systematically connected in order to stimulate work across the security and economy tracks:

(1) Identification of the 20-30 most important critical economic infrastructure for specific economic sectors, including understanding their territorial dimensions (where they are, what territories they connect to).
(2) The security provisions necessary for keeping these critical economic infrastructure safe (so they can perform their functions) and what armed actor will be responsible for providing security services, and at what cost. These considerations might also 'non-physical' security service such as direct channels of communications to sources of security risk.
(3) The investment necessary for 'anticipated reconstruction' to improve the operation of critical economic infrastructure, and identification what actor can invest in and deliver such anticipated reconstruction in different sites.

Finding responses to these three areas of inquiry would require consultation with relevant actors across the entire territory of Yemen and especially with a range of private sector actors, from small players, to SMEs to large corporations. These efforts might also **nurture a 'web of economic truces' around critical economic infrastructures related to specific economic sectors**, such as for instance those that are important to enhance Yemen's food security.

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