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**by**

**THE GOVERNMENT OF YEMEN**

## NOTE

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**Republic of Yemen  
Ministry of Planning  
and Development**

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**Action Program for the Development of the  
Republic of Yemen 2001-2010**

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## GLOSSARY

NGOs	= NON GOVERNMENTAL ORGANIZATIONS
UNDP	= UNITED NATIONS DEVELOPMENT PROGRAM
WB	= WORLD BANK
GDP	= GROSS DOMESTIC PRODUCT
EFARP	= ECONOMIC, FINANCIAL, ADMINISTRATIVE REFORM PROGRAM
FFYP	= FIRST- FIVE YEAR PLAN
SFYP	= SECOND FIVE- YEAR PLAN
LNG	= LIQUEFIED NATURAL GAS
PEC	= PUBLIC ELECTRICITY CORPORATION
IDA	= INTERNATIONAL DEVELOPMENT AGENCY
CBY	= CENTRAL BANK OF YEMEN
NBY	= NATIONAL BANK OF YEMEN
LIBOR	= LONDON INTER BANKING OFFICIAL RATE
YBRD	= YEMEN BANK FOR RECONSTRUCTION AND DEVELOPMENT
CPI	= CONSUMER PRICE INDEX
IMF	= INTERNATIONAL MONETARY FUND
US\$	= UNITED STATE'S DOLLAR
YRIs	= YEMENI RIALs
ACT	= ADEN CONTAINER TERMINAL
GIA	= GENERAL INVESTMENT AUTHORITY
FDI	= FOREIGN DIRECT INVESTMENT
FIAS	= FOREIGN INVESTMENT ADVISORY SERVICES
GER	= GROSS ENROLLMENT RATIOS
DHS	= DEMOGRAPHIC HEALTH SURVEY
ODA	= OVERSEAS DEVELOPMENT ASSISTANCE
SSN	= SOCIAL SAFETY NET
SBAP	= STAND -BY-ARRANGEMENT PROGRAM
SFD	= SOCIAL FUND FOR DEVELOPMENT
GNP	= GROSS NATIONAL PRODUCT
PGC	= PEOPLE'S GENERAL CONFERENCE
BOT	= BUILD- OWN-TRANSFER
YESC	= YEMEN EXPORT SUPREME COUNCIL
ESCA	= ECONOMIC AND SOCIAL COMMISSION FOR WEST ASIA
SDR	= SPECIAL DRAWING RIGHT
BPD	= BARRELS PER DAY
NCSSN	= NATIONAL COMMITTEE FOR SOCIAL SAFETY NET
CSO	= CENTRAL STATISTICS ORGANIZATION
NAPPE	= NATIONAL ACTION PLAN FOR POVERTY ERADICATION
PSDs	= PROGRAM SUPPORT DOCUMENTS
GOY	= GOVERNMENT OF YEMEN

## EXECUTIVE SUMMARY

### I. INTRODUCTION

The Republic of Yemen is one of the least developed countries having population about 18 million in 2000. There are major internal and external events that caused the economic and the social situation to suffer great shocks in the beginning of the 1990's. After the reunification of the two parts (South & North) in May 1990, the Republic of Yemen suffered a series of extraordinary circumstances that complicated the task of economic performance. Those circumstances included: (a) the Gulf War of 1990-1991 resulting in the expulsion of about one million Yemeni expatriate workers from the Gulf States, whose remittances had contributed significantly to the country's foreign exchange revenues (estimated yearly more than one billion dollars); (b) an interruption of external financial assistance from the Gulf States and other bilateral donors; (c) the disruption of regional trade relations, particularly the closure of borders to Yemenis export markets.

These external shocks and the resulting economic hardships during 1990-1994 were followed by internal conflict of 1994. By the end of this militant conflict, the country's economy seemed to lie in ruins as it was burdened with tremendous challenges: large fiscal deficits, a heavily indebted public sector, sharply accelerating inflation, a rapidly depreciating local currency, repressed international trade, large-scale unemployment, inadequate human resources and increasing debt arrears, as well as declining confidence in the economy in general.

### II. GOVERNMENT'S RESPOND

The Government announced its own economic reform programme in late 1994 in order to respond to the country's deteriorating economic situation. More formally, a Five-Year Programme of comprehensive economic reforms, Economic, Financial and Administrative Reform Programme (EFARP), were initiated in 1995, with the primary purpose of tackling inflation and stabilizing exchange rate deterioration. Tight fiscal policies were introduced in order to reduce the budget deficits by decreasing public expenditure and increasing government revenue. On the expenditure side, government subsidies on petroleum products, electricity, communications, and basic consumer goods, such as wheat and barley, were reduced. To increase revenues, the Government improved its tax collection procedures, and devalued the official exchange rate, starting with customs evaluation, which generated additional revenues in oil exports and customs revenue. It also raised the interest rates and the commercial banks reserves requirement. This initial stage of economic reform took the form of an emergency cure in which the focus was on stopping the deterioration of the economy. By the end of 1995, the economy observed a 34 per cent reduction in the budget deficit and attained an 8.58 per cent real annual growth in GDP.

Despite the EFARP's successes in 1996, which received worldwide attention, the state of the economy was still characterized by large subsidies and heavy reliance on the public sector, which was definitely not sustainable. Faced with insufficient financial resources to continue its reform efforts, the Government entered negotiations with the International Monetary Fund (IMF), the World Bank, the United Nations and other multilateral/bilateral donors for assistance. The donor organizations have provided financial support, policy advice, and technical assistance to the Government's reform strategy, aimed at putting the economy on the path to sustainable and steadily-accelerating real economic growth, attaining financial stabilization, and strengthening the country's external position. On March 20, 1996, the IMF approved a 15-month Stand-by Agreement totaling SDR 132.4 million (US\$ 193 million), linked to a two-phase reform strategy, macroeconomic stabilization and structural transformation. Shortly afterwards, the World Bank agreed to lend the Government US\$ 80 million in support the reforms in trade policy, privatization, and the phasing out of price controls.

Economic reform programmes that had started in 1995 were continued in the following years. In 1996, the primary emphasis was on further strengthening the domestic economy. By the end of the year, such efforts had already begun to yield substantial positive results: the inflation rate declined to 12 per cent, the exchange rate stabilized, and the country's fiscal and balance of payment positions began to show signs of improvement. The Government prepared its 1997 programme as an extension of what had been undertaken in 1995 and 1996. Nonetheless, 1997 marked an important turning point after the Parliament approved the First Five-Year Plan (FFYP) 1996-2000 on December 30, 1996. The plan, prepared with the direct financial and technical assistance of the United Nations Development Programme (UNDP), was complementary with the EFARP policies and set forth a number of economic and social development goals and policy implementation strategies along with the time frame for their implementation. While the economic reform had started in 1995, the FFYP 1996-2000 advanced its efforts by prioritizing project objectives necessary to achieve the country's overall socio-economic development goals. These objectives included the acceleration of the economic growth rate, employment generation, improvement of the education and health sectors, and introduction of protective measures for environmental and water resources.

The country held its second national parliamentary elections on April 27, 1997. The election results were considered largely successful and deemed free and fair by the international community, which sent a strong signal that prospects for internal political stability were positive. The People's General Conference won two-thirds of the seats and shortly thereafter formed its new government. The international donor community, both multilateral and bilateral, responded favorably to the election results, rewarding the country with various economic assistance pledges to the end of the century. Moreover, re-scheduling the country's debts on Naples Terms at the Paris Club in late 1996 appeared to have set the stage for re-scheduling its bilateral debts to Russia, which is the country's major creditors.

Shortly after the election, the new Government was formed and began to take its economic reform to the next phase. In October 1997, the IMF approved a loan and credit package, under the Enhanced Structural Adjustment Facility and Extended Fund Facility (ESAF/EFF), over a three-year period up to the year 2000, amounting to SDR 370.6 million (US\$ 512 million), in order to support the Government's economic programme. Meanwhile, the Government continued to apply tight fiscal policies aimed at decreasing budget deficits to around 3% of GDP. As stability started to be felt in key macroeconomic indicators by the latter half of 1997, the economy seemed ready for more fundamental economic reform. Thus, the Government also began to focus on structural adjustment components such as public investment in infrastructure, direct and indirect tax reforms, trade liberalization, financial sector reforms and privatization. All these in turn, require changes in the legal framework to create an environment more favorable to private sector and an overhaul of the bureaucracy by reducing government paperwork and personnel. Furthermore, social protection during the economic adjustment period has been also an important component in the reform programme for development.

### III. DOMESTIC DEVELOPMENT CONSTRAINTS

Despite the relative achievements of the Reform Program that have been realized during the period (1995-2000), the economic and social indicators continue to provide an unsatisfactory profile of the economic performance and the living conditions of the population:

- 1- The GDP Per Capita is \$ 349 in 1999 and the unemployment rate is estimated to range between 25- 35 per cent of the labor force.

## **2- Population**

The population growth rate is 3.5% in 1999, which creates great pressures that undermine the achievements of the development programs. It also creates pressures on sources of natural wealth and causes several environment problems. Hence, the significant depletion of underground water and the decline of its quality are considered normal consequences of the population increase and of the diverse activities emanating from it. Moreover, the population density has left its prints on land through the excessive use that affects its quality. In rural areas, the depletion of plant coverage due to over herding and woodcutting for fire or construction use, and in quantities that exceed the planting rate creates a hazardous environment situation.

## **3- Poverty**

Poverty in the country almost doubled between 1992 and 1998, with the number of households below the "food poverty line" rising from 9% to 17% respectively according to the Household Budget Survey. This is attributable to the depreciation of the local currency, subsidy elimination, and other external factors (influx of returnees and refugees, suspension of foreign aid, impact of regional conflicts). By adding food, clothes, housing, education, health and transport into an "upper poverty line", the percentage of households living in poverty rose from 19 to 33 over the same period. Hence, poverty is becoming more widespread amongst the 18 million people who live in the country's urban and rural areas.

## **4- Education**

Even though literacy rates have improved over the years, illiteracy is still very high in the country. There are differences in rural and urban illiteracy rates (64 % vs. 34 % respectively) as well as major differences between genders. These gender discrepancies are also reflected in the actual school enrollment rates. Furthermore, these are significant variations among governorates when it comes to gross-enrolment ratios (GER) for basic and secondary education. 45 % of pupils enrolled in the first grade do not complete the basic education cycle, and the drop-out is greater in secondary schools.

## **5- Health**

Yemen has experienced a relative improvement of health services and life expectancy has increased over the recent years. In 1997, the overall life- expectancy rate increased from 57 to 58 years.

Even though, the infant mortality (estimated at 81 death per 1000 birth) has declined considerably in the last decade, it is still higher than the low – income country average of 64. The major causes of morbidity and mortality in Yemen are communicable diseases, hence preventable.

The delivery of health services is hampered by the fact that about 77% of the population lives in highly scattered communities, which in addition often cannot afford commuting costs to health care facilities. Only 45% of the population has access to health services (25% in rural areas). Still about 60 per cent of the population has no access to safe water and only 24 per cent has access to sanitation and 35 per cent to electricity.

Over the past two years, approximately 150 private clinics have been opened. Emergency medical services practically do not exist, as there are no public ambulances services. Also the population per doctor is more than 5000 people per doctor. The expenditure on health is 1.24 % of GDP in 1999.

## **V. PROSPECTS FOR THE NEXT DECADE (2000-2010)**

The economic prospects for the next decade looks better than those of the previous decade as the country settled its disruptive internal and external problems of the 1990s. The settlement of



Yemen's border dispute with its all neighbors, particularly with Saudi Arabia has certainly resulted in normalizing and strengthening the relations between Yemen and all its neighbors.

The Program of Action is derived from both the SFYP (2001-2005) and the Yemen Vision 2025, which both aim at moving Yemen from low-income group to middle-income group with diversified economy and social development. The whole economy is expected to grow at a rate between 6.5 to 7.5 per cent during the next 10 years. This entails raising Per Capita income from \$349 in 1999 to \$700 by 2005 and \$1050 by 2010, which means, it is being doubled every five years. Meanwhile, Per Capita growth is accompanied by diversification of the economy and development of the social structure.

The mission implied by Yemen Vision 2025 is to provide Yemeni citizens better standard of living and higher economic and social welfare, comprehensively and equitably.

The mission is to be accomplished through a comprehensive development strategy relying mainly on four key factors stated briefly as follows:

- 1- Development and upgrading of human power as the dynamic factor for growth and information technology economy. Thereby, establishing human resource development as the cornerstone for economic and social development.
- 2- Diversification of economic stature in order of moving away from high dependency on oil production and export to densification of income generation and employment creation through increasing agricultural, industrial, fisheries and tourism shares in gross domestic product.
- 3- Improving investment attractiveness and competitiveness of the economy in order to be able to mobilize domestic private investments and attract foreign direct investments and technologies, thereby, integrating with international economy on the bases of competitiveness and equity.
- 4- Export led economy. In line with the new economic direction towards openness and liberal economic and trade policies, it is essential to encourage export oriented investments and economic activities.

#### Objectives of the Program of Action

According to the comprehensive development strategies and objectives of both the SFYP (2001-2005) and the Yemen Vision 2025, the main objective of the Program of Action for the next ten years can be specified as follows:

- a- Achieving an annual rate of growth of real gross domestic product at a rate between 6.5-7.5 per cent in order to be able to double Per Capita income every five years.
- b- Reducing poverty at a rapid pace so that poverty percentage could be reduced from the present level of 33% to 15% by the year 2010.
- c- Encouraging massive investments in all sectors of the economy, especially, those characterized by labor intensive technology, in order to create as much employment as possible, thereby, reducing unemployment rate from the present level of about 35% to 10% by the year 2010.
- d- Raising sectoral annual rate of growth within the range of 8% to 10% in order to raise the aggregate economic growth rate, create employment, consequently, approaching economic diversification.
- e-Preparing the economy to effectively and competitively integrates to the world economy through strengthening economic integration locally, regionally, and internationally.

These objectives will be carrying out through a set of macro and sectoral policies, which aim to generally continue the efforts of the structural reforms already initiated under the IMF's Stand-By- Arrangement (SBA) by broadening and deepening them.

Thus, the government's effort in the coming years will continue to focus on: tax and expenditure policies; revenue administration; the civil service; pension funds; subsidy elimination; customs administration; budget management; indirect monetary control and

monetary management; the banking system; trade and tariff policies; the public enterprise sector largely through rapid privatization; and the economic environment.

The achievement of the Program of Action objectives requires a lot of resources, wide capabilities, and a long period of time. However, it is possible to achieve some of these objectives on the short and the medium-term. To do that, a lot of efforts and procedures have to be taken by the Government and the international community.

The government is seeking to expand the role of the private sector by reducing the crowding-out effect of a larger and inefficient government.

Also, as a complementary move with the EFARP policies, the Second Five-Year-Development-Plan (SFYDP) 2001-2005 preparation is now underway, aiming at the achievement of certain social and economic objectives, including accelerating the economic growth rate of the whole economy at a rate between 6.5-5.5 per cent during the period of 2001-2005, reducing the high population growth rate, generating employment, reducing poverty, improving education and health and introducing protective measures for the environment and water resources. The NGOs are also working with the government hand-in-hand and rendering services even in the remote areas, the civil society is increasingly becoming active and has been participated in raising awareness about environmental protection, civil rights and about rights of the underprivileged women and children, and above all Governance in the country is increasingly becoming transparent.

The total expected investments during 2001 to 2010 is estimated to be \$24199.5 Millions, about \$ 14199.5 Millions is expected to be financed from Domestic Saving, \$ 5579.5 Millions from Foreign Direct Investment (FDI) and the rest \$4427.5 Millions is expected to be financed from foreign resources as; grants, soft loans, and concessional multilateral loans.

The Government of Yemen considers foreign assistance of the IMF and the World Bank, and all other donors as an important factor in helping and in fulfilling the gap between the limited available resources and the required resources for achieving the targeted economic growth and to promote sustainable human development in the next decade (2000-2010).

## I. PERFORMANCE IN THE 1990s

There are major internal and external events that caused the economic and social situation of Yemen to suffer great shocks at the beginning of the 1990s. First came the Gulf War of 1990, which brought in its wake the return of about one million returnees from the Gulf States (particularly, from Saudi Arabia and Kuwait). The remittances from these returnees (estimated yearly at \$1 billion) ceased, and most of the returnees became unemployed and poor. In addition, some donors stopped their large aid programs in Yemen. Second the internal militant conflict followed in 1994, taking resources away from social and economic development. The civil conflict also damaged much of the economic and social infrastructures of the country. The outcomes were: balance of payments deficit, high inflation, large-scale unemployment and increasing international debt. These all led the government to adopt a package of structural adjustment reforms with the help of the IMF and the World Bank. These macro economic reforms required large cutbacks in social services welfare and removal of subsidies for basic foods. The results of this program, however, have been very successful. Real non - oil GDP grew by about 5% in 1997 after a stagnation in the early 1990s. Furthermore, after having experienced high rates of CPI inflation (71 percent in 1994, post conflict), CPI inflation has been stable at around 26 percent in the last years. Other outcomes are the decrease of the deficit to 2.4 percent of GDP in 1997 from 16.3 percent in 1994. The exchange rate stabilized and the balance of payments became stronger.

The success in macroeconomic stabilization has regained private sector confidence in the economy. Yet, Yemen economic development experience has not been smooth due to socio-political and economic complexities. To raise the standard of living and improve the quality of life of the citizens based on the success in macroeconomic management, the Government prepared the FFYP Sectoral Strategy to maximize utilization of available resources and benefit from sector-wise relative advantages. First, since the mining and quarry sector plays a strategic role in the country's development, providing an important source of hard currency earnings and financial resources to government investment expenditures, the FFYP emphasized two main objectives in order to increase its oil and gas revenue: (a) to expand extraction activities to ensure a rise in the oil and gas production or, at least, to maintain the current level; and (b) to improve the contract conditions with private oil companies operating in the fields. Second, the manufacturing sector was to be developed in order to exploit its natural capacity to absorb modern technology and know-how, and the high potential to employ and train workers. Third, the Government recognized that the prospect of agricultural development was increasingly related to water resources availability. Thus, establishing water resources management and policies took strategic importance and priorities in the FFYP. In addition, excellent opportunities for fishing and fish processing for exports were realized.

### - Sectoral Indicators

#### (a) Structure of the Economy

In 1999, the GDP of the country consisted of industries, government services, and other private, non-profit services. The weight of government services in the total GDP had increased steadily from 15.60 per cent in 1990 to 24.8 per cent in 1999.

As shown in table (1), the traditional economic base of the country is agriculture, forestry, and fishing, which contribute around 23 per cent of the country's total GDP. As a result of oil discovery in 1984, mining and quarrying became another important industry. In particular, with an unexpected output increase in crude oil extraction in 1994, and high prices of crude oil in the recent years before the end of 1997, it grew to be the second largest industry in economy, contributing 16 per cent of the GDP in 1999.

Although the manufacturing sector accounted for only 8.2 per cent of GDP in 1999, its potential role of providing job opportunities and thus, substantially contributing to the domestic economy, is apparent.

**TABLE (1)**  
**STRUCTURE OF GDP AT PRODUCERS PRICES, BY ECONOMIC ACTIVITY**  
(AT CONSTANT PRICES FOR 1990-1999- %)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
Agriculture, forestry, and fishing	24.4	22.2	24.3	24.3	23.1	22.3	21.4	21.6	23.4	22.6
Mining and quarrying	13.7	12.7	9.9	9.9	13.9	15.0	16.1	16.0	15.6	16.2
Manufacturing	9.4	9.5	9.2	9.4	8.7	9.7	9.2	8.6	8.5	8.2
Electricity, water, and gas	1.2	1.3	1.2	1.2	1.1	1.1	1.1	1.1	1.1	1.1
Construction	2.7	2.9	3.1	3.1	2.5	2.7	3.3	3.9	3.8	3.7
Whole and retail trade	7.3	7.6	7.1	7.2	6.2	6.4	6.6	6.5	6.7	6.9
Transport, storage, and communications	14.9	13.8	14.9	12.3	9.8	8.6	6.9	7.6	7.7	7.8
Financial institutions and real estate	8.4	8.5	7.7	7.5	7.9	7.2	6.6	6.4	7.2	7.2
Community, social, and personal services	1.2	1.3	1.2	1.2	1.2	1.1	1.2	1.3	1.1	1.2
Producers of government services	15.6	18.2	20.3	22.1	24.5	24.9	25.4	25.3	24.4	24.8
Producers of private, non-profit services of household	0.2	0.2	0.1	0.2	0.2	0.1	0.2	0.2	0.2	0.2
Import duties	3.2	4.6	3.1	3.4	3.3	2.9	3.2	2.9	2.2	2.1
Less: imputed bank	2.1	2.5	2.1	2.0	2.2	1.9	1.2	1.1	1.8	1.7
Services charge										
GDP at market prices	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

### (1) Real GDP

The economy appears to have responded positively to the economic reform programme. Table (2) below shows that its real GDP registered an impressive annual growth rate of 10.91 per cent in 1995. Although the economy's performance dropped slightly in the following years, partially due to the Government's contractional fiscal and monetary policies, it still achieved over 4 per cent growth rates in both 1998 and 1999. The macroeconomic objectives for 1996-1997 had included real GDP growth of 2.5 per cent in 1996 and 5 per cent in 1997. The actual GDP growth rates surpassed these targets. However, because of the sharp decline in oil revenue following a plunge in world oil prices since late 1997 and the curtailment in government expenditure as a consequence, the country's real GDP growth is slowed down in 1999 to 4.25 per cent (table 2).

**TABLE (2)**  
**REAL ECONOMIC GROWTH RATE, 1991-1999**  
(In percentage)

	1991	1992	1993	1994	1995	1996	1997*	1998**	1999**
Real GDP growth rate	1.90	8.36	4.07	2.13	10.91	5.91	8.12	4.91	4.25

\* Provisional Actual.

\*\* Provisional Data

### (2) Non-oil GDP

Most industries registered negative growth rates during the 1994 militant conflict, however they achieved positive rates in 1995. Therefore, to a certain degree, expansion of the non-oil sector

industries is considered to have rebounded to normality. Nevertheless, their growth was respectable as a whole in 1997 and 1998, registering rates of 8.2 percent and 5.3 per cent, respectively (table 3).

In order to achieve real non-oil GDP growth of six per cent a year on average toward year 2000, the programme for calendar year 1996 aimed at attaining three per cent real growth in the non-oil sectors. The 1996 results show that this goal was successfully met. In addition, the non-oil sectors were expected to grow at 5.92 per cent in 1997, out-pacing the overall GDP growth rate in the same year. Thus, the 1997 programme's goal to achieve 5.5 per cent growth in non-oil GDP was also met. However, the 1998 performance was not estimated to have been as high, whereas non-oil GDP is still considered to have grown at a faster rate of 3.59 per cent than the total GDP.

TABLE (3)  
REAL NON-OIL GDP GROWTH RATE, 1991-1999  
(In percentage)

	1991	1992	1993	1994	1995	1996	1997*	1998**	1999**
Non-oil GDP growth rate	3.1	11.8	4.1	(2.3)	9.5	4.6	8.2	5.3	3.6

\* Provisional Actual.

\*\* Provisional Data

( ) Indicates negative.

Under the Government's initiatives to encourage private sector participation, industries as a whole grew faster than the overall GDP since 1995. As seen in table (4) below, the total industry grew at 10.58, 8.57 and 8.22 per cent in 1995, 1997 and in 1998 respectively. These were higher than the GDP growth rates; 9.5, 8.2 and 5.3 percent in 1995, 1997 and in 1998 (table 2).

TABLE (4)  
ANNUAL REAL GROWTH RATES OF SECTORS, 1991-1999  
(In percentage)

	1991	1992	1993	1994	1995	1996	1997*	1998**	1999**
Agricult., forestry & fishing	(7.42)	19.09	4.44	(3.41)	6.92	1.86	8.77	13.73	0.88
Mining and quarrying	(5.57)	(15.42)	4.24	42.65	19.90	13.54	7.46	2.49	7.81
Manufacturing	3.60	4.44	6.01	(5.34)	23.75	0.61	1.05	3.76	.68
Electricity, water & gas	13.93	1.86	1.82	(10.29)	13.60	12.25	1.97	2.38	7.21
Construction	8.07	17.00	1.73	(17.17)	23.14	28.18	28.43	1.44	0.73
Wholesale and retail trade	4.82	1.67	6.85	(13.13)	15.45	8.19	6.63	8.19	7.56
Transport, storage, & commc.	(5.97)	17.45	(13.89)	(19.20)	(2.82)	(14.01)	18.27	6.26	5.59
Financial institutions and real estate	3.73	(2.36)	3.81	5.61	0.71	(2.68)	4.67	17.91	4.47
Community, social, and personal services	5.38	3.35	3.06	3.94	(1.04)	12.38	4.20	5.78	5.38
Total of industries	(2.42)	7.00	1.11	(0.76)	10.58	3.63	8.57	8.22	3.87

\* Provisional Actual.

\*\* Provisional Data

( ) Indicates negative.

#### (b) Agriculture

In the FFYP, it was initially expected that the agricultural sector would grow at an average annual rate of about 7 per cent, the manufacturing industries by 8 per cent annually, and other sectors at 8.2 per cent. Recent performance of the agricultural sector, which is one of the most important sectors in the country, has been exceeded the 7 per cent of the FFYP (8.77, 13.73 per cent in 1977 and in 1998 respectively).

Prior to reunification, the Governments banned the import of vegetables, fruit, and some other agricultural produce in 1989 in order to encourage the growth of the country's agricultural sector. As a result, the country became flooded with cheap fruits and vegetables. Yet, the country's export markets were slammed shut due to the consequence of the Gulf crisis. Some produce remained unharvested, prompting rural people to migrate to the cities as the export of their produce became extremely difficult.

Nevertheless, agriculture continues to be the largest sector, with agriculture and forestry combined contributed close to 23 per cent of the country's GDP (table 1). The proportion of the population engaged in agriculture is still dominant, estimated to be about 50 per cent in the late 1990s; most of these workers are women, children, and the aged.

The arable land under cultivation was estimated to be around one million hectares in 1995, representing less than two per cent of the total area of the country. The overall growth in agricultural production has not been enough to meet the domestic demand for food; resulting in a wide gap between consumption and production. For example, output from the agricultural sector increased only by 1.72 per cent in 1996 compared to that in 1995. The annual growth rate, improved slightly in 1997 to 2.98 per cent. Yet, it was the second-smallest growth rate, after the financial institutions and real estate, among all the industries, and insufficient to keep up with the country's rapid population growth rate. Consequently, at the end of 1996, self-sufficiency in grain was only 35 to 40 per cent, and 50 to 60 per cent for dairy products. Meanwhile, food imports have grown rapidly, accounting for more than 33 per cent of total imports in the same year.

The country grows cereals, cotton, fruits, vegetables, tobacco, and coffee. Table (5) shows that cereal production has been declining during the past six years, except for a small increase of 1.19 per cent in 1995 and 27.94 per cent in 1998. The growth patterns of vegetables and cash crops, such as cotton, sesame, tobacco, and coffee, are similar; their production growth has been steady, except for 1994 when they both registered negative growth. Fodder has been growing positively since unification, even in 1994. It increased at impressive rates of 20.16 in 1997 and 26.5 in 1998.

The gap between local food production and consumption is the greatest challenge to the country. The agricultural sector currently has the capacity to supply population with most of their demand for vegetables and fruit, but meets only less than half the domestic demand for cereals. In order to reduce reliance on imported goods and also to relieve the pressure on the limited resources such as water and farmland, the Government realized that taking proper initiatives to decrease population growth and increase the levels of education for efficient agricultural production is necessary.

TABLE (7)  
PRODUCTION OF AGRICULTURAL CROPS, 1992-1999

	1992	1993	1994	1995	1996	1997	1998	1999
Cereals (tons)	886908	910196	870266	880588	731169	712278	911304	757932
Growth rate (per cent)		2.63	(4.39)	1.19	(16.97)	(2.58)	27.94	(16.83)
Vegetables (tons)	680482	730896	645769	668800	703244	717631	747131	759820
Growth rate (per cent)		7.41	(11.65)	3.57	5.15	2.05	4.11	1.7
Fodder (tons)	815608	856388	861534	877957	907650	1090639	1380571	1399477
Growth rate (per cent)		5.00	0.60	1.91	3.38	20.16	26.53	1.37
Cash crop (tons)	40351	42431	38852	43460	50174	56644	63784	65010
Growth rate (per cent)		5.15	(8.43)	11.86	15.45	12.90	12.61	1.92
Fruit (tons)	335684	362858	360749	402160	391278	469352	554785	57873
Growth rate (per cent)		8.10	(0.58)	11.48	(2.71)	19.95	18.20	(89.57)

( ) Indicates negative.

### (c) Oil

Commercial quantities of oil were discovered in the Marib oil field in 1984. Since then, three major oil export pipelines have been constructed to provide the necessary flexibility for the operating companies in case of further discoveries. After reunification, output continued to increase at a rapid rate due to the coming on stream of new oil fields. The major oil producing areas now include Masila, Marib, and Jannah.

As shown below in table (6) below, the value of crude oil exports constitutes most of the country's revenue from commodity exports. When international oil prices escalated in the winter and spring of 1995-1996, the country earned windfall oil profits, as did other oil exporting countries. Consequently, the country's mining and quarrying sector experienced a rapid growth at 19.90 and 13.54 per cent for 1995 and 1996 respectively, after that it slowed down to 7.81 in 1999 (table 4).

TABLE (6) CRUDE OIL EXPORTS AS A PERCENTAGE  
IN THE TOTAL EXPORTS, 1991-1998

	1991	1992	1993	1994	1995	1996	1997	1998
Crude oil exports (Million Rials)	7092	2921	3423	9973	74907	242171	304835	58197
Total exports (million Rials)	7685	3951	4495	11216	79434	251830	320293	61677
Crude oil exports/total exports	92.28%	73.93%	76.15%	88.92%	94.30%	96.16%	95.17%	94.36%

The Government's share of oil exports has more than doubled in this decade, rising from 66,385 barrels per day (bpd) in 1990 to 145,205 bpd in 1997. Oil revenue not only constitutes the major source of hard currency for the country, but also its share in the government's budget revenue has been significant, at around 70 per cent.

The oil output provides the country's primary source of income, leading to its economic growth. The total output had reached the highest level in its oil production history, at 420,000 bpd, at the end of 1996. However, output from the two mature fields in Marib and Masila seems to have peaked and then begun to fall. Total crude oil production was estimated 390,000 bpd at the end of 1998. New fields are under construction and will be operational soon, yielding additional oil. However, they are smaller fields and may only replace anticipated declining output from the older fields. Thus, the total output is expected to be around 400,000-450,000 bpd.

The country's proven oil reserves are estimated at four billion barrels as of January 1999, one billion barrels of which are recoverable. They will be completely depleted in 29 years if crude oil production remains at the current level. The Ministry of Oil and Mineral Resources has taken the initiative of reevaluating the country's geological data for further exploitation potential by actively inviting more private oil companies to participate in the efforts through promotional offers.

Domestic consumption of petroleum products has been rising steadily, increasing from 49,687 bpd in 1991 to 66,803 bpd in 1997, except in 1994 during the civil strife (table 7). The combined consumption of oil and gas covers about a half of the country's domestic energy demand, while wood fuel, the primary source of household energy in rural areas, covers the other half. Given the country's high rate of population growth (3.5%), energy demand is expected to double in next ten years. The Government's strategy is to encourage greater household use of gas thereby stemming deforestation and freeing up higher value oil products for export.

TABLE (7)  
DOMESTIC CONSUMPTION OF PETROLEUM PRODUCTS, 1991-1997

Barrels per day	1991	1992	1993	1994	1995	1996	1997
Gasoline	20029	21601	23652	22949	25138	23968	24506
Diesel	17009	17748	17138	17633	18676	20239	21909
Kerosene	2467	2560	2779	2532	2961	2913	4661
Fuel oil	10182	12469	14017	10146	13926	15661	15727
Total	49687	54378	57586	53260	60701	62781	66803
Percentage change		9.4%	5.9%	(7.5%)	14.0%	3.4%	6.4%

( ) indicates negative.

#### (d) Refining

The country has a major refinery at Aden and a smaller unit, with a capacity of 10,000 bpd, at Marib. Both refineries are managed by the Yemen Refining Company, which is controlled by the State-owned General Corporation for Oil and Mineral Resources. Due to the significant damage incurred during the 1994 militant strife, the capacity of the Aden Refinery Plant declined from its design capacity of 170,000 bpd to the actual production level of 100,000 bpd. Rehabilitation and modernization of Aden Refinery is one of the projects specified in the country's FFYP, aimed at modernizing the ageing existing units and setting up new units to rationalize energy inputs and improve the product qualities. A two-year plan to renovate the facility and raise its capacity to 150,000 bpd gained Iranian support in February 1996. In 1997, the output from the Aden Refinery Company registered a 10.8 per cent increase.

#### (e) Natural gas

With oil exports being the dominant share in total exports of the country, export revenue had been highly dependent on oil prices. To reduce such heavy dependence on one sector, which exposes the economy to a vulnerable situation, and to generate needed employment opportunities for the population, development of the non-oil sectors and export diversification is among the country's top economic priorities in the next decade (2001-2010).

Since natural gas was discovered in 1984 together with oil, commercially recoverable reserves in the country have been rising. With estimated natural gas reserves of 16.9 trillion cubic feet, the country has considerable potential as a gas producer and exporter in the future.

The bulk of these reserves are concentrated in the fields operated by the Yemen Exploration and Production Company. However, few facilities had been installed for recovery, resulting in the production level of only 540 million cubic meters.

In 1995, the Government began negotiations for gas development agreement with the French company, TOTAL; with the intention of developing natural gas resources for domestic use and exports as Liquefied Natural Gas (LNG). In early 1996, the Ministry of Oil and Mineral Resource signed an LNG joint venture between TOTAL and the Yemen General Gas Corporation. The joint venture is the largest single energy project. It aims at developing natural gas from Marib and Al-Jaw fields, transporting it via pipeline to a natural gas processing plant and an export terminal on the country's southern coast, and exporting 5.2 million tons of LNG per year over 25 years beginning in 2001.

Export markets for LNG were expected to be found in Europe, where gas is a favored source of energy on environmental grounds, and in South-East Asia, for its petrochemical industries.

In January 1997, the venture parties agreed to include two American companies, Hunt Oil and Exxon, and the Yukong Group of South Korea as partners in the project. Recently, Hyundai of South Korea has also joined this consortium as the newest partner, while TOTAL remains the managing company of the project. A total of 13 trillion cubic feet was allocated to this project, with a 15 per cent share to the Government and the remaining 85 per cent share to the foreign companies.



The total investment in the oil and gas sector over the five-year period of 1996-2000 was YRIs 817,000 million (US\$ 6,285 million). Foreign investment is almost YRIs 390,000 million (US\$ 3,000 million), of which 75 per cent is directed to the LNG project alone. The partners have begun financing arrangements. The Government anticipates earning over US\$ 600 million from gas exports in the early stages.

#### (f) Electricity and Water

Despite the fact that the power sector plays an essential role in the country's economic development, the electricity output is yet inadequate for a country having about 18 million people. The State-owned Public Electricity Corporation (PEC) supplies ninety per cent of all electricity in the country. Its maximum electricity capacity is registered as 609 megawatts, but actual output level is between 350-400 megawatts.

Moreover, electricity only reaches 25 to 30 per cent of the population, as many of the rural and mountainous parts of the country are not connected to the national transmission and distribution grid due to the high cost. Power generation in remote areas beyond PEC's Network is currently supplied mostly by diesel engines. Thus, the Government's General Authority for Rural Electrification and Water Supply is investing in small electricity projects in rural areas, with an element of community participation.

In 1995, under the growing demand for electricity at a rapid 15 per cent annual rate, the Ministry of Electricity and Water publicly announced its support for private power generation, seeking to attract private sector investment. In October 1996, the PEC signed a \$US 20 million Build-Own-Transfer (BOT) contract, the first of its kind in the country, offering up to 1.4 gigawatts of new capacity over a ten-year period.

In addition, there remains room for improvement in electrical power generation when discoveries of uranium, radium, and various radio-active materials are to be exploited.

Water and sewage services are even less adequate and the ROY is considered it as one of the most water-scarce countries in the world. For example, the 400,000 residents of Taiz, the country's third-largest city, receive public water once every 30 to 40 days. Also, in Sana'a, raw sewage runs in to major streets in some parts of the city, in addition, to a shortage of water supply. During the period of 1990-1996, about 39 per cent of residents in the country as a whole did not have access to safe water.

There is increasing demand for water from the rapidly growing population and the expanding agricultural sector. The existing water supply is being depleted and groundwater in the highlands is being pumped out at such a rate that large parts of the rural economy could disappear in the coming generation.

The total annual renewable water resources are estimated at 2.1 billion cubic meters. With a population of about 18 million, not more than 130 cubic meters of water is available per person each year. This figure is considerably lower than the average of 1,250 cubic meters in the Middle Eastern and North African region and the worldwide average of 7,550 cubic meters. The country will face a severe water supply crisis in the near future.

The conditions of water supply and sanitation in rural area is particularly poor; less than twenty per cent of rural inhabitants have access to potable water and even fewer have access to safe sanitation, as compared to the urban areas where eighty per cent and sixty per cent of inhabitants have access to potable water and safe sanitation, respectively. Given that about seventy per cent of the total population lives in rural areas, the magnitude of inadequate water supplies in the country as

a whole is easily understood to be severe. In addition, water shortages have constrained the country's potential for urban industrial development.

Rapid population growth has drastically increasing demands on the already stretched water resources; and the lack of a synchronized control management mechanism to mitigate the problem has not helped the country to find a real solution. For example, modern drilling and water pumping methods provided to farmers, subsidized electricity supply, and cheap diesel local prices lesser than the prevailing international prices have all contributed to over pumping of groundwater. Therefore, the Government is aiming to remove all price distortions and unsustainable incentives that have resulted in the over pumping.

In addition, water supply costs are rising sharply as water is found at a deep level. Pumping groundwater must be discouraged by changes in the relative prices, which correctly reflects the value of scarce resources. Such pricing policies include introducing higher prices for diesel, levying higher tariffs and taxes on pumping equipment, eliminating credit subsidies for pumps, and removing existing incentives to the production of water-intensive products. It is also in the Government's agenda to privatize water and sewage services in order to manage this vital, scarce resource properly and more efficiently.

The Government has been involved in several projects to alleviate the water problem. In 1996, the World Bank financed Taiz Water Supply Pilot Project obtained in Taiz amounting for US\$ 10.2 million. It aimed at mitigating the immediate water shortage in Taiz by doubling the water supply by 1997 and also identifying new water sources to meet projected demand to the end of year 2000. The Project's objectives are: (a) to rehabilitate and construct demand-based community-managed rural water supply schemes; (b) to provide materials for the construction, by beneficiaries, of safe waste-water and sewage disposal and safe drinking water storage facilities; and (c) to convey health and hygiene messages regarding water handling and safe sanitation. Overall IDA-financed projects are estimated to US\$ 406 million, to support the Government in developing comprehensive water strategy and action plan; setting up a National Water Resource Authority; increasing agricultural production; and protecting and conserving the environment.

#### (g) Financial

The banking system in the country consists of the Central Bank of Yemen (CBY), ten commercial banks, and three specialized banks for the promotion of agriculture, industry, and housing, and three Islamic banks. As of the end of June 1998, one of the commercial banks, the National Bank of Yemen (NBY), is 100 per cent owned by the Government and another commercial bank, the Yemen Bank for Reconstruction and Development (YBRD), had the majority shares by the Government (51 per cent). Moreover, the Ministry of Finance was also the majority shareholders of the three specialized banks with holding percentage of seventy or higher.

In the years following the 1994's conflict, commercial banks' intermediation functions came to a halt. Nominal credit growth in the country's private sector dropped from around 19 per cent annually over 1991-1993 on an average to 13.4 per cent at the end of 1994. Three factors were considered to have contributed to this phenomenon: (a) negative real interest rates due to high inflation and hence a lack of incentives for banks to lend or attract deposits; (b) the absence of effective legal recourse for banks to recover non-performing assets; and (c) the Central Bank regulation prohibiting the use of foreign currency deposits as collateral.

The real interest rate moved to a positive position as a result of macroeconomic stabilization in the past few years. In addition, banks were freed from the constraints of the past, as the CBY embarked on an effort to overhaul the banking sector in 1996 with the support of a US\$ 80 million loan from the

World Bank. Major repositions of constraints included: (a) permission for banks to lend in foreign exchange and deregulation of banking fees and charges; (b) reduction of reserve requirement from 25 per cent to 10 per cent; and (c) remuneration of legal reserves at 5 per cent and hard currency reserves at LIBOR-less-50 basis points. Expected benefits were: improved resource use, reduced transaction costs and hence reduced bank-lending rates, and increased bank intermediation.

In 1997, the Government began proceeding with privatization of NBY and YBRD. This was done by negotiating to relieve the banks of non-performing loans to public enterprise debt, contracting an independent auditor to perform a diagnostic review of the banks, consolidating financial monitoring of the banks in one ministry, inviting bids from a financial adviser for the sale of Government shareholding of at least 51 per cent, and transferring bank operational management to strategic partners. In addition, separate contracts were also signed with independent auditors from international accounting firms to prepare special audits of the 1996 accounts for the three specialized banks. Their financial positions were to be determined based on adequate and reliable information in order to decide the banks' future status.

The CBY also engaged in many on-site and off-site supervisory activities which resigned-in many of the bank directors. New requirements include external auditing and new accounting norms, such as monthly reporting of delinquent borrowers and a classification of loan and equity portfolios, thus bringing Yemeni banks in line with international standards. Meanwhile, the supervision capacity of the CBY itself was to be enhanced, through a new recruitment process of inviting qualified candidates to its Supervision Department and a medium-term development programme for the Department as well as salary restructuring for the entire CBY.

Furthermore, a new law was proposed as a cornerstone for a more revitalized and efficient banking sector. The main stipulations were: (a) an eight per cent capital adequacy ratio, paid-up capital to gross lending, for commercial banks in order to strengthen their financial positions; (b) new criteria for bank licensing in order to improve the quality of banks at entry; (c) introduction of better accountability of individual directors, especially regarding credit concentration, insider lending, and non-performance in order to ensure good governance and soundness of banks; and (d) a framework for penalties applicable for all financial institutions for infractions of banking law and regulations. Under an amendment, all banks were permitted to engage in financial leasing so that increase diversity of financial instruments would be available, thus minimizing credit risk and providing a vehicle for medium-term credit.

#### (h) Tourism

The country is endowed with a unique culture, historical heritage and varied natural environment and topography, including the long coastal line of beaches and islands, which have great potential to attract international tourists and compete with other countries. Therefore, despite a shortage of modern hotels and restaurants, the country's tourism had been on the rise. Since the end of the militant conflict in 1994, the total number of tourist arrivals has increased, reaching a peak of 84,000 visitors in 1997. Recent annual growth rates were 52.5 per cent in 1995, 21.3 per cent in 1996, and 13.5 per cent in 1997. These surpassed the growth rates of tourist arrivals in the Middle East region as a whole, which were 6.3 per cent, 4.4 per cent, and 5.0 per cent in 1995, 1996, and 1997, respectively.

Tourist revenues have been increasing after 1994. As shown in table (8) below, US\$ 33 million was received in 1995 with an annual growth rate of 73.7 per cent. In 1996, revenues amounted to US\$ 42 million and grew to US\$ 69 million in 1997, registering a remarkable annual increase of 64.3 per cent; and they are reported by the Ministry of Culture and Tourism to have reached US\$ 84 million in 1998.

The importance of tourism for the national economy is apparent. Foreign currency revenue from the tourist industry in 1997 contributed significantly to the country's total export revenue, after oil

sector. Tourism also vitalizes investment in the economy's infrastructure and brings employment opportunities throughout the country, even in some remote areas. There are three dimensions of tourism that can be further developed: business tourism, cultural tourism, and leisure tourism. The Government has taken the initiative of modernizing business facilities, advertising its cultural wealth, and improving the quality of services and facilities in tourist establishments; it has also invited private-sector investment to develop the sector.

TABLE (8)  
TOURIST ARRIVALS AND RECEIPTS, 1991-1998

	1991	1992	1993	1994	1995	1996	1997	1998
Tourist arrivals (thousands)	44	72	70	40	61	74	84	82
Growth rate (per cent)	(15.4)	63.6	(2.8)	(42.9)	52.5	21.3	13.5	(2.4)
Receipts (US\$ million)	21	47	45	19	33	42	69	84
Growth rate (per cent)	5.0	123.8	(4.3)	(57.8)	73.7	27.3	64.3	21.7

( ) Indicates negative.

## - Social Indicators

### (a) Population

The country's population was estimated to be 16.5 million in 1997 and 17 million in 1998 and about 18 million in 2000. The fertility rate, 7.2 births per woman, is one of the highest in the world. At the same time, overall death ratios gradually decreased, reaching 12.2 per cent for males and 10.4 per cent for females in 1997. Table (9) below presents annual population growth rates by age group, forecast for a ten-year period ending year 2005. The country's population is expected to grow at around 3.4 to 3.7 per cent per year. With such high annual growth rates, the population will double in twenty years.

TABLE (9)  
ANNUAL POPULATION GROWTH RATE BY AGE GROUP: FORECAST, 1995-2005  
(In percentage)

	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
Age 0-14	2.99	3.01	3.36	3.32	3.30	3.36	3.37	3.80	4.19	4.30	4.09
Age 15-64	4.38	4.51	4.17	4.16	4.08	3.91	3.69	3.55	3.39	3.33	3.38
Age 65+	(2.62)	(1.85)	(2.06)	(1.40)	(1.07)	0.00	0.90	0.00	0.36	0.35	1.06
Total	3.43	3.55	3.56	3.57	3.54	3.53	3.45	3.57	3.68	3.70	3.65

Note: ( ) indicates negative.

Initially until year 2001, the middle age group, 15-64 years of age, is expected to grow at the fastest rate among the age groups, slowing down gradually to below the national average after year 2002. In contrast, the youngest group, 0-14 years of age, is expected to grow at increasing rates, finally surpassing the expected annual growth rate of the middle group and the national average growth rate. Age group 65 and above is expected to decline until year 2000 and then begin to increase gradually, contributing to overall population growth.

The population is youthful, with the age group 0-14 representing around 47 per cent of the total, the age group 15-64 representing 50 per cent, and those 65 years and above 3 per cent. Thus, the country is faced with a pressing demand for nutrition, child health care, education, and employment opportunities.

### (b) Employment

The contribution of the population to the labor market increased from 1994 to 1999 by 46 per cent due to the large number of school drop-outs and to non-enrolment in the education system. In addition, the existing population size of about 18 million and its rapid growth rate resulted in the labor force growing at an annual rate of 4.5 per cent, with 130,000-150,000 new job seekers annually. The annual growth rate of the female labor force is estimated to have been 9.3 per cent on average during the period 1994-1998, and that of male workers 4.3 per cent. In consequence, the relative importance of males in the total labor force declined from 81.8 per cent in 1994 to 78.3 per cent in 1998, while the female workers' contribution increased from 18.2 per cent to 21.7 per cent during the same period.

The concentration of the young in the labor force among the young is noticeable. According to the 1994 Census, 67 per cent of female workers and 70 per cent of male workers are in the age bracket of 15 to 44 (table 10). About 9.6 per cent of this group was unemployed. In contrast, 4.6 per cent of the labor force aged 45 and above were unemployed, with the overall unemployment rate registering 9.1 per cent (some other official and non official sources estimate unemployment rate to be between 25-35 %). Therefore, the country faces a particularly challenging task of training an increasing flow of young workers.

The Government traditionally acted as employer of last resort and, therefore, the total number of public sector employees rose to 430,000 by 1996. However, since the beginning of the implementation of economic reforms, the country's employment condition seemed to have worsened, at least in the short term, as a result of the freeze of new recruitment and the down – sizing of employees in the public sector, while the private sector remained too weak to absorb replaced workers.

The Government recognized the need to address the employment issue and drafted a new national population strategy and action plan at the Second National Population Conference held in October 1996. As one of its efforts to facilitate skill-matching mechanisms between job seekers and private sector requirements, the Government requested the assistance of the United Nations Development Programme (UNDP) in establishing a labor market database and information system to monitor the labor market and identify all basic factors and constraints affecting the country's employment conditions.

TABLE (10) DISTRIBUTION OF LABOR FORCE

Age group	Both	Female	Male
10-14	6.5%	15.6%	4.2%
15-24	22.8%	25.3%	22.1%
25-34	25.8%	23.2%	26.5%
35-44	20.8%	18.5%	21.4%
45-54	12.8%	10.4%	13.4%
55-64	6.9%	4.6%	7.5%
65+	4.3%	2.3%	4.8%
Total	100.0%	100.0%	100.0%

### (c) Vocational Training Programme

With the return of a large number of laborers from the Gulf States during the Gulf Crisis in 1990, the labor supply in the country increased dramatically. However, most of these surplus workers were unskilled or semi – skilled and the country's labor market lacked qualified personnel with professional and technical skills.

To meet rising demand for skilled workers in the private sector, the Government created, in 1995, the National Council for Vocational Training with a majority of private sector representatives, whose mission was to supervise vocational and technical training. To help strengthen the country's capacity to train skilled labor, the Government also launched the Vocational Training Project in 1996, supported by the World Bank with a credit of 15.7 million SDR. The private sector has shown strong commitment to supporting the management and financing the project, not only by providing pre-employment enterprise-based and in-service training but also by mobilizing funding for the project.

The project consists of three components: (a) to provide technical assistance, equipment and training materials, and to rehabilitate facilities to help upgrade quality in each of the country's 15 vocational training centers; (b) to support community-based Adult Education and Training Programmes specifically targeted to women; and (c) to set up a new governorate structure by strengthening the capacity of the General Authority for Vocational and Technical Training, the public agency in charge of overseeing policy-making and setting national standards for vocational training while monitoring implementation.

Efforts to promote technical skills among the country's future labor force have resulted in measurable progress. In recent years, the total number of basic school graduates eligible to enroll in vocational and technical school has been around 400,00 annually, three per cent of which usually consider attending technical and vocational institutes. However, the Ministry of Labour and Vocational Training reports that until 1997, the annual in-take of new trainees in all technical vocational institutes and center in the entire country was about 1,600. In 1998, the number enrolled in various programmes including short-term intensive courses increased to 10,000. In addition to the quantitative growth, qualitative re-direction of the training programmes, such as promotion of skills based on market requirements and producing addition to the quantitative growth, quantitative re-direction of the training programmes, such as promotion of skills based on market requirements and producing manpower with immediately employable skills has been undertaken.

#### (d) Education

Education is a key factor in the development and changes in a country's economic and social conditions. Under its structural reform programme, the Government is committed to maintain an adequate expenditure-to-GDP ratio for primary education. As shown in table (11) below, the expenditure on education has remained close to six per cent of GDP during the period of 1990-1999; except in 1995 when it dropped to 4.55 per cent, the year when the economic reform programme started and total government expenditure was only 26.7 per cent of GDP as compared to over 30 per cent during other years.

TABLE (11)  
EXPENDITURE ON EDUCATION, 1990-1999  
(AS percentage of GDP)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
Education expenditure	4.89	5.68	5.61	5.76	5.52	4.55	5.10	5.23	6.74	6.00

Also in 1999, education expenditure 19.62 percent of the total government spending remained, as it was 19.7 per cent in 1993. Around 85 per cent was recurrent expenditure, leaving only 15 per cent targeting for investment and maintenance. Moreover, the major portion of the recurrent expenditure went towards salaries and the rest was allocated for goods and services. Such an insufficiency in investment in the education sector inevitably leads to a low standard of educational staff, low quality of school premises, and limited capacity of admission. The number of school

classroom, and teachers in both basic / formal (primary) and secondary has increased at remarkable rates over the past several years.

As seen in table (12-A), from 1991/1992 to 1997/1999, the number of primary school increased from 8,533 to 11,520. The number of classrooms did not increase steadily every year, but it increased, nonetheless by 28 per cent in the five – year period, from 63,569 to 81,517. The number of primary school teachers grew at a higher rate of 87 per cent from 63,569 in 1991/1992 to 81,517 in 1996/1997 and to 90,661 in 1998/1999. The expansion of secondary education was more remarkable. With the increases of school and classrooms at 136 percent and 100 percent respectively in the same five-year period. Moreover, the number of secondary school teachers went up from 5,753 to 16,672 at a growth rate of 190 percent, from 1991/1992 to 1996/1997 and to 13,818 in 98/99 (table 12-B).

Student enrolment also rose. The 1994 census indicated that 55.04 per cent of the children aged between 6 and 15 were in formal education, the enrolment ratio was up to 73.45 per cent in 1997. Nevertheless, the enrolment of student between 16 and 18 years of age in secondary education was only 26.17 per cent in 1997, far below the world standard.

As for primary – school children, enrolment dropped in 1992/1996, compared to the immediately preceding years, but rose immediately afterwards in both cases. As of 1996/1997, 60 per cent more students attended primary schools as compared to 1991/1992. In particular, the 36 per cent increase of enrolment from 1995/1996 (2,42,472 pupils) was faster than the growth rates of classrooms and teachers. Thus, the number of students per classroom and per teacher, which are indicative of the quality of education, increased in 1996/1997. Nevertheless, these numbers have shown a declining trend in general, suggesting that primary education has been improving.

Enrollment in secondary schools has been steadier than that of primary schools. The figure for 1996/1997 (320,902 pupils) was double that of 1991/1992 (154,800 pupils), and it increased to 323,124 in 98/1999. Recent movement of student /classrooms and student /teacher ratios show similar patterns to those observed in the case of primary education: a decline in general. In particular, there were 19 students on average per teacher in 1996/1997 compared to 27 students in 1991/1992, amounting to a 28 per cent reduction, but it increased to 23.4 in 98/1999.

Despite the noticeable progress made recently in primary and secondary education in general, there is still a need to increase access to and improve the quality of education: adult illiteracy remains high: 62 per cent of adults were considered to be illiterate according to the World Bank estimate in 1997. The number of admittance to both basic and secondary education is increasing at estimated annual growth rates of 3.2 percent and 4.2 per cent respectively. However, around 63 per cent of students enrolled in the first years of basic education drop out before completing the ninth grade. About 45 per cent of those enrolled in high schools drop out before reaching the twelfth grade and obtaining the diploma. The deficiency in the absorption capacity of the school system and the lack of awareness of the importance of education seem to explain this tendency.

The need for better public education is particularly urgent for under –served population, which tend to be female, rural, or both. Nationwide, 37 percent of the adult men and 74 percent adult women are illiterate. Although the literacy rate in the country as a whole is 44 percent, it differs between rural and urban areas. Literacy is significantly lower in rural areas, with only 15 per cent of females and 58 percent of males are able to read and write, then in urban areas where 52 per cent and 77 per cent, respectively, are literate. This is no surprise as over 50 per cent of the student population is located in urban areas though 77 per cent of the total population lives in rural areas. Few teachers are willing to work in rural communities, preferring to stay in cities in which there is a greater demand for teachers and working conditions seem to be better.

Gender imbalance in school enrolment is acute. Gross enrolment rates in rural areas reveal that educational opportunities for girls, 18 per cent of whom are much more limited than for boys, 55 percent of whom attend school. On the nationwide average, 80 percent of male children, and

only 39 per cent of female children attend primary school. The disparity between the sexes gets even larger with each successive education level: there twice as many boys as girls in the first grade, three times as many in the sixth grade, and more than six times as many in the ninth grade.

The Government has approved a reform programme calling for improving the quality of primary and secondary education, increasing the number of females enrolled and expanding education facilities in under-served areas. A new education law has also been passed, introducing compulsory basic education for a nine-year cycle. However, to enforce the new initiatives, community participation is crucial, particularly beyond the primary level. The Education Sector Management Reform Project recently initiated by the Ministry of Education attempts to improve the capacity of education authorities at the Governorate level in order to become involved in the planning decision-making, and implementation of education.

TABLE (12-A)  
SCHOOL ENROLMENT AND NUMBER OF SCHOOLS, CLASSROOMS AND TEACHERS IN  
BASIC/FORMAL SCHOOLS, 1991-1999

	1991/1992	1992/1993	1993/1994	1994/1995	1995/1996	1996/1997	1997/1998	1998/1999
Enrolment	2059 492	2011 724	2400 836	2493 017	2425 472	3294 241	2522924	2579897
Number of School	8533	8097	9488	9579	10 007	10 158	10820	11520
Number of Classroom	63569	61 200	73 233	78 789	76 344	81 517	88942	90661
Student /classroom Ratio	32.4	32.9	32.8	31.6	31.8	40.4	28.37	28.46
Number of Teachers	524 96	58 627	70700	78 646	85 688	98 336	108074	122577
Student/teacher Ratio	39.2	34.2	34.0	31.7	28.3	33.5	23.34	12.05

TABLE (12-B)  
SCHOOL ENROLMENT AND NUMBER OF SCHOOLS, CLASSROOMS AND TEACHERS IN  
SECONDARY SCHOOLS, 1991-1999

	1991/1992	1992/1993	1993/1994	1994/1995	1995/1996	1996/1997	1997/1998	1998/1999
Enrolment	154800	150856	194663	232506	254255	320902	294369	323124
Number of school	815	852	912	1224	1396	1924	2196	2309
Number of classroom	3616	3630	4692	5678	6061	7232	8573	9076
Student /classroom ratio	42.8	41.6	41.5	40.9	41.9	44.4	34.34	35.60
Number of teachers	5753	7292	8617	11130	11469	16672	5894	13818
Student/teacher ratio	26.9	20.7	22.6	20.9	22.2	19.2	49.94	23.38

#### (e) Health Care

Infant mortality rates fell from 93 per 1,000 live births in mid-1990 to 80 per 1,000 in 1997, a decline of 14 per cent in seven years, indicating a steady improvement in general health conditions in the country. During the same period, life expectancy increased from 57 to 58 years, though it remains the lowest in the ESCWA region.



Despite such remarkable achievements, there is a shortage of public health services and a lack of essential drugs. The poor state of the country's current health care system is obvious from the following indication: (a) only 45 percent of the total population have access to health services: (b) a high rate of 42 to 73 percent of patients per area are passed on to expensive private health facilities due to the lack of services in government facilities: and (c) an immunization coverage reached only 28 per cent of the overall population. About one million cases of infection were reported among the 16 million in 1997 and about 41 percent of the entire population is estimated to be suffering from some kind of disease.

Lack of financing, poor organizational and managerial structures, and inadequate training of health care personnel have led to difficulties, particularly, in reaching rural residents. Merely 30 per cent of the rural population on average have access to health care: worse yet, public medical facilities in many of the rural areas are almost non-existent. Also many peoples who live in highly scattered communities throughout the rugged countryside cannot afford the added cost of commuting to distant health care facilities. As a result, over 6,000 people die every month from malaria, enteritis, dysentery, respiratory diseases, typhoid, hepatitis B, and other illnesses. In addition, maternal mortality among the highest in the world, at an estimated rate of 1.000 per 100.000 births.

The Government has made it a priority to establish more effective health services and provide them to the most needy segments of the population. As in the case with the primary and secondary education, the government has maintained a steady expenditure-to-GDP ratio for primary health care since the beginning of the FFYP implementation. Thus, the number of physicians in the country increased from 3,220 in 1995 to 3,800 in 1997, and the number of dentists from 206 in 1995 to 256 in 1997. During the same period, the number of hospitals beds also increased, from 93 to 96 and from 10,700 to 110,074, respectively.

However, the magnitude of health care expenditure is still small and inadequate, accounting for only 4.5 and 3.8 per cent of the national budget in 1998 and in 1999 comparing to 4.0 and 4.5 in 1991 and in 1992 respectively. Also the expenditure as a percentage of GDP is still small accounting for only 1.24 percent in 1999. The figure is considered to be extremely low when compared to other developing countries. In consequence, 75 per cent of government health care costs are covered by personal contribution of the households, while the Government contributes the remaining 25 percent.

Recurrent expenditure typically constitutes most of the total national health budget: for example, more than 85 per cent of the 1997 budget was for recurrent expenditure, leaving only less than 15 percent allocated for investment. In addition, wage costs constitute a large portion of operative expenditure, and thus there are limited resources for non-wage items, such as equipment, maintenance, and supplies. Hence, distortion in the allocation of public funds has exacerbated the low quality of public health care services.

To address the failure of the country's health care system, the Ministry of public Health has put forward a Health Sector Reform Strategy. The long-term objectives are to achieve: (a) adequate and universal access to health care services: (b) equity in both delivery and eventually the financing of health care: (c) enhanced allocation and technical efficiency of the service delivery system (d) improved quality of health services: and (e) long term financial stability in the system.

The Reform will take place in two phases. Initially the key aspects of the reform will be focused on lessons learned, key legislation passed, revision of the financial system initiation, and major actors brought on board. A five-year consolidation phase will follow, in which the lessons learned in the initial phase will be fashioned into long-term systems, policies, and regulation. In addition, at least 40 per cent of districts will be integrated in to the District Health Systems, (DHS) in the first phase and the remaining 60 per cent will be integrated in the second phase. Key innovation of the DHS approach, in which a district will be the basic unit of service provision, are managed by team work, not individuals, community participation and management decentralization

to the district level. The initial phase coincides with the end of the FFYP for the years 1996-2000, followed by the beginning of the consolidation phase in year 2001, which will coincide with the Second Five Year to be implemented in 2001-2005.

**TABLE (13) :**  
**EXPENDITURE ON HEALTH SERVICES,**  
**1990- 1999 (as percentage of GDP)**

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
Health Expenditure	1.15	1.31	1.18	1.32	1.00	0.86	1.21	1.08	1.60	1.24

### (F) Social Safety Net work

Economic reform programmes continue in the country, but a further negative impact on the country's economy is expected as a result of job losses, acceleration, a decline in the provision of social services, and thus the deterioration of living standards. To mitigate such adversity and protect those most negatively affected, the Government created the Social Safety Network (SSN) to accompany the economic adjustment policies. Element of the SSN include the Social Welfare Fund, the Public Works Fund, the Social Fund for Development, and Vocational Training Programme.

#### 1-Social Welfare Fund

The Social Welfare Fund was established with a budget of YRIs 1 billion allocated in 1996 in order to provide direct support to particularly vulnerable groups such as the poor, the handicapped, the elderly, and dependent women. Under the supervision of the Ministry of Insurance and Social Welfare, the Fund disburses financial assistance to destitute families, who are suffering from the removal of the generalized subsidies on basic commodities and services, which will be eliminated completely by the year 2001.

#### (2) Social Public Works projects Program

This Fund was set up in mid 1996 as an emergency fund under the supervision of the Ministry of Planning and Development and with support of the World Bank amounting SDR 17 million. It assists in creating income –generating employment opportunities for unskilled laborers while at the same time upgrading and rehabilitating environmental and sanitary conditions in the country. The Fund comprises small-scale intensive-intensive civil works projects in country-wide localities ranging from waste management, water distribution systems, road repairs, terracing and drainage works of soil conservation to repair work on health centers and school building. So far, up to 96,000-manpower work months have been generated.

#### 3-Social Fund for Development

Under Law No.10 of 1997, the Social Fund for Development (SFD) was established as an independent institution with funding jointly provided by the OPEC Fund for International Development, and the Government. This nation-wide public institution is to contribute to the Government's efforts towards alleviation of poverty and unemployment in the country, while cushioning the hardships associated with the reform program and inducing greater community participation.

The SFD implements three activities: (a) the Communities Development Programme to finance a number of projects aimed at affording basic social services: (b) the Small and Micro-Enterprise for water Development, and environment, to the most needy communities Programme, to open up the banking sector to small entrepreneurs and facilitate providing them with small capital and the business know-how so that long –term sustainable employment opportunities will be created outside the public sector through straight- forward banking operation, and (c) the

Institutional Capacity Building programme to support the NGOs which are active and effective in their role in drawing up and implementing programmes and development projects.

### III. DOMESTIC OPPORTUNITIES AND CONSTRAINTS

#### (a) Peace and Stability

Yemen's most pressing international issue was the undemarcated border with the Kingdom of Saudi Arabia. During 1996 and 1997, negotiations intensified to reach a solution amicable for both sides. After the historic visit of Crown Abdullah Ibn AbnuI Aziz to Sana'a, who headed large and important Saudi delegates, on the occasion of celebration the 10<sup>th</sup> anniversary of the national day of the reunification, which followed by a successful visit to Jeddah, Saudia Arabia by the president Ali Abdullh Saleh on June 12-13, 2000

In a historic event, which has dispelled tension and potential conflict, Yemen and Saudi Arabia signed an International Land and Sea Border Treaty in Jeddah on June 12 2000. They had defined the borders according to the guidelines laid down by Al-Ta'ef Agreement, as well as agreeing border issues not covered in the agreement, and noted that the Memorandum of Understanding had made a great contribution to a final solution. The International Land and Sea Border Treaty was signed by Yemen's Deputy Minister and Foreign Minister Ba Jammal and HRH Saoud Al-Faisal, Saudi Arabia's Foreign Minister, and attended by President Saleh, Crown Prince Abdullah, and officials from both countries.

Following the signing of the treaty, President Saleh held a press conference. He opened by saying: "We have reached a peaceful, cordial and satisfactory solution that will be protected by the coming generations from Saudi Arabia and Yemen. We have signed a treaty for final and permanent international borders." He added that the main problem had been how to define the borders in Jabal Thar and Ras AL Ma'Wuj, but that it had been "perfectly solved", and that this had been the case with the other borders, from Jabal Thar to the 19th Parallel, and from the 19th to the 52nd Parallel.

Normalization of relations is expected to lead to increase economic cooperation between the tow countries and enhance the stability in the region.

In addition, Yemen and Eritrea agreed to bring the 1995 dispute over the Eriterian occupation of the Greater Hunaish island in the Red Sea to International Arbitration Court, with the supports of France, the tow countries stated their agreement to abide by the outcome of a decision by the international Court. The decision by the International Arbitration Court was in favor of Yemen, which won the case.

Also, Yemen and its neighbor Oman solved their border problem, and the relation between the tow countries is excellent.

In addition, the relation with the Gulf States has improved a lot in recent years, particularly, with Kuwait, which just assigned its new ambassador in Sana'a in May of this year 2000.

Relations with the west are good and have improved in recent years. This was reflected by new Cooperation agreements with the European Union Signed in 1997.

#### (b) Economic Infrastructures

Despite the improvement of the physical economic infrastructures in the past 10 years (roads, ports, airports, water supply systems, power supply, telephones, ...etc.). Still there are less than 10% of the road network are paved, the network does not reach a large proportion of the population, and most of it is in poor conditions. Moreover, electricity from the public grid reaches only about 35% of the population, only about 40% of the population has access to safe drinking water, and telecommunications penetration is still very low outside major cities and rural areas.

The SFYP (2001-2005) is aiming to continue to build a complete basic infrastructure in order to encourage local and foreign investment and to facilitate production, marketing and distribution.

Therefore, it is very important to build the basic infrastructure and enhance the available means through the following policies:

- 1- Enhance and develop the transportation and communication sector by enlarging and modernizing the available transportation and communication means in order to tie all the governants with each other and with the outside world.
- 2- Encourage private and foreign sector to invest in the infrastructure activities.
- 3- Pave more roads in order to tie all governants, districts, and urban areas, which in turn, will ease the supply of public services and encourage investment over all the country.
- 4- Extend energy power capacity and increase the size of the available consumption capacity for production and housing uses and to provide its services to rural areas through more public investment for production and repair power sources and encourage the private and foreign investment in enhancing and developing energy power production.
- 5- Increase the water consumption for both production and housing uses under some measures of water rationalizing.
- 6- Complete the sewage projects in large and small cities in the country in order to avoid water contamination and diseases.

### (c) Policy Reform

The causes of the macroeconomic imbalance during the post-unification period of 1990-1994 were quite straightforward. Large fiscal deficits and their financing through inflationary credit and monetary expansion caused inflation to accelerate and resulted in a loss of confidence in the Yemeni rial. Together with negative interest rates and a lack of investment opportunities, this induced substitution of bank deposits in Yemeni rial into foreign currencies, leading to a rapid depreciation of the Yemeni rial in the parallel market. In order to restore confidence in the domestic currency and stabilize the economy in general, the Government established a set of medium-term adjustment programmes designed to reduce basic monetary and fiscal imbalances during the five-year period 1996-2000.

The macroeconomic goals include a steady increase in real non-oil GDP growth to six per cent a year on average, a reduction in the core inflation rate to about five per cent a year on average, a reduction in the balance of payments deficit, a reduction in the current account deficit to an average equivalent to two per cent of GDP, and the maintenance of sufficient foreign exchange reserves to cover four and a half months of import value.

In support of these objectives, the programme entails forceful stabilization measures: significant budgetary cuts through the removal of subsidies and price increases; the avoidance of any domestic bank financing of the public deficit; auction sales of government Treasury Bills to allow for non-bank financing; tighter monetary policies; the achievement of positive real interest rates; contraction of aggregate demand; adoption of a floating exchange rate system; and the unification of the exchange rate system; and the unification of the exchange rate.

#### 1- Price adjustment

Several key economic products and services, such as sugar, rice, wheat, flour, milk, edible oil, medicines, gasoline, diesel, kerosene, liquefied petroleum gas, electricity, telephone services, water, and sewage services were subsidized by the Government, through fixed prices to consumers and users. For example, commodities were imported at an official exchange rate that remained fixed at higher rates, such as US\$ 1=YR1s 96 for wheat and US\$ 1=YR1s 92 for wheat flour, while the Yemeni rial depreciated in the parallel market. Thus, the Central Bank was essentially financing the subsidy costs. Such intervention was introduced for the purpose of providing basic necessities at low prices to the country's most vulnerable groups during the economic hardship in the period of 1991-1994. In addition, to a certain degree, subsidizing energy prices to domestic industries and agricultural activities.

However, the subsidies had not only become too costly but also resulted in distortions in resource allocation at the macroeconomic level, especially as the subsidized prices of commodities were set at levels significantly below their economic costs. In particular, the low prices of subsidized items, such as electricity, petroleum derivatives, water for industrial and agricultural uses, led to excessive use of these goods and services, overburdened the government budget, and exacerbated environmental degradation.

In order to remove the distortions, substantial price adjustments were introduced and most subsidies have been gradually lowered or eliminated since the beginning of 1996. Thus, the Ministry of Finance projects that the total expenditure on subsidies would be down to US\$ 120 million in the 1998 budget. After the elimination of a subsidy on one of the key commodities, wheat and wheat flour, in 1999, there is only one item left that is still subsidized which is diesel.

## 2- Reducing inflation rate

The inflation rate measured by consumer price index (CPI) rose sharply during 1991-1995. A five-year average inflation during this period recorded 38.4 per cent in Sana'a, with the peak at 58.5 per cent in 1995, while a five-year average inflation in Aden was 44.4 per cent. One main cause of such high rates of inflation was the monetary financing of the central government deficit, which was precipitated by the country's unification and the 1994 civil conflict. Another factor was the sharp depreciation of Yemeni rial (YRI), which significantly worsened from mid-1994 to mid-1995.

Large increases in the prices of fuel, power, water, and wheat produced a major inflation spike in January 1996, soon after the Government started implementing the gradual elimination of subsidies on these goods and services. However, prices in general remained relatively stable for the rest of the year. In fact, the core inflation rate, which excludes the effect of large increases in administered prices, fell sharply under the concurrent contractionary monetary policies. Thus, general inflation also fell nationwide from 56 per cent in 1995 to 30 per cent in 1996, and further down to 5.4 per cent in 1997. The Government's objective to reduce inflation to an annual rate of 7 per cent during the FFYP period was successfully met.

## 3 - Monetary policy

The EFARP's monetary policy goals were: to attain a significant reduction in inflation, establish the conditions for bank re-intermediation, and enhance confidence in the currency in order to attract increased inflows of remittance and private capital into the economy.

### (a) Money supply

In addition to the Government's restrictive fiscal measures under the EFARP, the Central Bank of Yemen (CBY), in December 1995, offered Treasury Bills to the public for the first time in its history in order to establish an alternative source for government budget financing from the private sector, absorbing excess liquidity, and to broaden the availability of rial-denominated financial instruments. By the end of 1996, the nominal value of Treasury Bills sold in auction amounted to 15 per cent of the total money supply. The CBY continued the auction in January and February 1997, with the total nominal value of YRI 8.987 million. Starting from March 1997, the CBY auctioned three-month Treasury Bills. With the practice proven to be successful, it now auctions 30-, 90-, 180-, and 360-day instruments to private investors. The Treasury Bills sales to the non-bank sector, which not only led to a reduction of the Government's debt to the domestic banking system, but also served to establish a market rate through the interaction of supply and demand.

Money supply growth was modest at a rate of 8.6 per cent annually in 1996, about one-sixth of the annual growth rate of 48.5 per cent in 1995 and less than one-third of the annual growth rate of 31.7 per cent in 1994. The CBY continued to maintain its tight monetary policy and the money supply grew at moderate rates of 10.7 per cent a year in 1997 and 11.7 per cent in 1998 (table 14).

**TABLE (14)**  
**MONEY SUPPLY AND GROWTH RATE, 1991-1998**

	1991	1992	1993	1994	1995	1996	1997	1998
Broad money (Billion Yrls)	79.3	79.2	127.0	167.2	248.3	269.6	298.4	333.4
Growth rate	-	22.6%	30.7%	31.7%	48.5%	8.6%	10.7%	11.7%

#### (b) Floating exchange rate

The official exchange rate of the Yemeni rial was about four times higher than the parallel market rate (US\$1=YRI 12.01 versus US\$1 = YRI 46.75) at the beginning of 1993. The gap continued to widen and, in mid-1994 during the civil strife, the official rate jumped to ten times higher than the parallel market rate (US\$1=YRI 12.01 versus US\$1=YRI 119.00). The Government devalued the Yemeni rial to US\$1=YRI 50.04 in the first quarter of 1995 and maintained this exchange rate throughout the year. This correction, applied to customs evaluation, was expected to have generated additional rial revenue on an annual basis of YRI 10.3 billion in oil exports and YRI 8.3 billion customs revenues. However, the official exchange rate still remained two to three times higher than the parallel market rate until the end of 1995.

The Government began 1996 by removing all controls on the exchange rate. On January 1, 1996, the Government floated the rial for all private sector transactions under its exchange system reform, while continuing to apply the official rate of exchange to budget accounting, transactions between the Ministry of Finance and the CBY, and customs valuation. By mid-1996, however, multiple exchange rates were eliminated when the Government fully unified all exchange rates at the level of the floating rate in order to restore the market-clearing role of the exchange rate and promote efficient markets and external competitiveness.

The Yemeni Government also adopted a policy of pursuing exchange rate stability through strongly disciplined fiscal and monetary policies. Under the successful implementation of these policies, the Yemeni rial became fully convertible and the parallel market exchange rate remained remarkably stable at the general range of YRI 160 per US\$ for the last three years.

#### 4 – Fiscal policy

The Government's budget deficit has remained relatively large since 1991 and averaged around 15 per cent of GDP in 1992-1994. The large government wage bill, accounting for closely to sixty per cent of current expenditure, together with military expenditure, continued to compress development expenditure, which comprised only three per cent of GDP, in 1993 and 1994.

The Government set up its 1996 budget objectives and implemented several discretionary fiscal measures to reduce the cash deficit: to reduce recourse of domestic bank financing and instead secured domestic non-bank resources; restricted certain non-development outlays through containing the overall government wage bill, eliminating general subsidies, and phasing out support to public enterprises, while allowing for an increase in development expenditure such as the investment in infrastructure; and to achieve and maintain fixed expenditure-to-GDP ratios for social sectors, particularly in primary health care as well as primary and secondary education.

As a revenue-enhancing measure, the tax base was expanded when new production and excise taxes were introduced. Implementation of the income tax reforms undertaken in 1996 and the introduction of a general sales tax system during 1997 were also expected to increase the budget revenue. In addition, replacing import restrictions by the *ad valorem* tariff would provide more revenue to the Government.

#### 1. Government budget

In the first half of 1996, the Government passed a budget, under the auspices of the IMF and the World Bank, which targeted a 1996 deficit to be 3.8 per cent of GDP. This reasonably

transparent budget helped reinforce the concretionary monetary measures introduced in 1995. Furthermore, the economic reform programme under the IMF ESAF/EFF specified that by reducing and eliminating subsidy outlays as well as containing the wage bills, the budget deficit should be cut to 2.5 per cent of the GDP in 1997 and 2.2 per cent in 1998. But the reform program was successful in reducing the budget deficit in 1998, since the budget deficit was 1.9 % of GDP in 1998 (in 1997 the budget deficit was 3.6).

As shown in table (15) below, the budget deficits were over 10 per cent of GDP until 1994 and were reduced to 5.9 per cent in 1995, and to only 0.1 per cent of GDP in 1996.

TABLE (15)  
GOVERNMENT FISCAL STATUS AS PERCENTAGE OF GDP, 1991-1999

	1991	1992	1993	1994	1995	1996	1997	1998	1999
Government revenue	26.0	18.7	17.3	15.8	20.8	35.2	40.4	47.4	27.9
Government expenditure	30.1	31.2	31.2	32.2	26.7	35.3	41.5	49.4	31.8
Budget deficit	4.2	12.5	14.0	16.3	5.9	0.1	3.6	1.9	3.9

In addition to the tight fiscal policy introduced in 1995 when government expenditure was reduced to 26.7 per cent of GDP, such remarkable reductions of budget deficits were also due to large increases in Government revenue. In January 1995, the official rate of exchange applied to budget accounting was devalued by more than four times. Subsequently, by mid-1996, the Government fully unified all exchange rates at the prevailing level of the floating market rate, which led to a further depreciation of the Yemeni rial. This exchange-rate-related factor brought windfall revenues. Moreover, relatively high world crude oil prices during the concurrent period resulted in higher-than-expected oil export receipts and exceptional payments from foreign oil companies. Hence, there was a fiscal surplus for the first half of 1996, and the year ended with a small deficit of YRIs 464 million. A large increase in the government expenditure in 1997, at a nominal rate of 34.5 per cent, put the government budget into a deficit at 3.6 per cent of GDP, despite the 29.2 per cent growth in the revenues from 1996.

The share of oil revenue in the total current government revenues, exclusive of that of capital and investment revenue increased from 5.68 per cent in 1994 to 11.05 per cent in 1995 and to 17.81 per cent in 1996. It is also estimated to have contributed to 50.77 per cent of the total current revenue in 1997. However, a significant drop in world oils prices and their continuous declines since the end of 1997 resulted in a huge reduction in the 1998 government revenue. Preliminary results show that oil export revenue in 1998 was US\$ 445 million, a 63.per cent reduction compared to US\$ 1.2 billion in 1997. As a result, the deficit-to GDP ratio worsened in 1998 to 5.8 per cent.

The 1999 budget was prepared based on an oil price forecast of US\$ 12 per barrel. As of February 1999, oil prices were still lower and thus oil revenue was expected to be lower than planned, which, in turn, affected the Government's budget position adversely. However, world oil prices have since then recovered and are expected to average higher than initially forecast by the Government. Thus, the Government's revenue increased.

#### Balance of Payments

The balance of payments of the country traditionally suffered from fundamental weakness of its economic structure, such as dependence on private transfers, a limited export base, and volatile crude oil export revenue, and from expansionary demand policies that maintained high volume imports relative to exports. Balance of payment deficits were financed mainly by printing new money.

### 1. Trade balance

The negative impact by neighboring countries following the Gulf Crisis of 1990-1991 included the closure of their markets to Yemeni exports. Consequently, the trade balance swung into a massive US\$ 971.3 million deficit in 1993. The value of exports was less than half of that of imports during this immediate post-unification period. In 1994, exports grew at a rate above 50 per cent from the 1993 level. In particular, crude oil exports almost doubled as shown in table (16).

TABLE (16)  
TRADE BALANCE, 1992-1998 (In millions of US\$)

	1992	1993	1994	1995	1996	1997	1998
Exports	1066.2	1166.8	1796.2	1980.0	2262.8	2264.0	1145.2
Crude oil	819.5	833.6	1615.4	1735.0	1976.2	1934.9	930.2
Oil products	141.6	178.8	77.8	133.0	209.8	199.2	102.3
Non-oil exports	105.1	154.4	103.0	112.0	76.8	129.9	112.7
Imports	(1935.5)	(2138.1)	(1522.0)	(1831.0)	(2293.5)	(2406.5)	(1674.4)
Crude oil and products	(138.1)	(165.4)	(207.9)	(172.0)	(176.5)	(165.3)	(84.9)
Oil and gas sector	(370.3)	(426.6)	(172.8)	(114.0)	(95.9)	(84.5)	(54.4)
capital goods							
Others	(1427.1)	(1546.1)	(1141.2)	(1546.0)	(2021.1)	(2156.7)	(1535.1)
Trade balance	(869.3)	(971.3)	274.2	149	(30.8)	(142.5)	(529.2)

( ) Indicates negative.

Meanwhile, on the import side, non-food items declined by 31.8 per cent from 1993 to 1994. As a result, the trade balance moved to a surplus of US\$ 274.2 million in 1994. However, the trade balance deteriorated from 1994 to 1995 with imports growing twice as fast as exports in the following years. Furthermore, with food imports growing at 33.3 per cent from US\$ 687.0 million in 1995 to US\$ 915.5 million in 1996, it plunged back to a deficit in 1996. While the food imports in 1997 remained basically the same as those in 1996, the gap between export and import values widened due to a 12 per cent increase in non-food imports.

Due to the heavy dependence of Yemeni exports on oil, the country's economic performance is vulnerable to external shocks. The economic crisis in South-East Asia has direct adverse ramifications in the economy since about 95 per cent of Yemeni exports are oil exports and 76 per cent of them go to non-Arab Asian countries.

### 2. Current account

When the trade balance registered the largest deficit in the country's history in 1993, the current account deficit also reached a peak of US\$ 1,247.8 million. However, it moved positively in 1994. Not only the improvement in the trade balance, by US\$ 1,245.5 million, from a deficit of 971.3 million to a surplus of 274.2 million, but also the improvement in net service exports, by US\$ 310.0 million, from negative 866.3 million to negative 556.3 million, contributed to such a quick recovery. Since then the country has been running current account surpluses; US\$ 235.4 million in 1994, US\$ 194.0 million in 1995, US\$ 106.3 million in 1996, and US\$ 25.3 million in 1997.

### 3. Capital account

The capital account deficit set a high record in 1994 and has remained sizable; US\$ 841.0 million in 1994, US\$ 826.0 million in 1995, and US\$ 397.1 million in 1996. These large deficits essentially reflected the country's large amortization obligations on medium and long-term loans as shown in table (17) below.

However, the capital account of the country moved to a surplus of US\$ 24 million in 1997 as



its amortization obligations were drastically reduced to less than a third of the 1996 level, when the country successfully negotiated the write-off of some of its outstanding debts. As of September 1998, the deficit moved back to US\$ 184 million. Nevertheless, the negative figure was primarily due to trade-related factors.

**TABLE (17)**  
**STATUS OF MEDIUM AND LONG-TERM LOANS, 1992-1998**  
(In millions of US\$)

	1992	1993	1994	1995	1996	1997	1998
Medium-and long-term loans (net)	(761.8)	(787.4)	(684.6)	(694.0)	(520.7)	(66.4)	(86.4)
Disbursements	160.6	129.0	82.1	53.0	138.3	151.7	81.6
Amortization obligations	(922.4)	(916.4)	(766.7)	(747.0)	(659.0)	(218.1)	(168.0)

() Indicates negative.

Due to the large capital account deficits, the overall balance of payments continued to be negative until 1996 in spite of the current account surpluses maintained since 1994. The overall deficit was about US\$ 674 million in 1994, US\$ 553 million in 1995, and US\$ 393 million in 1996.

#### (d) Conducive Environment for Private Sector Development

The root of economic difficulties in the country is not restricted to macroeconomic management, but rather lies in more fundamental infrastructure of the economy. Therefore, the Government has launched structural reform programmes to complement macroeconomic stabilization, focusing on longer-term changes in the legal, regulatory, and policy environment of its economy. These reform programmes seek to achieve structural transformation of the productive sectors and increase the efficiency of resource allocation by reforming public-sector inefficiencies, reducing state domination, and establishing policies conducive to improving the climate for private-sector investment.

The Government's structural reform priorities include: major improvements in the tax system; the elimination of subsidies; reform of the civil service and customs administration; legal reform to enhance banking system intermediation; financial sector reform focused on indirect monetary control, the quality of the banking system and prudential supervision; trade liberalization, tariff reform, and harmonization of excise taxes; multi-sector privatization; liquidation of State-owned enterprises; and major liberalization of the investment and regulatory framework to further enhance private sector investment and activity.

In addition, the Government expenditure is to be re-oriented toward social development and public investment in infrastructure in order to implement the reform with the minimum negative social impacts.

##### 1- Tax system reform

In addition to an upward adjustment in some excise and sales taxes that had been envisaged in the 1995 budget, the Government initiated a broad-based structural reform of the indirect and direct tax systems in 1996. Following a large increase of 90.65 per cent a year in the total tax revenue in 1995, which was probably a rebound to the reduced collection due to disruption by the 1994 civil strife, the total tax revenue grew by 51.06 per cent in 1996. As seen in table (19) below, this large increase was primarily attributable to a jump in the indirect taxes collected, which increased by 118.17 per cent, and in the direct taxes collected, which increased by 42.31 per cent.

Compared to the result of 1996, a growth rate in the Government's tax revenue in 1997 was smaller, yet still significant, at 18.99 per cent. Income and profit taxes marked notable growth at

30.23, 35.4 per cent in 1997 and in 1998 respectively as a result of simplified collection methods and increased efficiency in tax assessment measures. On the other hand, indirect taxes increased only modestly at 15.53 per cent in 1997.

Motivated by the drive to boost Government revenue as projected in the 1999 budget, new amendments to Income Tax Law No. 31 of 1991 have been introduced. In order to broaden the income tax base, and to improve compliance, the amended measures include consolidation of all income for tax purposes, rationalization of rates, brackets, exemptions, deductions, and income coverage, as well as bank provisioning. Primarily affected sources of income are salaries and other payrolls, revenue from rented real estate, and profits from commercial and industrial activities. The new law is expected to lead to more than doubling of Government revenue from payroll taxes, which are the most effectively collected, reaching up to 82 per cent of the total tax base compared to less than fifty per cent of its tax dues collected in general.

Amendments to the existing Production, Consumption, and Services (Excise) Tax Law were introduced in 1998, to broaden the indirect tax base, improve tax compliance, eliminate cascading, increase tax efficiency and neutrality, and improve incentives. In addition, a draft General Sales Tax Law, which replaces production tax with the basic rate often per cent for general goods and services, and zero rating for exports, is expected to be approved by the Parliament and put into effect by the beginning of the year 2001.

TABLE (18)  
GROWTH OF TAX REVENUE, 1991-2000 (In percentage)

	1991	1992	1993	1994	1995	1996	1997	1998	1999	*2000
Direct taxes	38.81	30.61	28.49	20.79	42.31	44.72	28.86	34.92	18.14	2.45
Indirect taxes	31.34	5.03	19.80	1.58	118.17	53.43	15.53	(7.61)	8.32	11.09
Total tax revenue	33.23	11.79	22.48	7.80	90.65	51.06	18.99	4.34	11.89	7.78

\* Estimated Data.

( ) Indicates negative.

## 2- Trade Liberalization

The country's trade regime had been primarily geared toward protection of highly import-dependent, import-substituting industries. Restrictive trade policies included: (a) use of quantitative restrictions to protect local producers and export restrictions to protect local consumers and users; (b) the tariff structure in which tariffs were highest on final goods, lower on intermediate goods, and still lower on production inputs; and (c) an overly-complex and inefficient customs administration based on a process requiring fifty signatures to clear goods and with few controls in determining the value of commodities or length of time to clear them. In addition, poor administration of duty rebate and related programmes aimed at encouraging exports as well as the high freight costs due to a low volume of trade in most Yemeni ports had resulted in a strong bias against export-oriented firms.

In order to promote diversification of the economy and to provide improved incentives for exports and higher value-added processing industries, the Government completely eliminated import licensing in 1996, removed export controls and restrictions, replaced import bans with tariffs, and streamlined customs clearance procedure.

Under the tariff reform, the number of tariff bands as well as tariff rates were substantially reduced to four bands and the rates were to be between five and twenty-five per cent *ad valorem*. A five per cent tariff rate is imposed on medicine, food, and raw materials, while a higher rate often; fifteen, or twenty-five per cent is imposed on intermediate or finished goods. In addition, the Government has instituted an excise tax on industrial inputs and a production tax on local manufacturers to create a level playing field between imported goods and domestically produced counterparts.

### **1. Aden Free Trade Zone**

Until the closure of the Suez Canal for eight years since 1967, the Port of Aden was not only a regional service and distribution center for the Mediterranean region, but also the world's fourth largest port with the capacity to handle 6,300 ships annually. However, it lagged behind during the 1970's and 1980's when neighboring countries in the region generated substantial oil revenue and, equipped with modern facilities for handling containers, entered into the transshipment business. While these competitors became established as regional cargo centers, the Port of Aden's operational capabilities remained at the level of 1960's due to a lack of investment capital.

As one of export promotion measures, the Government passed the Free Trade Zone Law No. 4 in April 1993, and designated 170 square kilometers of land in Aden as the first free trade zone in the country. The Multipurpose Terminal was constructed under the supervision of the Yemen Port Authority. This first alongside berths for large dry-cargo vessels in the port's history allowed Aden to offer container transshipment services.

Being in a prime location to offer container relay services, the Port of Aden steadily grew, measured in the number of total ship calls and the tonnage of bulk, general and containerized cargoes. Its container throughput volume almost doubled from 1994 to 1997. The Terminal not only generated valuable foreign exchange earnings from its transshipment services, but also served to reduce the cost of imports to the country, such as raw materials required for construction and other industries, as well as foodstuffs.

Expanded operations in the Free Trade Zone would contribute further to reducing ocean freight rates and lowering the cost of commodities through an increased frequency of service and a larger volume. Aden's potential to restore its former position as a major service and distribution center seemed promising because of its strategic location, dry climate, clear weather, and ideal geography for a harbor. Thus, in November 1995, a concession agreement was approved to construct and operate a new container terminal and industrial development zone.

The Government signed a contract with a foreign joint-venture company to construct the Aden Container Terminal (ACT), and dredging commenced in the North Shore of Aden Harbor in April 1997. Furthermore, under a terminal management contract signed on October 21, 1997, on a twenty-year build-operate-transfer basis, the Port of Singapore Authority Corp., a private enterprise, took charge of managing and operating the ACT. The project of more than US\$ 450 million investment aimed to have the Terminal's first two berths operational in March 1999. The first phase of the ACT itself is estimated to have created 500-1,000 employment opportunities to local people, suggesting a relatively small impact. However, the significance of this step should be recognized in its potential to expand to the second and third phases as well as the development of an industrial zone, which may create 10,000 to 20,000 jobs in the future.

### **3- Privatization**

A major component of the structural adjustment of economic reform often demands the government's withdrawal from most of the production and services aspects of the economy through privatization of public sector enterprises. Priority should be given to rebalance public and private sector roles in the economy, promote greater efficiency in the allocation and use of resources, improve quality of the services and products, and accelerate private-sector-led growth and investment by providing better business opportunities. In addition, successful privatization would not only generate one-time budgetary revenue but also halt a continuous drain on the national budget.

As part of its comprehensive economic reform, the government initiated its own privatization programme in early 1995 when Cabinet Decree No. 8 broadly defined the general principles and guidelines for privatization. The Government's objectives were to disengage the State from the productive sector; reduce the financial burden on public expenditure; promote widespread private share ownership; and reincorporate the maximum number of public enterprise employees in the

private sector.

To achieve these objectives, the Government set up a Technical Privatization Office to supervise the privatization process based on certain regulations and guidelines. The initial stage of shifting public enterprises to a financially self-supporting basis included granting them the pricing, hiring, and managerial autonomy. It was also in a plan of action to gradually phase out budget transfers to public enterprises and to settle their arrears. By year 2000, the Government aims at privatizing about 70 per cent, measured in terms of employment, of the existing 212 public enterprises. The programme gained initial momentum by focusing on the privatization of smaller enterprises in the tourism sector and the return of nationalized farms to their original owners.

In late 1997, the Government requested IDA support from the World Bank. The proposed support project consisted of three components: (a) an institutional support component that provides technical assistance services and training for the technical privatization office and the concerned ministries managing the project; (b) a transactions component that provides legal and financial advisory services for the preparation of the sale of major enterprise assets, and consulting services to help address any associated policy and regulatory issues; and (c) a programmatic transactions component that provides assistance for the preparation of the sale of smaller assets.

The new phase focuses on expanding the country's institutional capacity for privatization, accelerating the privatization of larger public enterprises as well as smaller ones, and attracting non-local investors, both Yemenis expatriate and foreigners, into the process. The major enterprise considered for privatization were Yemen Air Transport Sector, Yemen Surface Transportation Sector, Yemen Cement Company, Yemen Drug Company, Yemen Telecommunications Sector, and Aden Refinery. In addition, the Ministry of Electricity and Water announced its support for private power generation in Yemen, and wants to add 1,400 megawatts of capacity in the next ten years.

#### (e) Domestic resource mobilization

The moderate growth of the economy has coincided with unfavorable political and economic factors along with large economic imbalances. Investment and its relationship with savings are considered to be one of the most important determinants of economic growth. Furthermore, the domestic resources gap reflects the existing gap between the volume of domestic savings and that of the necessary investments to achieve growth targets. The extent of the gap depends, to a large extent, on the goals that Government seeks to achieve, and hence the volume of necessary investments for achieving the goals. The rate of savings depends largely on consumer behavior, public infrastructure, and investment conditions as well as on supportive economic policies. The rates of savings and investment in country reflect a structural imbalance embodied in the weakness of productive capabilities and high consumption propensities in society as well as unstable conditions that prevailed in the period 1990-94, and which did not encourage stimulating investment.

As table (19) shows, the resources gap reached its peak in 1993 at 30.9% of GDP equivalent to five times its ratio in 1990. This rise is due to the significant increase in total consumption compared with a moderate growth of total investment. Private consumption played a key role in the increase of total consumption since it mounted to 90.2% of GDP in 1993.

The return of a large number of emigrants caused accelerated growth of consumption expenditure. Moreover, increased liquidity in the hands of individuals, whether resulting from savings in or as a consequence of remittances of Yemeni labor during the past two decades, has contributed to boosting consumer propensities.

During 1993 to 1997, the situation improved with the reduction of total final consumption to 77.3% of GDP in 1997 as a result of contracting both public and private final consumption. It is also noticed that the rate of investment expenditure to GDP remained stable during 1995-96 in spite of the decline of the total investment growth in constant prices to 4.4% in 1996 compared to 22.3% in

1995. In both 1998 and 1999 the rate of total consumption remain stable, they were 82.4 and 82.7 respectively. Also the rate of domestic saving was almost stable during 1998-1999.

These changes indicate that the economic stabilization policies which took place since the beginning of 1995 have targeted reducing the imbalance between total domestic expenditure and output (income) through basically pressuring domestic expenditure and specifically private consumption, but not pushing for increased production.

TABLE (19)  
RESOURCES GAP AS A PERCENTAGE OF GDP (1990-99)

Item	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
Gross consumption	92.7	106.2	103.7	110.8	99.4	79.8	84.5	77.3	82.4	82.7
Private	74.8	86.5	83.4	90.2	78.1	81.3	70	61.1	67.6	68.8
Public	17.9	19.7	20.3	20.6	21.3	16.5	14.5	16.2	14.8	13.9
Gross investment	13.2	16.3	19.4	20.1	22.5	25.4	25.4	27.7	32.3	23.8
Gross demand	105.9	122.5	123.1	130.9	121	123.2	109.9	105	115.2	106.5
Resources gap	5.9	22.5	23.1	30.89	21.9	23.2	9.9	5	15.2	6.5
Exports	14.6	14.2	12.6	15	19.1	24.9	40.1	35.3	27.8	36.7
Imports	20.5	36.7	35.8	45.9	37.9	48.1	49.9	41.4	43.0	43.1
Domestic savings	7.3	-6.2	-3.8	-10.8	0.6	2.2	15.5	22.7	17.65	17.30

#### (f) Investment

Investment Law No. 22 of 1991 was issued for the purpose of promoting and regulating the investment of Yemeni, Arab, and foreign capital "within the context of the State's general policy and the goals and priorities of the national economic and social development." Under the Law, foreign investors, Arabs and non-Arabs, are given the same rights as of locals, including 100 per cent ownership of projects, with no conditions of local labor requirements, and no controls on capital flows, and benefit from a series of incentives. For example, a project licensed under the provisions of the Investment Law was exempted from all types of customs duties and taxes for fixed assets imported to establish, expand, or upgrade its operation during the period specified in the license. Upon commencement of production, a licensed project was also exempted from various taxes such as profit tax, real estate tax, stamp tax, business practice tax, other taxes levied on capital, and income taxes imposed on interest on loans and dividends related to the project.

In addition, customs duties were increased on the "imported end-production commodities which are comparable to locally-produced commodities" in order to protect local production for a period not exceeding three years. On the export side, any existing project exported or part of its production was entitled to exemption from all fees and taxes levied on exports, the exemption from production excise or other taxes on exported goods and services produced by a project licensed under the Law, exemption of 50 per cent of tax payable on profits earned from export revenue, and the recovery of all customs fees and duties paid on imported inputs included in the portion of production exports.

Under Article No. 33 of the Investment Law No. 22, a General Investment Authority (GIA) was established in 1992 as an independent juridical entity with autonomous financial status. The GIA executes the provisions of the Law and supervises investment projects. Its functions defined in Article No. 34 of the Law include: (a) to receive and appraise license applications; (b) to issue permits, approvals, and certificates related to project operations and the rights, exemptions, and benefits accorded to them; (c) to obtain, on behalf of project sponsors, all approvals required for

their implementation; (d) to assist projects in dealing with other governmental agencies concerned in order to overcome any impediments or obstacles facing project implementation; (e) to study the laws, regulations, and decrees related to investment in country, as well as regional and international agreements dealing with investment matters and make appropriate proposals; (f) to make necessary appraisals of problematic projects to determine their actual performance and benefit to the national economy; (g) to conduct research related to investment as well as the problems and obstacles hampering effective promotion and orientation of investment; (h) to identify investment opportunities and viable projects in the country and promote them in likely investor circles within and outside the country; (i) to collect and disseminate vital information regarding the investment climate in the country to potential investors; (j) to keep a record of invested capital and review its valuation upon disposal of liquidation for re-export or transfer abroad; and (k) to approve a transfer of net profits and re-transfer of capital abroad based on the results of examining the project's financial position and verifying the compliance by provisions of the Investment Law.

Law No. 14 of 1995 amended the original Investment Law to reduce governmental involvement beyond that envisioned in 1991. Moreover, in early 1996, investment prohibitions applying to certain industrial sectors were eliminated. Investment licensing is also to be eliminated later, except in those instances where investors obtain concessional tax and import duty treatment.

The Government, with the technical assistance from the IMF and the World Bank, undertook a comprehensive review of the investment incentive structure and added an even wider array of amendments in 1997. As a result, governmental involvement in investment decisions was further reduced to assist the setting up of projects, with the role of the GIA changed from that of an approving agency to one of a more facilitating nature, with its focus on investment promotion. Moreover, under the new set of regulations, not only incentives to potential investors were increased through additional tax exemptions, but also the time required for a project approval declined from 45 days to no more than ten days.

Table (20) shows, by sector the profile of 288 projects that were licensed during 1998. Although the Investment Law provides identical benefits to all sectors, the distribution of projects across sectors is quite uneven. More than 50 per cent of them, measured in number, were industrial projects, followed by service-sector projects, which made up 25 per cent of the total. In terms of investment costs, the service sector was the largest, registering YRIs 27.3 billion or 44 per cent of the total, exceeding the industrial sector total of YRIs 23.0 billion. The licensed projects as a whole were expected to create 10,177 jobs, the majority of which were in the industrial (41.5 per cent), service (39.2 per cent), and tourism (12.4 per cent) sectors. Despite the country's long coastal line, fishery has not attracted investors' attention. In order to exploit the country's growth potential based on its rich coastal waters of the Red and Arabian Seas, more concentrated investment promotion must be strategically planned and carried out with special focus on the fishery.

### (g) Governance

The Republic of Yemen was proclaimed on 22<sup>nd</sup> of May 1990, as a result of the reunification between the two previous parts (North and South).

The Unity Agreement, which gave birth to the decoration of the new state, provided - inter alia - for the coming into force of the Constitution Referendum was held on 16<sup>th</sup> May, 1991, where 98.3 % of those who voted said "YES". That Constitution remained in force until 1<sup>st</sup> October 1994, when a number of significant amendments were approved by parliament. Where they aimed toward a more democratic government. According to the constitution, the Republic of Yemen is an Arab and Muslim country. Islam is the state's official religion and Arabic is its official language, Islamic Shariah is regarded as the source of all legislation's. Article 4 of the constitution indicates that, "the people are the source of authority. They exercise this authority either directly through referendum

general elections, or indirectly through the legislative, executive and judicial authorities and through democratically elected local councils".

Article 5 is concerned with the political system of the state. It states that, the Republic's political system is based on political pluralism to facilitate the peaceful transference of authority. The law regulates the rules and procedures that are relevant to forming political parties and organization and the practicing of political activities. It is strictly forbidden to exploit an official status or public funds for the narrow interests of a particular party or political organization.

Article 7 of the constitution, that national economy is based on the freedom of economic activity in the best possible way to serve the interests of individuals and society. It also beholds the principle of fair and honest competition amongst various economic sectors (private, public, mixed, and cooperative). Private property, according to the constitution, must be respected and protected. According to article 40, "all citizens are equal in their rights and public " It also states that, " every citizen has the right to participate in the political economic, social and cultural life. The state guarantees freedom of expression and opinion through speech, writing and / or photography."

Article 24 allows for equal political, economic, social and cultural) opportunities for all people. The constitution regards the family as the basic building block of society. The family must be held by the principles of religion, morals and patriotism.

Women are referred to by article 31 as the beloved second half of men who have their rights and duties. Also, the citizen has the right to resort to courts to protect their rights and legal interests.

Women are given their full rights on par with men by this law. They are allowed full and faire opportunities to vote, and to committee themselves as candidates for parliament. Article 5 state that, the supreme committees will take all appropriate measures to encourage women to exercise their voting rights and will set up women's committees which will be entrusted with registering the names of female voters in the voting registers and verifying their during the balloting process."

On 27 April 1997, the country held its first democratic elections since civil conflict in 1994 and the second since unification in 1990. The elections were considered reasonable and free by international observers and were seen as a substantial step towards fair democracy building. The General People Congress (GPC) won a clear majority of parliamentary seats. Also in 1999, the first presidential election was held.

Since the 1997 elections, government reform has been an important issue for country's democratic institutions. The president has established a consultative council to advise the president on such matters as democrat building, NGOs and other social questions. High on the agenda of the newly- elected parliament are the issues of decentralization and civil service reform. A draft law on local Administration was proposed in 1977, which established elected councils at the district and governorate levels, authorizes the collection of a selected set of tax revenues, and delegates control over local-level development activities. This proposed law resulted in a greater role for private sector and NGOs in carrying out responsibilities related to service delivery.

One of the obstacles that still hinder the development and the consolidation of political practice in Yemen resides in the fact that the society still suffers from high illiteracy. Such obstacle stands against raising political awareness in general and political participation in particular.

Political participation in any society must take place through institutional frameworks that constitute legal channels for political activity. These frameworks are still in the early stages. The political participation process is also limited to the concept of political and social mobilization without reflecting real and effective participation. Thus, restraining political participation to practicing right of candidature and right of voting would not accomplish sufficient interest in all aspects of the political, social and economic life.

In order to encourage and consolidate the role of political participation in society, the Government is seeking to eliminate these obstacles that constrain the political participation process. This can be achieved through reducing or eliminating centralization in the administration, which

hinders the consolidation of the democratic path, Implementing decentralization and issuing the local decentralization.

### Women

Women during the past 10 years have become an effective and interactive partner in all aspects of life including the political activities. Woman has an important role in all developing activities through her interactive in building the society. In addition, to her participation in enhancing and improving the democratic process, whether in the parliament elections or through her role in the political life and in all social activities such as political parties, Unions and Associations.

The latest figures in the education field show that the significant improvement in the numbers of girls in the basic education, where it increased the females number from 516 thousand in 90/91 to 980 thousand in 1999/ 2000, with annually growth rate about 19%.

Also there has been an increase in girls' number in the secondary school, it increased from 20.000 thousand in 90/91 to 94 thousand in 99/2000. Also in the teaching field, where the number of females teachers increased from 9, 869 in 90/91 to 29,610 in 99/2000, despite the fact that, it does not exceeds 20% of the total number of teachers in the year of 99/2000.

The constitution has granted women the right of political participation at equal footing with men. The amended constitution confirms, "All citizens are equal in rights and in public duties."

Hence, women registered significant presence in the parliament elections of 1993 and 1997. However, of the twelve political parties and organizations that participated in the 1997 election, only six of them nominated female candidates to the election.

In respect to women's membership in political parties and organizations, and despite political pluralism in Yemen, women are still in low profile. The importance of the role of women and the extent of participation in public life varies from one party to another, as well as from one governorate to another, reflecting the disparity between the legal and the social situation of the women. Legal regulations and rules guarantee women equal rights as men. However, they tend to collapse in front of the prevailing conditions reflected in the social traditions and family attitudes that limit any broad participation of women in most aspects of life.

These requisites reflect the traditional perspective of the role of women in society that still prevails in the minds of many people. Therefore, there is an evident disparity with respect to the posture on the rights of women. It remains one of the central issues on which positions converge and diverge. The concept of women's rights is a relative concept that varies with changing conditions, situations, and interpretations. Hence, political parties vision and programs have reflected secondary roles for women. This was evident from the eagerness of parties to ensure wider women participation during voting despite a limited female candidature..

The percentage of women registered in the 1997 elections reached 28% compared to 16% in the elections of 1993. Twenty-three women applied for candidature in Parliament in 1997 of which 9 were party candidates. Seventeen candidates fought the election battle but only two became members of parliament. In 1993, 48 women presented their candidature, of which 42 went through the election process. Only two became members of parliament

In spite of what women have achieved during the past 10 years, the Government is aiming to wider the role that should be granted to women's organizations and associations and in all other economic activities in order to achieve integration of women in the path of development. In other words, the government's policies should be concentrated on the following: More equality between women and men in all aspects of lives:

- 1- Increase the percentage of women participation in the labor force.
- 2- Increase the participation of women in the medium and small size projects.
- 3- Increase more training and vocational programs, particularly in planning, accounting, financing, distribution, marketing, advertisements, management ...etc.
- 4- More participation in political activities



## **Environment**

Yemen, like many other developing countries, has witnessed economic and social growth without considering the environment aspect. Hence, and due to institutional and legislative shortages, it currently faces several environment related problems, whether at the overall economic level or at the sector level. Urban growth has accelerated in Yemen, increasing pressures on the limited natural resources to the extent that surpassed the authorities capacity to administer resources in a sound environmental way. Cities currently encounter several problems, of which the most important are:

- Water scarcity and its haphazard depletion.
- Severe shortage of sewerage systems.
- Inefficient collection and disposal of solid waste.
- Weak and chaotic urban planning and lack of balanced urban development.

As for rural areas, in addition to some shared problems, the increase in the size and momentum of natural resource exploitation represented in over herding, wood-cutting, and soil degradation have an effect on the environment.

This situation has seriously led, since the beginning of the nineties, to increase government's concerns, which have materialized in the establishment of the Environment Protection Council in 1990 as well as in issuing the environment protection law in 1995. Moreover, environment issues have been incorporated in the First Five-Year Development Plan (1996-2000), in the national population strategy of 1991-2000 and in the Second Five-Year Development Plan (2001-2005). The mass media has also started to participate in awareness campaigns on environment issues. Also the Scientific Institutions are initiating research relating to the environment. Similarly, some popular initiatives have emerged through non-government organizations concerned about environment protection.

### **(f) Human Resource Constraints:**

#### **Population Pressure on Natural Resources**

Population increase in Yemen creates great pressures that undermine the achievements of the development programs. It also creates pressures on sources of natural wealth and causes several environment problems. Hence, the significant depletion of underground water and the decline of its quality are considered normal consequences of the population increase and of the diverse activities emanating from it. Moreover, the population density has left its prints on land through the excessive use that affects its quality. In rural areas, the depletion of plant coverage due to over herding and woodcutting for fire or construction use, and in quantities that exceed the planting rate creates a hazardous environment situation.

Also, the demand for food and its local production is positively related to the rise in the population growth rate. According to the current growth rate, the responsibility lies on agriculture, animal and fish wealth sectors to undertake the difficult mission of doubling output during a relatively short period not to exceed 19 years, in order to maintain the current levels of self-sufficiency and to provide food for every increasing mouths.

#### **Poverty**

Poverty in the country almost doubled between 1992 and 1998, with the number of households below the "food poverty line" rising from 9% to 17% respectively according to the Household Budget Survey. This is attributable to the depreciation of the local currency, subsidy elimination, and other external factors (influx of returnees and refugees, suspension of foreign aid, impact of regional conflicts). By adding food, clothes, housing, education, health and transport into an "upper poverty line", the percentage of households living in poverty rose from 19 to 33 over the same

period. Hence, poverty is becoming more widespread amongst the 18 million people who live in country's urban and rural areas.

Also, social indicators reflect very low human development. For example, 44% of male and 72% of female are illiterate. Furthermore, 45% of pupils enrolled in the first grade drop out before grade nine. The situation of health is equally inadequate, where only 55% of the population has access to health services. The main findings of the 1998 Household Budget Survey can be highlighted in the following characteristics:

- Government employees have higher incidence of poverty than private sector's employees, which is due to low government wages and to overstaffing in this sector.
- Large household size (6,8 members on average) is perceived as the most important factor in explaining why families are poor, thus supporting the argument emphasizing the strong positive correlation between household size and poverty prevalence.
- the proportion of poor households who are inactive amounts to 16.3%. which is high compared to other Arab Countries.
- Poverty has been always higher in rural areas, and rural household is at 50% higher risk of being poor.
- Female-headed households are more likely to be poor than male-headed household. A female-headed household implies a higher risk of being poor by about 20%.
- Poor people are more likely to be employees or working within a family activity compared to the non-poor who happen to be either employers or self-employed.
- Family ties, kinship relations, and tribal links are strong, and are seen as important elements of the social safety net. Thus, more consideration should be directed to enhance such positive role.

#### Determinants of poverty

Poverty is not the outcome of the economic process alone, rather it is the result of economic, social, cultural, and political factors that interact to either alleviate or deepen the severity of the phenomenon. The major underlying causes of poverty in Yemen can be seen in:

*Population growth:* The population growth in Yemen is among the highest in the world and the total fertility rate (5 children per woman) is more than double the world average. Thus, population doubles every 19 years. Also, more than half the population is less than 15 years of age leading to a high dependency ratio. Also, about 76% of the population lives in rural areas, of which 80% reside in communities of less than 500 people, hence making it very difficult and costly to provide essential services

*Scarcity of Water:* the country's most dependable source of fresh water is the net precipitation. Thus, per capita water supply is about 2% of the world average and 85% below the amount needed for domestic use. Although agriculture depends mostly on rainfall, ground water has reached a state of over-exploitation as a result of over drilling. Moreover, the exhaustion of groundwater will similarly affect the major cities, including the capital Sana'a. Moreover, while the total land area of the country is estimated at 555,000 km<sup>2</sup> (excluding the Empty Quarter), there is limited land for agriculture production, with only 1.6 million hectares (2.9%) of cultivable land, and 2 million hectares of marginal land (3.7%) of the total area.

*Insufficient Infrastructure:* where less than 10% of the road network is paved, the network does not reach a large proportion of the population, and most of it is in poor conditions. Moreover, electricity from the public grid reaches only about 35% of the population, only about 40% of the population has access to safe drinking water, and telecommunications penetration is still very low outside major cities.

*Inefficient Civil Service:* The over-centralized nature of governance and public administration has resulted in the marginalization of regional authorities and led to the underdevelopment of their capacity to plan and implement social and economic development. Moreover, absence of

accountability and transparency created an environment that is non-conducive to private sectors investment.

*The Returnees and Refugees:* The influx of Yemenis returning from the Gulf Countries especially after the Second Gulf Crisis in 1990-91 as well as refugees fleeing War and unrest in the neighboring African countries throughout the 1990s has created additional burden on the ailing economy. The majority of the returnees were unable to bring back their assets hence were impoverished, and many of them have not been able to reintegrate in to the society. Also, such influx created large demand for housing and infrastructure, education and health services, and employment opportunities.

*Gender Perspective:* Illiteracy, immobility, lack of control over fertility, limited access to participation in decision-making, and ignorance about their legal rights; in practice all have reduced the quality of life for women, as well as their potential contribution to raising standards of living.

*Qat related Issues:* Although qat is a major source of rural income, qat plantation consumes between 50-60% of water used for irrigation, which aggravates the water problem. Moreover, pesticide misuse associated with expansion in qat plantation has been increasing tremendously during the last few years with its adverse effect on the environment.

### Government commitment

The government is committed to addressing the underlying causes of poverty and alleviating its effects through several nation-wide programs. There is also an ongoing effort to pull together all anti poverty activities into a National Action Plan for Poverty Eradication (NAPE), which would be most explicit in terms of objective policies, institutional and resource requirements, as well as on the implementation modality.

The implementation of the First Five-Year Plan (FFYP) for the years 1996 to 2000 reflected the shift towards a more pragmatic and development approach in dealing with poverty, as well as highlighted government's social development priorities. The overall objective of the plan was to generate and distribute economic and social development opportunities among governorates in order to reduce the current wide disparities.

However, the FFYP was overtaken soon after its formulation by a comprehensive Economic, Financial and Administrative Reform Program (EFARP), which have been implemented by the government since early 1995 with the support of the World Bank and the IMF as well as the assistance of a broad range of international donors. The EFARP exacerbated the constraints on social development, overwhelmed the traditional/informal social welfare mechanisms, and led to the emergence of poverty from a household phenomenon to a societal problem. Policies and measures adopted to counteract poverty reflected a combination of ongoing efforts to reduce poverty in the long-term, primarily by means of achieving high economic growth, and measures intended to mitigate the short-term adverse impact of the EFARP on the poor and other vulnerable groups.

Moreover, a National Committee for Social Safety Network (NCSSN) chaired by the prime minister was established in June 1998. The main responsibility of this entity is to formulate pro-poor policies, and to ensure that relevant authorities implement them. Moreover, and in response to the need to prepare a PRSP which ought to reflect views and aspirations of the various segments of the society, the government, by means of decree No. 14 for the year 2000, formed (i) a steering committee presided over by the minister of finance and membership of both ministers of planning & development and of insurance & social affairs to oversee the preparation of the interim PRSP (IPRSP), (ii) a technical committee with representation from the relevant line ministries entrusted with the preparation of the IPRSP under the supervision of minister of planning & development.

The regular publication of official reports monitoring poverty in Yemen, which began in 1998, is an indication of government commitment to address the problem. Hence, the ministry of planning & development through the Central Statistics Organization (CSO) is undertaking an ambitious national poverty alleviation survey. In addition, the government has already embarked on

preparing the Second Five-Year Plan (SFYP) for economic and social development covering the period 2001-2005. The plan's overall objective is centered on generating economic growth, creating employment opportunities, and ensuring social stability.

## **- Social Services Provisions**

### **Education**

The constitution of the country states that education is a right for all citizens and shall be guaranteed by the government through building cultural and educational schools and institutions.

Even though literacy rates have improved over the years, illiteracy is still very high in Yemen. There are differences in rural and urban illiteracy rates (64 %vs. 34 % respectively) as will as major differences between genders. These gender discrepancies are also reflected in the actual school enrollment rates. Furthermore, these are significant variations among governorates when it comes to gross-enrolment ratios (GER) for basic and secondary education. 45 % of pupils enrolled in the first grade do not complete the basic education cycle, and the drop-out is greater in secondary schools. Public expenditure on education represented 6.0 % of GDP in 1999.

There has been direct correlation between the construction of new schools and the increase of literacy rates. Over the last twenty years, the number of primary schools tripled, secondary schools are, said to have almost increased twenty-fold. Furthermore, the religious institutions provide parallel education to the official education system in the country.

The remaining high rate of illiteracy rate does however confirm that there is still a great need for improving the quality and quantity of education. On the University level, 90 per cent of graduates are social science student even though science, engineering, and medical faculties exit. As a result, vocational training programmes have become a priority also in the aid program of donor countries.

### **Health**

Yemen has experienced a relative improvement of health services and life expectancy has increased over the recent years. In 1997, the overall life- expectancy rate increased from 57 to 58 years.

The rate of mortality is one of many indicators of any country. Infant mortality (estimated at 81 death per 1000 birth) has declined considerably in the last decade. This rate is still higher than the low – income country average of 64. The major causes of morbidity and mortality in Yemen are communicable diseases, hence preventable.

The delivery of health services is hampered by the fact that about 77% of the population lives in highly scattered communities, which in addition often cannot afford commuting costs to health care facilities. Only 45% of the population has access to health services (25% in rural areas). Over the past two years, approximately 150 private clinics have been opened. Emergency medical services practically do not exist, as there are no public ambulances services. The population per doctor is more than 5000 people per doctor. The expenditure on health is 1.4% of GDP in 1999.

### **(g) Industrialization and technological development**

Industrialization in Yemen is not a successful sector as it should be. Manufacturing represents 10% of GDP (including oil refinery), 4% of labor force. During the last decade, investment increased in both public and private sectors, where most of this investment came from expatriate transfers from abroad.

The consumption goods industry, particularly clothes and food, represents a big part of the added value in this sector. Due to the big local market and protection policy, these consumption goods industries gained large profits. The consumption of the text tile industry is low 6.6% of the total added value industry goods; chemical industry (including oil refinery) realized a large growth rate reached 20%, which is the highest rate between all different branches. Building material

industry kept its rate at 21.1%, but wood industry and its products lost part of its contribution at 1995 when its rate reduced to 4.7% due to the stagnation in the building sector.

In general, one can say that industry sector is not successful one, and this may be due to the following reasons:

- 1- Low investment due to the unsecured environment for investment attractiveness.
- 2- The weak infrastructure such as power and water supply, weak net communication and transportation such as roads, transport means, particularly, in the scattered areas.
- 3- The low Per Capita income (\$343) that made the local markets an attractive for large production.
- 4- Most industry projects depend on machineries and raw materials from abroad, which make this industry depends on external factors such as the prices of the machines and input.
- 5- Labor force is characterized by untrained and unskilled, which means labor is not able to work in new industries and modern technologies. Thus, many industries import foreign skilled labor.

Thus, these factors impede industry sector and led to high cost of production, which resulted to noncompetitive prices comparing to the world market prices.

The government policy is aiming to develop and help industry sector especially, private industries and this required:

- 1- More investment should be attracted to the industry sector.
- 2- Introduce more information about industries in the country.
- 3- Create a peaceful environment for investment.
- 4- Develop and complete the basic infrastructures for industries
- 5- Attract local and foreign investment in infrastructure projects, since the government resources are limited
- 6- Build big commercial centers and invest in institutions for training.
- 7- Encourage medium and small industries, especially, outside the big urban areas.
- 8- Strengthening the relations between different industries and National economy sectors such as agriculture.

## V. EXTERNAL OPPORTUNITIES AND CONSTRAINTS

### (a) Official development assistance (ODA)

The total Official Development Assistance (ODA) disbursed in 1997 was US \$ 638.65 million. This constituted a 41.3% increase over 1996. This increase is mainly due to the EEF and the SBA from the IMF and the World Bank, although many of the bilateral donors increased their support to Yemen in 1997.

There has been an increase in aids from the United Nation System, which increased its disbursements by over 73% in 1997, and contributing 76% of the ODA. The IMF disbursement increased by 117%, to US \$304.5 million and the IDA by 39.5 % to U S \$ 145.7 million. The non-UN system multilateral donors decreased their disbursements in 1997 by 56.3 % compared to 1996, but still represented 5 % of ODA. Bilateral donors contributed US \$ 116 million, 21.5% increase over 1996 and representing 18 % of ODA.

The main donors were Netherlands (US\$11 million), Germany (US\$27.5 million), Japan (US\$ 25.4 million), AMF (US\$ 21 million), WFP (US \$ 11 million), UNDP (US\$ 8.8 million), EU( US\$ 8.5million) and France (US\$ 7.3 million).

Of the United Nations system, the largest donor is the IMF, contributing 62% of total UN assistance to Yemen, followed by IDA (30%), WFP (2%) and UNDP (1.8%). It is expected that the UN system will continue to have the leading role in providing assistance to Yemen over the next 5 years.

The shift to a programme approach in the current programme cycle (1997 - 2001) has had major implications for resource mobilization in three important ways: a) a substantial increase in the level of funding; b) flexibility in funding arrangements; and c) promoting financial accountability.

Resource mobilization for the implementation of national programmes and PSDs stands out as a major achievement of the programme modality in the country. In the previous cycle (1992-1996) total programme resources amounted to \$30.391 million while the current level of programme support stands at \$80.3 million. These funds have been raised on the basis of national programme frameworks to which donors and the government has pledged support. The government has pledged: \$2.5 million for the national programme on poverty alleviation; \$1.2 million for water resources management; and about \$ .5 million to environment. This has had an immense benefit in terms of directing funding support to areas of national priority such as water and poverty alleviation in a systematic and sustained manner. Previously, funds would be allocated to ad-hoc projects where once funding support ends there is no clear cut strategy for sustainability of project activities both institutionally and financially.

The effectiveness of the Programme Approach in coordinating donor support is another: value added that generates funding support for the national programmes. The case of the water programme is particularly notable. The programme on Sustainable Water Resources Management is a good example of how the process can create partnerships at all levels and lead to cost sharing. The Dutch are key partners in the implementation of the national programme on water resources. They participated in the formulation phase and continue to be full-fledged stakeholders in other phases of the programme. Recently they have expressed an interest in cost-sharing additional components of the national programme. Similarly, other bilateral such as the Japanese and the Italians have given funding to the Poverty Alleviation programme. Specifically, the Italians are committing \$500,000 to the subprogramme on the Socio-economic Development for Sotora Islands and the Japanese are to support the sub-programme on National Programme for Productive Families for a total amount of \$400,000.

#### (b) External Debt burden

Another major source of balance of payments disequilibrium is the country's huge external debt. The country's total external debt stock at the end of 1994 amounted to US\$ 8.2 billion, equivalent to twice the country's GDP. Of this amount, nearly half was in arrears. The size of debt relative to GDP declined in 1995 but still remained substantial at US\$ 8.7 billion, which was 163 per cent of GDP. The external debt continued to increase, reaching around US\$ 9 billion, more than 180 per cent of GDP in 1996.

The Russian Federation has been the country's largest bilateral creditor with approximately US\$ 5.7 billion debt in 1994 that made up more than two-thirds of the country's total debt. The amount owed increased to US\$ 6.4 billion by the end of 1995, US\$ 3.9 million of which was outstanding arrears. The Russian Federation accounted for about 65 per cent of total debt, and for about 90 per cent of total amortization and interest arrears. The outstanding debt owed to the Gulf States was estimated to amount to US\$ 1.6 billion in 1995.

In principle, the official policy of the government is to remain current on loan payments to multilateral and bilateral creditors and other suppliers of credit. Debt service burdens on country had been substantial. External debt service obligations were typically close to or more than one-third of the Government's budget revenue. Despite the significant progress achieved in domestic economic stabilization immediately after the implementation of EFARP began, the country's external economic performance lagged behind and its position remained fundamentally weak. Given the scarcity of foreign exchange resources, the country fell into arrears. The inability to service external debt obligations continued to erode the country's credit-worthiness and undermine donors' confidence.

The reform programme seeks to avoid compounding this difficult situation through a prudent

external debt management policy; no increase in short-term debt is to be incurred on a net basis, and the contracting of non-concessional medium or long-term debt is to be strictly limited. The reform programme also provided for complete elimination of the existing external debt services arrears by the end of 1996 and the avoidance of any new arrears. In early 1999, the CBY announced that the Republic of Yemen had met all international debt obligations for 1998 to a total of US\$ 160 million.

Resolution of the debt problem in the context of reform would generally improve donors' confidence and thus increased their support. In 1997, the Paris Club creditors agreed to some restructuring and cut the country's burden by up to 67 per cent. At the same time, the Russian Federation forgave the country 80 per cent of its debt and the accrued interest. Furthermore, the Russian Government also signed an agreement to re-schedule the remaining 20 per cent of the country's debt under the Naples Terms in 1998, which allowed 67 per cent of outstanding debt to be written off. Accordingly, the external debt of country was reduced. As of February 1999, its total outstanding debt was US\$ 3.2 billion, constituting 60 to 70 per cent of GDP.

### (c) The export sector

#### Performance of the External Sector

- The deficit in the balance of payments reflects structural rather than temporary imbalance in the economy. This structural imbalance is reflected in limited domestic goods that enter trade exchange (limitation of non-oil exports) due to weakness of the economy's productive capacities. The rapid trade liberalization along with continued smuggling has had a negative impact on domestic production.
- The relative improvement in the current account and consequently in the balance of payments is mainly attributed to a rise in the value of exports (quantitatively and price-wise) and to the relatively stable remittances of Yemenis working abroad.

The decrease in debt will have a positive impact on improving the balance of payments and will provide resources to enhance economic growth. Yet, the balance of payments remains in a critical position due to the structural imbalance between imports and exports, thus requiring to obtain foreign resources (aid and loans) to support the economic reform program and to build the export and production, which in turn, will help in providing a part of productive investment and enhancing the productivity of labor force.

### (d) Foreign Direct Investment

The Foreign Direct Investment (FDI) inflows to the country declined in 1994. Foreign investors moved out of the country due to the militant conflict in the summer of 1994. The negative impact lingered, resulting in the net disinvestments in 1995. Investors seem to be still hesitant to come back as indicated by the second-smallest amount of FDI inflows to the country in 1997. Over the past five years, FDI inflows to the economy have, in fact, declined by 97 percent.

The Government requested the Foreign Investment Advisory Service (FIAS), a joint service of the international Finance Corporation and the World Bank; to conduct a survey of investors in order to learn about their perceptions of the country as a potential investment site.

According to the FIAS survey results, investors found long-term business potential in the areas of (a) transshipment service, container storage, and warehousing in the Aden Free Zone; (b) infrastructure such as power, telecommunication, water, waste management, roads, sea ports, and airports; and (c) renewable resource such as fisheries, food, and beverages – particularly coffee, mutton, and honey. Tourism also attracted the particular interest of foreign investors.

Despite this potential, however, potential investors have taken a "wait and see" attitude, except in the petroleum sector where the investment decision is primarily based on the availability of oil reserves and the exploitation costs. According to those interviewed, impediments to FDI inflows were perceived to lie in the following: (a) difficulties in the area of governance and judicial foundations due to overlapping jurisdiction among different governmental agencies, discretionary application of laws and regulation, under-paid and thus unmotivated civil services lack of protection

for property or contract enforcement; (b) seriously out-dated and inadequate investment law; (c) lingering restrictions on the financial sector and the poor record of the judiciary and enforcement of judgments, and (d) a lack of education, including basic literacy in the work-force, vocational training, and management skills.

In addition, most FDI inflows are known to be recurrent. Therefore the country is faced with a particularly difficult challenge of attracting first-time investors because of its very short lack record as a host country to FDI. Thus, the Government may play a key role to facilitate investment by providing basic information regarding the legal framework for business activity, administrative procedures, resource availability, or business contacts.

#### (e) Vulnerability to Shocks

There are major internal and external events that caused the economic and social situation to suffer great shocks in a short time period. First came the Gulf War of 1990, which brought in its wake the return of about one million returnees from the Gulf States (particularly, from Saudi Arabia and Kuwait). The all-important remittances from these returnees (estimated yearly at \$1 billion) ceased, and most of them became unemployed and poor. In addition, donor interest in Yemen stopped their large aid programs. Second Civil conflict in Yemen followed in 1994, taking resources away from social and economic development. The civil conflict also damaged much of the economic and social infrastructures of the country. The outcomes are: balance of payments deficit, high inflation, large-scale unemployment and increasing international debt which all led the government to adopt a package of structural adjustment reforms with the help of the IMF and the World Bank. These macro economic reforms required large cutbacks in social services welfare and removal of subsidies for basic foods. The results of this program, however, have been very successful.

The economy is heavily dependent on oil exports for income and foreign currency, and thus vulnerable to fluctuations in the world oil market, which are beyond the country's control. For example, due to a surge in world oil prices in 1996 through 1997, the oil export revenue of the increased from 1996 to 1997. However, it has suffered tremendously from the plunge in oil prices to a twenty-year low on average that began from late 1997. Moreover, the current LNG market prospects are grim due to the global economic slow-down and particularly the recession in potential export markets such as India and South-East Asian countries. As a result, the joint venture with France's TOTAL to start up a liquefaction plant has been delayed. The Government is set to implement an austerity programme to weather through this down-turn. Therefore, diversification of the economic structures essential in the long run.

Since the second Gulf War, traditional donors have not come back with the same level of financial commitment as before. As a result, implementation of the reform has been hampered

Also, the regional conflict, particularly in Africa Continent led to thousands of refugees to the country. In addition to, thousands of the Iraqis and Sudanese.

Recently, the government is becoming increasingly concerned about the number of refugees fleeing into the country from the Ethiopian -Eritrean conflict. There are about six hundred refugees have entered Yemen since the latest outbreak of fighting. Twenty thousand refugees are currently in Yemen, and it is estimated that one hundred thousand Africans are living in the country illegally.

Thus, all these refugees add another burden to the country's hard economic conditions



## VI. The Program of Action for The Next Decade (2001-2010)

- A. The Program of Action is derived from both the SFYPD (2001-2005) and from the Yemen Vision 2025, which both aim at moving Yemen from low-income group to middle-income group with diversified economy and social development. This entails raising Per Capita income from \$349 in 1999 to \$700 in 2005 and to \$2100, at least by 2025, which means, it is being doubled every five years. Meanwhile, Per Capita growth is accompanied by diversification of the economy and development of the social structure.
- B. The mission implied by Yemen's Vision 2025 is to provide Yemeni citizens better standard of living and higher economic and social welfare, comprehensively and equitably.
- C. The mission is to be accomplished through a comprehensive development strategy relying mainly on four key factors stated briefly as follows:
- 1- Development and upgrading of human resources as the dynamic factor for growth and information technology economy. Thereby, establishing human resource development as the cornerstone for economic and social development.
  - 2- Diversification of Yemeni economic structure in order to move away from high dependency on oil production and export to diversification of income generation and employment creation through increasing agricultural, industrial, fisheries and tourism shares in gross domestic product.
  - 3- Improving investment attractiveness and competitiveness of the economy in order to be able to mobilize domestic private investments and attract foreign direct investments and technologies, thereby, integrating with international economy on the bases of competitiveness and equity.
  - 4- Export led economy. In line with the new economic direction towards openness and liberal economic and trade policies, it is essential to encourage export oriented investments and economic activities.

Table (20) below shows the expected average real sectoral economic growth rates of the SFYP (2001-2005). The expected promising sectors are; fishing grows by 20 percent, construction by 12.1, mining and quarrying by 10 percent, restaurant & hotels by 9 percent, community, social, and personal services by 8 percent, manufacturing by 7 percent, and agriculture and forestry by 6 percent. The average total economy growth rate is expected to be between 6.5-5.5 percent.

**TABLE (20)**  
**AVERAGE SECTORAL REAL GROWTH RATES OF**  
**THE SFYP 2001-2005 (%)**

Agriculture and forestry	6
Fishing	20
Mining and quarrying	10
Manufacturing	7
Oil refining	5
Electricity, water & gas	7
Construction	12.1
Wholesale and retail trade	7
Restaurant & Hotels	9
Transport, storage, & commc.	6
Financial institutions	7
Real estate business services	7
Community, social, and personal services	8
Government services	5
Oil sector	0.0
<b>Total Economy Growth</b>	<b>5.5-6.5</b>

\* Not included import's duties and bank services charge

D. According to the comprehensive development objectives of both the SFYP (2001-2005) and the Yemen Vision 2025, the main goals of the Program of Action for the next ten years can be determined as follows:

- 1- Achieving an annual rate of growth of real gross domestic product between 6.5-7.5 % in order to be able to double Per Capita income every five years.
- 2- Reducing poverty at a rapid pace so that poverty percentage could be reduced from the present level of 33% to 15% by the year 2010.
- 3- Encouraging massive investments in all sectors of the economy, especially, those characterized by labor intensive technology, in order to create as much employment as possible, thereby, reducing unemployment rate from the present level of 35% to 10% by the year 2010.
- 4- Raising sectoral annual rate of growth within the range of 8% to 10% in order to raise the aggregate economic growth rate, create employment, consequently, approaching economic diversification.
- 5- Preparing the economy to effectively and competitively integrates to the world economy through strengthening economic integration locally, regionally, and internationally.

**E. All those objectives will be nursued though a concrete set of macro and sectoral policies summarized as follows:**

**(a) Fiscal Policy.**

The fiscal policy is viewed vital and decisive in facilitating achievement of mission objectives within the first decade of the 21-century. The main components of the fiscal policy could be stated as follows:

- 1- Mobilizing financial resources domestically and from abroad to secure required financing for investments necessary to achieve targeted growth rates of income and employment.
- 2- Restructuring of fiscal budget components in favor of increasing investments in infrastructure projects, health, and education services Vis a Vis rationalizing expenditures on current activities, with serious emphasis to encores and to improve government revenues from diversified sources.
- 3- Working seriously to reduce budget deficit and maintain it at no more than 3% of GDP.
- 4- Improving tax laws to ensure maximum motives and incentives to private sector to invest and take incentives initiatives in economic activities in order to increase economic growth and create employment opportunities.

**(b) Monetary Policy.**

The monetary policy is directed to enforce growth potentials through the following measures:

- 1- Adopting expansionary monetary policy to encourage private investments to help achieve growth objectives.
- 2- Maintaining macro economic stability in the monetary sector in order to keep inflation at low level, stabilize exchange rate and increase foreign exchange.
- 3- Complete the necessary legislative and executive steps to establish and operate stock market in Yemen.
- 4- Encouraging establishment of specialized credit institutions to provide easy terms credits to women, productive families, poor people, handicapped, rural activities, small industries, and handicrafts.

**(c) Foreign Trade Policy.**

In line with transformation of market economy and liberalization of economic policies, a long with export promotion policies, the foreign trade policy is designed as follows:

- 1- Encouraging and promoting economic activities with export potentials and competitiveness, especially in agriculture, industry, fisheries, and tourism.
- 2- benefiting from bilateral and multilateral trade agreement along with regional free trade zone arrangement to promote exports and attract joint ventures.

**3- Finalizing required steps for Yemen to become a member in World Trade Organization, particularly it has been accepted as a watch member in World Trade Organization.**

**(d) Agriculture Policy.**

The main aspects of agricultural of policy rely on the following:

- 1- Rationalizing water use and improving irrigation methods to limit irrational utilization of scarce underground water.
- 2- Encasing and supporting agricultural research and extension services as well as improving animal endowment.
- 3- Expanding establishment of dams and water reservoirs to maximize water use in irrigation.
- 4- Expanding provision of easy terms credit to small farmers, fishermen, and cooperatives.
- 5- Upgrading and expanding fishing infrastructures including fishing technologies, storage, transportation, marketing, and quality control laboratories.
- 6- Encouraging fish exports.

**(e) Industrial Policy:**

The industrial sector consists of two subsectors: the mining and extraction sector and the manufacturing sector. The policy aims at:

- 1- Encouraging oil and minerals exploration in order to bring into exploitation new flicks of crude oil and some minerals such as gold, copper, iron, silver, zink, and others along with extracting marble and granite stones.
- 2- Insetting in natural gas utilization in electric power generation and household uses.
- 3- Expanding physical infrastructure required stimulating industrial investment means, particularly, electric power, water supply, road network, communication facilities, and others.
- 4- Providing incentives and priorities to industrial investments projects that use local raw and intermediate inputs and characterized by labor intensive technology.
- 5- establishing industrial zones to facilitate locating of small and medium scale industries and micro projects supported by required utilities.
- 6- Provision of easy terms credits for small and medium scale enterprises to create more job opportunities and to help poverty alleviation efforts.
- 7- Setting up strict specifications and quality controls to ensure competitive domestic products.
- 8- Promoting industrial product exports.
- 9- Promoting investments in high- tech and informations based technologies.

### **(f) Tourism Policy:**

Yemen is considered as a touristic rich country with diversified touristic products including historic, cultural, beaches, diving and health care tourism. To promote tourism potential the following policy is adopted:

- 1- Preparing and publishing a tourist map that shows the exciting and attracting points.
- 2- Encouraging private sector to invest in tourism enterprises including hotels, resort means, tourist agencies, and other services.
- 3- Preserving tourist attraction and promoting tourism, both locally and abroad.

### **(g) Social Development:**

This broad sector includes health, education, technical and professional training, human resource development, and safety net.

However, it is quite understood that achieving those goals and objectives is not easy task or merely at hand. In fact, there are several challenges and constraints along the way of the goals and objectives. The main challenges could be briefly stated as follows:

#### **1- Water Scarcity:**

Yemen is considered one of the poorest countries in water resources in the world; water Per Capita doesn't exceed 150 Cubic Meters, which is far below the international average of 7500 Cubic Meters.

#### **2- High Population Growth Rate:**

Population growth in Yemen is once again, once of highest in the world. The annual populations growth rate is 3.5% in 1999, which creates a high pressure on scarce resources that hinders development potential.

#### **3- Low Skills and Capacities of Human Resources:**

Human resources are characterized by low productivity, low participation in labor force high dependency ratio of 349%, high illiteracy rate of about 47% of population, low school enrollment of about 59% of school age children, and health service coverage of only 50% of the population.

#### **4- Lack of Sufficient Infrastructures:**

Infrastructure facilities in Yemen are still insufficient including electric power supply, water supply network, roads and bridges, communication services, and others.

#### **5- Low Per Capita Income and Low Saving Capacity:**

Per Capita income in Yemen is no more than 349 dollar, which is under poverty line; thereby saving capacity is quite limited.

#### **6- Increasing Dependency on Foreign Sector:**

Several macrocosmic indicters reflect increasing dependency of the economy on foreign sector as oil production represents 31% of GDP, oil exports represents 95% of total exports, and oil revenue contributes more than 60% of government revenues. In addition,

development investments is almost dependent on loans and foreign assistance, meanwhile imports represent almost 50% of GDP.

**(n) Investment for the Next Decade (2001-2010)**

Table (21) below shows the total required investment for the next decade (2001-2010), its estimation based on the following indicators:

- 1- The exchange rate is YR1 165 = \$1
- 2- The ratio of capital to GDP is estimated to be between " 4 to 5".
- 3- The GDP is expected to be 7000 Million dollars in 2000 (it was 6795 Million dollars in 1999)
- 4- The ratio of total local value of investment to the Gross Domestic Product in year 2000 is about 20%, which results to an economic growth rate of about 4.25%, and since the Program of Action for (2001-2010) aims to achieve yearly real economic growth rate between 6.5-7.5 %, the yearly total required investment as a percentage of the GDP is depicted in table (21) below:

TABLE (21)  
INVESTMENT PROGRAM FOR 2001-2010 (AS A PERCENTAGE OF GDP)

Year	Total Expected Inv. (In million \$)	(%)	Source Domestic Saving	(%)	Source Foreign (FDI)	(%)	Source Foreign (soft loans, grant, and Concessional multilateral loans)	(%)
2001	1750	.25	1050	0.15	350.0	0.05	350	.05
2002	1837.5	.25	1102.5	0.15	367.5	0.05	367.5	.05
2003	2002	.26	1155	0.15	462.0	0.06	385	.05
2004	2080	.26	1200	0.15	480.0	0.06	400	.05
2005	2295	.27	1360	0.16	510.0	0.06	425	.05
2006	2430	.27	1440	0.16	540.0	0.06	450	.05
2007	2660	.28	1520	0.16	565.0	0.07	475	.05
2008	2800	.28	1600	0.16	700.0	0.07	500	.05
2009	3045	.29	1785	0.17	735.0	0.07	525	.05
2010	3300	.30	1980	0.18	770.0	0.07	550	.05
<b>Total</b>	<b>24199.5</b>	<b>-</b>	<b>14192.5</b>	<b>-</b>	<b>5579.5</b>	<b>-</b>	<b>4427.5</b>	<b>-</b>

The total expected investments during 2001 to 2010 is estimated to be \$24199.5 Millions, about \$ 14192.5 Millions is expected to be financed from Domestic Saving, \$ 5579.5 Millions from Foreign Direct Investment (FDI) and the rest \$ 4427.5 Millions is expected to be financed from foreign resources as; grants, soft loans, and concessional multilateral loans.