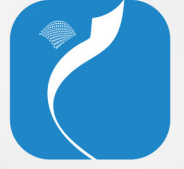


Position Evaluation
June 2024

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The Economic Escalation in Yemen: Consequences and Future Predictions

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The Economic Escalation in Yemen: Consequences and Future Predictions



Position Evaluation



June - 2024



We are a research institution concerned with studying Yemeni affairs and the regional and international influences on it. Through interpreting history, analysing the present, and predicting the future, in the aim of positive participating for better future of Yemen

Abstract

Several local and international factors, including events, have laid the foundation for the Central Bank of Yemen to make a series of significant and decisive decisions regarding the country's financial and banking sector. Among these factors is the continued implementation of new measures by the Houthis, targeting the finances of the legitimate, internationally recognized government, as well as the aforementioned financial and banking sectors. These measures have been particularly frequent since the signing of the so-called "Armistice Agreement" on April 2, 2022. The Houthis announced the issuance of a Yemeni 100-riyal coin, which was to enter circulation starting March 31, 2024¹. Additional geopolitical and security factors include the local classification of the Houthis as a "terrorist group" in October 2022 and the United States' decision to also designate them as a "terrorist group" following the events in the Red Sea in mid-February 2024. This U.S. designation comes after President Joe Biden's administration had previously removed the Houthis from the terrorist list in February 2021^{3,4,5}.

1. The Houthi militia announces the issuance of a 100-riyal coin, belqees.net, on: 3/30/2024, available at the following link: <https://shorturl.at/5ox65>

2. The National Defense Council classifies the Houthi militia as a terrorist organization and warns against dealing with it, Presidency of the Council of Ministers, on: 10/22/2022, available at the following link: <https://pmo-ye.net/post/3495>

3. Terrorist Designation of the Houthis, US Department of State, dated: 1/17/2024, available at the following link: <https://www.state.gov/terrorist-designation-of-the-houthis/>

4. Revocation of the Terrorist Designations of Ansarallah, U.S. Department of State, on: 2/12/2021, available at the following link: <https://www.state.gov/revocation-of-the-terrorist-designs-of-ansarallah/>

5. Washington: The classification of the Houthis as a "terrorist organization" comes into effect, Anadolu Agency, on: 2/17/2024, available at the following link: <https://shorturl.at/swzRh>

This paper aims to present an overview of the decisions made by the Central Bank of Yemen and the measures enacted by the Houthis.

It analyzes the factors contributing to the escalation in the economic and financial sectors and anticipates possible future developments and their broader impact on the economic situation.

The Path Toward Fiscal and Monetary Conflict

Economic issues have played a pivotal role in the Yemeni conflict. The Houthi group exploited the legitimate government's decision to implement economic reforms and lift support for oil derivatives, using it to obscure the coup they carried out at the end of 2014. This coup enabled them to extend their control over state institutions and seize economic resources meant for the government. The Houthis mobilized thousands of their fighters under the pretense of demonstrating against the removal of support for oil derivatives and calling for the government's overthrow⁶, ultimately leading to their invasion of the capital and subsequent control of large parts of the country.

The Central Bank continued to manage financial and monetary affairs from Sana'a, under the leadership of Governor Muhammad Awad, amidst an economic truce that ensured the flow of resources to the bank and its commitment to pay employees' salaries across all governorates. However, the legitimate government accused the Houthis of monopolizing financial resources and channeling them into their military operations, spending approximately \$100 million per month, according to government statements.

6. See: The Houthis protest in Sana'a to demand the overthrow of the government, France 24, on: 8/18/2014, available at the following link: <https://rb.gy/0tz9i0>

The government also accused the Houthis of depleting cash reserves. As a result, in August 2016, the legitimate government decided to cease dealing with the Central Bank in Sana'a and to stop supplying it with financial revenues⁷. That same month, the Central Bank announced the suspension of salary payments to public sector employees due to a lack of liquidity, exacerbated by halted oil exports and declining economic output. The Yemeni riyal's value then began to fall against the dollar, and the government rejected the bank's request to print more money⁸.

On September 18, 2016, former president Abd Rabbuh Mansour Hadi issued a Republican Decree restructuring the board of directors of the Central Bank and relocating its headquarters and operations center to the temporary capital, Aden⁹. The Houthis described this move as being influenced by the United States, with the group's leader urging citizens to donate in support of the Central Bank in Sana'a¹⁰. Following the transfer, the bank encountered technical and operational challenges, particularly from 2018 to 2019, due to the concentration of its human resources and technical capabilities in Sana'a.

7. The Yemeni Central Bank ... an economic battle against the Houthis, Al-Jazeera, on: 8/23/2016, available at the following link: <https://2u.pw/nbTumR0Q>

8. Yemeni Economic Bulletin: The war for monetary control is entering a dangerous new phase, Sana'a Center for Strategic Studies, on: 1/21/2020, available at the following link: <https://sanaacenter.org/ar/publications-all/analysis-ar/9500>

9. Republican decision regarding the restructuring of the Board of Directors of the Central Bank of Yemen and the transfer of its headquarters, Saba (official) Yemeni News Agency, on: 9/18/2016, available at the following link: <https://www.sabanew.net/story/ar/9118>

10. The leader of the Houthis calls on Yemenis to donate to the Central Bank and opposes its transfer, Al-Araby Al-Jadeed, on: 9/20/2016, available at the following link: <https://2u.pw/dvZWHVyu>

This was especially problematic in the banking supervision sector and was compounded by conflicts of authority between various government agencies.

These issues significantly impacted the Central Bank's management of the financial sector, leading to multiple restructurings of the bank's Presidential Leadership Council. Additionally, problems arose in managing the Saudi deposit, which hampered economic reform efforts and exacerbated the currency division and the depreciation of the riyal.

Despite these challenges, the Central Bank gradually managed to overcome many obstacles. However, the issue of weak government revenues and the government's reliance on overdrafts — borrowing from the Central Bank — remains a significant hurdle to economic stability. This instability is closely tied to the Houthis' control over resources and revenue collection within their territories, along with their recent targeting of government revenue sources.

Printing banknotes was one of the most significant decisions made by the Central Bank to address the liquidity crisis. Initially, the bank printed 600 billion Yemeni riyals¹¹. In 2014, local liquidity stood at 3,106 billion Yemeni riyals¹², increasing to 3,922 billion Yemeni riyals by 2020¹³. As the legitimate government continued to borrow from the Central Bank, the value of the riyal deteriorated further, particularly since a significant portion of government resources went to the Houthis.

11. See: The Governor of the Central Bank of Yemen reveals the volume of money printed in Russia, Aden Al-Ghad, on: 10/24/2017, available at the following link: <https://www.adengad.net/news/284054>

12. Central Bank of Yemen, Annual Report 2014.

13. Central Bank of Yemen, Annual Report 2020.

The legitimate government used newly printed money to pay salaries and wages, including those of certain nationwide parties.

In December 2019, through their control of the Central Bank branch in Sana'a, the Houthis issued a decision banning the use of newly printed money. They withdrew these new banknotes from circulation and approved the use of damaged currency¹⁴, claiming that the legitimate government was flooding the market with new banknotes and thereby contributing to the riyal's depreciation. The Houthis announced the introduction of the electronic riyal for payments — a move rejected by the Central Bank in Aden, which warned banks and exchange companies against dealing with it¹⁵. The Houthis also introduced a voucher system for obtaining in-kind goods. However, they failed to implement both the electronic riyal and the voucher system effectively, and they did not resolve the liquidity shortage¹⁶.

In October 2020, the Central Bank attempted to address price disparities by injecting larger-sized 1,000-riyal notes into the market nationwide¹⁷. However, this decision did not significantly impact the price differences. In December 2022, the Houthis responded by prohibiting transactions with banks licensed by the Central Bank in Aden unless they also obtained a license from the Houthis.

14. The Houthis prevent trading in the new currency and hold those who possess it legally accountable, Al Jazeera, on: 12/25/2019, available at the following link: <https://bitly.cx/Bdjd>

15. Central Bank: Not accepting the national currency is a legal violation, suhail.net, on: 12/23/2019, available at the following link: <https://suhail.net/nprint.php?sid=9750>

16. Yemeni Economic Bulletin: The war for monetary control is entering a dangerous new phase, Sana'a Center for Strategic Studies, on: 1/21/2020, available at the following link: <https://sanaacenter.org/ar/publications-all/analysis-ar/9500>.

17. Statement about addressing price distortions in the national currency, Central Bank of Yemen, on: 7/29/2017, available at the following link: <https://english.cby-ye.com/news/128>.

They also issued directives preventing merchants from participating in foreign currency auctions organized by the Central Bank for importing goods into Houthi-controlled areas, requiring participation through bank branches licensed by the Houthis for imports to government-controlled areas. Additionally, the Houthis instructed international organizations not to engage with banks lacking their approval¹⁸.

The Central Bank in Aden initiated procedures to establish a unified remittance network to replace private remittance networks, placing it under the Central Bank's supervision¹⁹. The founding meeting of this network, named Unified Network for Money (UNMoney), was announced in October 2022²⁰ as a Yemeni joint stock company. The Central Bank issued a circular in January 2023 mandating registration on and linkage to the network. Then, that same month, the Central Bank in Sana'a prohibited registration or connection to the UNMoney network. Moreover, the Houthis reiterated their December 2022 decision, banning dealings with banks licensed by the Central Bank in Aden without their authorization, preventing merchants from participating in Central Bank-organized foreign currency auctions for Houthi-controlled area imports, and requiring transactions through their licensed branches for imports to government-controlled areas. The Houthis also directed international organizations to avoid dealings with unlicensed banks²¹.

18. Report of the committee of UN experts specializing in Yemen in 2023.

19. The Central Bank approves the start of procedures for establishing a unified remittance network, Central Bank of Yemen, on: 10/11/2020, available at the following link: <https://cby-ye.com/news/58>.

20. Announcement of the founding meeting of the Unified Money Network Company in Aden, under the supervision of the Central Bank, the Unified Money Network, on: 10/3/2022, available at the following link: <https://www.unmoneye.com/ar/news/13>.

21. Report of the committee of UN experts specializing in Yemen in 2023.

The conflict surrounding the unified remittance network resurfaced in February 2024 when the Central Bank issued a circular mandating that exchange companies connect to the unified network and conduct internal transfers through it. The Houthis rejected this decision, escalating the situation. In response, the Central Bank suspended a group of banks for violating its instructions and following Houthi directives to cease dealing with exchange companies. The Houthis countered by suspending two exchange companies operating in government-controlled areas and linking to leaders within the unified network.

Both sides retracted their decisions: The Houthis lifted the suspension of the exchange companies, and the Central Bank resumed dealings with the banks, announcing its compliance with its instructions.

Although there were reports of joint understandings due to mediations, no official statement was released, and the Central Bank denied any deals or mediations.

In addition, the Houthis issued a “prohibition of usurious transactions” law, causing confusion in the banking sector, compromising depositor rights, reducing bank profits and threatening their financial stability. The situation further intensified with the Houthis’ announcement of minting a 100-riyal coin at the end of March 2024. The Central Bank rejected this move, deeming the newly minted currency counterfeit and illegal; the bank considered it a dangerous and unacceptable development²².

22. Press release from the Central Bank of Yemen (document), Central Bank of Yemen, dated: 3/30/2024, available at the following link: <https://cby-ye.com/news/657>

At the beginning of April 2024, the Central Bank decided to transfer the main banking centers to the temporary capital, Aden, setting a two-month deadline for completion²³. After this deadline, the Central Bank halted transactions with six prominent banks operating in the Republic: Tadhamon Bank, Bank of Yemen and Kuwait, Shamil Bank of Yemen and Bahrain, Al-Amal Microfinance Bank, Al-Kuraimi Islamic Microfinance Bank and International Bank of Yemen. These banks were allowed to continue serving customers²⁴, but there was no clarification on whether other banks, such as the Construction and Development Bank and the Commercial Bank of Yemen, had signed agreements to implement the Central Bank's decisions.

The Central Bank also announced that citizens and financial institutions should replace banknotes issued before 2016 of all denominations, granting a two-month period for this transition²⁵. In reaction, the Houthis announced they would stop dealing with 13 banks operating in government-controlled areas and prohibited individuals and institutions from engaging with them²⁶.

23. Decision of the Governor of the Central Bank regarding the transfer of the main centers of banks to Aden (document), Central Bank of Yemen, on: 4/2/2024, available at the following link: <https://cby-ye.com/news/658>

24. Decision of the Governor of the Central Bank regarding stopping dealing with several banks and banks (document), Central Bank of Yemen, on: 5/30/2024, available at the following link: <https://cby-ye.com/news/691>

25. Important announcement, Central Bank of Yemen, on: 5/30/2024 AD, available at the following link: <https://cby-ye.com/news/692>

26. The Houthis in Yemen announce a ban on dealing with 13 banks, Xinhua Agency, on: 6/1/2024, available at the following link: <https://arabic.news.cn/20240601/67da86fed1dc4168b12dd767a670bfc6/c.html>

This decision affected two government banks, the National Bank of Yemen and the Agricultural Cooperative Credit Bank, as well as several emerging banks: Al-Qutaybi Islamic Microfinance Bank, Al-Busiri Microfinance Bank, Aden Islamic Microfinance Bank, Aden First Islamic Bank, Al-Shamool Bank for Islamic Microfinance, Al-Salam Capital Bank for Islamic Microfinance, Tamkeen Microfinance Bank, Al-Inma Bank for Microfinance, Al-Sharq Al-Yemeni Finance Bank Al-Asghar Al-Islami, Hadhramaut Commercial Bank and Bin Doul Islamic Microfinance Bank. The Houthis also announced their own decision to replace new banknotes with old ones, compensating for any differences in exchange value.

On May 23, 2024, the Central Bank issued a decision restricting foreign remittance activities to qualified banks and exchange companies, which must obtain approval from the Central Bank to operate in this capacity. According to the decision, these entities are required to deliver remittances in the currency of origin unless the recipient specifies otherwise.

It's worth noting that the Central Bank's decisions are closely linked to those made by the legitimate government, aimed at regaining control over resources and cutting off funding sources for the Houthis. For example, Cabinet Resolution No. 75 of 2018 regulates the import process, and recent decisions involve transferring the main centers of telecommunications companies to Aden²⁷, among other measures.

27. The Ministry of Communications calls on mobile phone companies to quickly move their headquarters to Aden, belqees.net, on: 6/8/2024, available at the following link: <https://shorturl.at/eW30d>

The Houthis have implemented various measures with significant economic ramifications on government finances²⁸, consolidating their grip on financial resources. Here, we'll focus on tracking developments in monetary and banking procedures.

Reasons for the Escalation and Local and International Positions

The recent escalation was triggered by the Houthis' decision to mint the Yemeni 100-riyal coin, following the resolution of the crisis regarding bank suspensions due to the unified network. This decision prompted a strong response from the Central Bank in Aden, leading to announcements regarding the transfer of banks and the replacement of old banknotes, as previously outlined.

In response to the coinage decision, the embassies of the United States — including the U.S. embassy in Yemen — the European Union, Britain and France condemned the move, citing its exacerbation of economic division in Yemen and its contradiction with the legitimate government's counterterrorism efforts²⁹. The Central Bank's actions and decisions received official backing from the Presidential Leadership Council³⁰, which viewed them as crucial steps to address monetary distortions, combat inflation, bolster the national currency and safeguard depositors' funds.

28. For more, see: Al Mokha Center for Strategic Studies, Third Annual Strategic Report (2023).

29. The embassies of the United States, the European Union, Britain and France in Yemen condemn the Houthis' issuance of counterfeit currency, Kuwait News Agency (KUNA), on: 4/5/2024, available at the following link: <https://www.kuna.net.kw/ArticleDetails.aspx?id=3144329&language=ar>

30. The Presidential Leadership Council confirms its full support for the decisions of the Central Bank, the official Yemeni News Agency (Saba), on: 5/31/2024, available at the following link: <https://www.sabanew.net/story/ar/111986>

The Central Bank's stance asserts that the solution to the liquidity problem lies in circulating legal banknotes it issues rather than minting counterfeit currency. This rationale underpinned the decision to withdraw old banknotes. Additionally, the classification of the Houthi group as a "terrorist group" served as a pivotal factor prompting the decision to transfer banks' main centers to the capital, Aden. This relocation enables the bank to oversee nationwide banking operations and reduces the Houthis' influence and pressure on financial institutions. These measures align with the core responsibilities and competencies of the Central Bank.

The decisions made by the Central Bank sparked controversy and elicited various reactions, prompting counter-decisions from the Houthis. However, these actions were not entirely unprecedented. Previously, Houthi monetary authorities had ceased dealing with a group of banks they deemed unlicensed and had also prohibited the circulation of new banknotes. However, these decisions from the Houthis didn't garner much attention or support. The Houthis often accuse Saudi Arabia and the United States of being behind such decisions, especially considering their stance on the Gaza conflict. While these accusations have been repeatedly made over the years, the Houthis are currently attempting to leverage the Gaza conflict to justify their positions and criticize the actions taken by the Central Bank and the legitimate government.

However, tracing the decision-making processes reveals no direct link between the Gaza conflict, the Houthis' stance on it, and the recent decisions of the Central Bank.

Despite this, there has been a noticeable shift in the international community's attitude toward the Houthis in recent times, unlike in previous years. The Governor of the Central Bank has noted that international pressure has hindered decisive actions against the Houthis. For instance, despite the government's accusations that the Houthis seized around \$58 million from a bank branch in Hodeida, collected from import fees for oil derivatives under the Stockholm Agreement, the international community did not react to this incident.

Despite the Houthis' accusations against Saudi Arabia regarding the decisions of the Central Bank, they did not announce the suspension of ongoing peace consultations with them. Similarly, Saudi Arabia did not issue a clear statement supporting the recent economic measures of the legitimate government. Instead, the Saudi Defense Minister emphasized peace efforts and the necessity of progress on the road map to resolve the crisis, when he met with Presidential Leadership Council (PLC) Chairman Dr. Rashad Al-Alimi in early June 2024³¹.

At the local level, the Central Bank's decision³² to implement the unified network has provoked dissatisfaction among some exchange companies and institutions in the southern region. The Southern Money Changers Syndicate expressed support for the Central Bank's decisions but objected to the unified network, alleging Houthi infiltration and advocating for the establishment of an additional network involving more exchange companies.

31 .The Saudi Defense Minister discusses with Al-Alimi reaching a comprehensive political solution in Yemen, Al-Sharq News, on: 6/6/2024, available at the following link: <https://shorturl.at/8NdNe>

32. A statement by the Southern Money Changers Syndicate regarding the unified remittance network, Samaa Al Watan News, available at the following link: <https://rb.gy/7m4kk1>

The objection seems rooted in the perception that the Central Bank's exclusive adoption of the unified network could undermine the interests of existing networks and companies not involved in it.

Meanwhile, the Yemeni Banks Association, headquartered in Sana'a, appealed to the Central Bank to reconsider the decision to relocate banks' main centers to Aden, citing concerns about the impact on the banks' stability³³ due to the complicated work environment. Additionally, there are apprehensions regarding the security and political situation in Aden, where the Yemeni Ministry of Interior does not have complete control, and the Southern Transitional Council (STC), currently part of the government coalition, maintains military forces not under the command of the Ministries of Interior and Defense. Moreover, there are calls for the secession of the south from the Republic of Yemen.

To address these concerns, STC President and PLC Vice President Aidarous Al-Zubaidi visited the Central Bank primarily to convey positive messages. He reiterated the PLC's support for the Central Bank and emphasized the importance of providing security and support for banks, exchange companies and investors in Aden and all liberated governorates³⁴.

33. A source in the Yemeni Banks Association appeals to the Aden Central Bank to retract the decision to oblige banks to move their main centers to Aden Governorate, Yemeni Banks Association, available at the following link: <https://rb.gy/5p4iyx>

34. Major General Al-Zubaidi inspects the progress of work at the Central Bank and renews the Presidential Leadership Council's support for its decisions, the official Yemeni News Agency (Saba), on: 6/5/2024, available at the following link: <https://www.sabanew.net/viewstory/112247>

The Houthis have announced the replacement of banknotes at customs centers they established at regional and controlled borders, compensating for the difference between the two currencies³⁵. This action underscores their continued division of the economy and reliance on black-market mechanisms instead of the formal financial and banking system.

Banks are facing challenging circumstances due to conflicting decisions from both the Central Bank and the Houthis. The Houthis have forcibly prevented banks from relocating their centers to Aden, and technical issues hinder transferring staff to government-controlled areas. The impact is particularly severe for the six banks punished by the Central Bank, given their nationwide operations. The Houthis' decision indirectly penalizes these banks by prohibiting dealings with institutions not licensed by the Houthi monetary authorities in Sana'a. While banks have not issued public statements, some have reassured customers about their continued receipt of foreign remittances, amidst rumors suggesting otherwise following the Central Bank's decision on foreign remittances. Additionally, MoneyGram has complied with the Central Bank's directives, requiring agents to obtain approval from the Central Bank in Aden to operate through its money transfer network³⁶.

Due to the absence of opinion polls, it's difficult to gauge public sentiment regarding recent decisions. However, there is a popular demand to end economic division in Yemen.

35. The Central Bank of Yemen issues an important statement, Saba News Agency (controlled by the Houthi group), on: 5/31/2024, available at the following link: <https://www.saba.ye/ar/news3335788.htm>

36. Belqees.net, available at the following link: <https://www.facebook.com/share/p/gFeF1BS7NUFvqHrT/>

Possible Repercussions and Scenarios

The Central Bank's decisions have stirred up significant controversy and raised expectations regarding their outcomes and repercussions, particularly due to their timing and the bank's refusal to retract or negotiate them.

We'll explore the implications and potential scenarios in two parts:

- 1. The withdrawal of currency, and**
- 2. The transfer of bank departments**

It is anticipated that the Central Bank will issue a decision to cease dealing with banknotes issued before 2016 after the expiration of the specified two-month deadline. Consequently, these banknotes will no longer be accepted for circulation or storage by various financial institutions and individuals. However, this decision does not entail the elimination of the currency in the north, where it will continue to circulate due to the Houthis' influence.

Nonetheless, the liquidity crisis is expected to worsen, especially if tighter measures are implemented on external transfers to Houthi-controlled areas. This decision will likely prompt citizens, capital holders, money changers and banks to dispose of part of the old currency they possess, despite its potential damage. This could lead to a surge in the volume of liquidity initially, but it may also impact the exchange rate.

Although the Houthis' attempt to alleviate the liquidity problem by minting coins proved unsuccessful, the exacerbated liquidity crisis may compel them to resort to similar measures for different groups.

Coin minting offers the Houthis an additional and relatively easy source of income.

However, if the Central Bank imposes further restrictions on foreign transfers and banks, the Houthis may face difficulties in addressing the scarcity of hard currencies. Despite banning new banknotes as unauthorized and illegal, the Houthis have attempted multiple times to counterfeit currency and smuggle it into the country to mitigate the liquidity crisis³⁷.

Regarding the transfer of the main banks' centers and their operations departments to Aden, expectations suggest that conflicting decisions issued by the Central Bank and the Houthi authorities will likely result in the near-total separation of the banks. This analysis can be informed by comparing it to the situation with the Cooperative and Agricultural Credit Bank (CAC Bank), which was ordered to transfer its headquarters to Aden in early 2019.

The bank faced dismissal and Houthi-imposed sanctions, including restrictions on its financial services, such as the "CAC Hawala" service in 2021. The Houthis also issued a directive to cease dealing with certain banks, including CAC Bank. For instance, the Social Fund for Development, based in Sana'a, refused to work with CAC Bank in Aden for the 2022 unconditional cash-transfer program due to the sanctions and the financier's commitment, specifically UNICEF.

37. Report of the Committee of Experts on Yemen, 2022-2023. <https://rb.gy/li9hw1>

Although the bank participated in a tender in both Sana'a and Aden as a single entity, the Fund deemed this a violation of tender procedures. This scenario highlights the effectiveness of Houthi pressure on international organizations and bodies to avoid dealing with banks over the past years, particularly with the main organizations' centers located in Sana'a, and underscores the damage inflicted on banks due to this division.

The procedures this time differ somewhat as they are issued by the Central Bank, which has both local and international support. International recognition of the bank's decisions is crucial for the success of these measures.

The below descriptions, and table following them, lay out some potential expected future scenarios:

1- The first scenario suggests that the current situation will persist, meaning banks will be unable to relocate their centers to Aden. This could lead to isolation and stricter penalties. However, this scenario is unlikely unless it is part of a new joint settlement and understanding. Any economic agreements are often tied to political agreements or the final settlement of the conflict. This would require the Houthis to relinquish forcible control of state institutions, stop targeting the economy, refrain from counterfeiting currency and cease collecting revenues for their benefit.

In any case, a comprehensive settlement will not produce an ideal situation for the return of the state and its institutions, particularly with the military power remaining in the hands of the Houthis. However, it can provide common and acceptable points of understanding based on established references.

2- The second scenario involves the separation of the banks' main departments and their control and accounting systems, while the institution remains formally unified. The Central Bank would require these joint banks' operational data to be shared with branches in Houthi-controlled areas.

Transferring their activities and international dealings to the main or regional administration in Aden would lead to the isolation of banks in Sana'a. Consequently, banks would face losses and technical, accounting and administrative challenges. This scenario reflects the impact of conflicting policies, with the possibility of the Houthis imposing sanctions on banks that follow this step. However, the Houthis would struggle to find alternatives for the banks' international transactions, potentially isolating the banking system in Houthi-controlled areas in a manner similar to the Iranian banking and financial system, which is globally isolated.

This is compounded by shifting international attitudes toward the Houthis and their recent arrests and persecution of international organization staff in Sana'a³⁸.

38. The Houthis arrest dozens of UN and relief employees, Al-Sharq Al-Awsat newspaper, 6/7/2024, available at the following link: <https://rb.gy/aw3qhy>

The presence of relief and international organizations in Sana'a has previously strengthened the Houthis to oppose some government decisions.

3- The third scenario involves the possibility of establishing a limited coordination room for the Central Bank and its branch in Sana'a to manage bank supervision, aiming to address issues related to data monitoring and anti-terrorism financing.

However, this particular scenario is unlikely for several reasons: The classification of the Houthis as a "terrorist group," both locally and regionally, makes it unacceptable to have their representatives involved in monitoring banking and financial activities. Additionally, any understanding in this regard would require a comprehensive settlement and resolution of the legal status of the Sana'a branch. This scenario could also lead to the resignations of the current Central Bank Board of Directors.

4- The fourth scenario involves transferring banking centers and operations to Aden. This scenario faces significant opposition from the Houthis, who may seize the banks' assets and properties, attack bank staff, restrict their movements and turn the banks' situation into one like that of CAC Bank. However, the private ownership of banks could lead to different handling mechanisms compared to the government-owned CAC Bank. The Houthis have previously temporarily closed some banks and assaulted their staff³⁹.

39. Closing of the largest banks in Sana'a after the Houthis kidnapped its employees, Al Arabiya, on: 11/2/2019, available at the following link: <https://rb.gy/hqn179>

5- The final scenario considers the possibility of continued escalation in the economic realm, particularly concerning the financial sector, communications and import mechanisms. This could lead to the collapse of the current truce and a return to military escalation. While this option seems unlikely in the short term, it becomes more plausible in the medium term, especially if the understanding between Saudi Arabia and the Houthis fail.

In conclusion, given the slim chances of achieving a comprehensive settlement and the Houthis' refusal to relinquish control over state institutions or reverse the coup against legal and constitutional references and the outcomes of the dialogue conference, escalation is inevitable. The government is likely to use all available means, including the economic file, to counter the Houthis. The Houthis have frequently used the economic situation to stabilize their coup and financially strangle the government.

Table: Five Potential Scenarios for Implementing the Decision to Transfer the Main Centers of Banks from Sana'a to Aden:

| Scenario | Methods | Effects and Risks | Degree of Probability |
|--|--|--|--|
| The current situation of banks remains unchanged | Banks are maintaining their status and not relocating their operations centers | Local banks and government institutions are still refraining from engaging with these banks, leading to their isolation and subjecting them to new severe penalties imposed by the Central Bank | The situation remains weak due to the failure to reach a new settlement |
| Separating the main departments of the banks | Establishing primary or regional departments in Sana'a and Aden and separating control and data systems | Transforming banks in Sana'a into isolated entities, with key activities managed from main departments in Aden, especially regarding external communications. This separation leads to technical and administrative issues, double losses and hindered accounting operations, exposing banks to Houthi sanctions | In the medium term, the Houthis' countermeasures will likely force the banks' decision to become a reality |
| Settlement and joint coordination | Establishing a joint unit for bank supervision, based in Aden or abroad | Ending the division of monetary authorities and the resignation of the current bank board of directors | Weak prospects in the short and medium term |
| Transferring major centers | Relocating banking centers to the temporary capital of Aden without maintaining any centers in Sana'a | Banks facing potential Houthi sanctions, including asset confiscation, seizure and imprisonment of bank employees and cadres | Weak prospects |
| The resurgence of military conflict | Heightened tensions in the financial sector, import processes and other economic sectors, potentially sparking renewed warfare | The situation hinges on the results of military confrontations, where a return to war signifies increased polarization and economic downturn | Weak in the short term, with a moderate likelihood in the medium term |

Repercussions on the Government's Economic Performance

The economic performance of the legitimate government has faced significant challenges over the past two years due to Houthi actions in the economic sector. The government lost vital revenue streams from oil exports, taxes and customs on imports, as a large portion was redirected to the Hodeida port, controlled by the Houthis since the armistice agreement in April 2022. Beyond just resource collection, the Houthis impeded the circulation of banknotes in their territories, exacerbating inflationary pressures in government-controlled areas.

They also halted dealing with many Central Bank-licensed banks and controlled a substantial number of hard currencies for speculative purposes, profiting from expatriate remittances through an artificially fixed exchange rate. This situation widened the government deficit and led to continuous inflationary pressures.

To counteract these challenges, the government needed to respond to the Houthis across various economic sectors, including banking and finance, under the relatively stable conditions in Aden. With renewed cooperation with international institutions and the initiation of legislative reforms to introduce new financial services, like the International Bank Account Number (IBAN)⁴⁰ system, addressing the monetary division and market price distortions became crucial.

40. The Central Bank of Yemen begins procedures for activating the International Bank Account Number (IBAN) amid banking praise for its advantages, Central Bank of Yemen, on: 4/28/2024, available at the following link: <https://cby-ye.com/news/671>

Additionally, confronting Houthi measures that obstructed banking reforms and supervision was essential for improving the sector's efficiency.

However, the government won't see immediate benefits from these decisions; in fact, things may worsen initially. Aligned with decisions made in other economic sectors, these choices hold potential for medium- and long-term governmental improvement. They aim to curtail Houthi control over critical resources and cut off the group's funding sources for military operations.

The government struggles with a severe deficit in the state's general budget, stemming from declining revenues. The government's debt to the Central Bank soared to 7,642.2 billion riyals in March 2024⁴¹. Without Saudi Arabia's intervention and financial support for the general budget, the government would have teetered on the brink of bankruptcy, unable to meet salary obligations⁴².

Amidst the challenges facing the government, the electricity sector experiences heightened difficulties during the summer. Despite constituting of about 30% of government spending⁴³, it relies heavily on purchased energy and operates with notably low efficiency. With oil exports still not restored, the legitimate government's ability to meet citizen expectations and fulfill obligations remains under threat, particularly given the limited tax base in government-controlled areas.

41. Central Bank of Yemen, Monetary and Financial Developments Bulletin, March 2024.

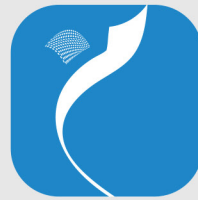
42. Sana'a Center for Strategic Studies, Challenges to Developing Public Revenue Sources in Yemen, December 2023.

43. See: Prime Minister Ahmed bin Mubarak's statements to Asharq Al-Awsat newspaper, available at the following link: <https://n9.cl/1dg5yK>

As popular discontent grows due to the depreciation of the riyal in government-held regions, the decision to confront the Houthis may become critical for the legitimate government before protests escalate and economic failures undermine resistance to the Houthi coup.

The ultimate outcome of the economic escalation remains uncertain, whether it leads to a parallel military escalation or applies pressure on the Houthis to engage in serious negotiations for a comprehensive settlement. Yet This shift represents a departure from the current state of stalemate, moving beyond the state of neither war nor peace, amid escalating humanitarian crises and rising poverty levels.

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