

Challenges of the War Economy in Yemen

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Introduction

The economic dimension is one of the most critical factors exposing the depth of the Yemeni crisis and its far-reaching effects on both the State and society. Since the outbreak of the war and the rise of multiple centers of power, Yemen's economy has undergone severe contraction and increasing institutional fragmentation. The legitimate government has lost its capacity to manage and allocate public resources in a way that ensures financial and social stability. This crisis has been marked by the suspension of oil and gas exports, the decline of external aid, the expansion of corruption and nepotism, and the fragmentation of governance among multiple actors who share influence and decision-making.

Within this environment, a distinct phenomenon has emerged—what can be described as a “war economy.” This system is marked by disorder and entangled interests, as State resources have been exploited to finance the parties and forces in control. At the same time, new networks of influence have arisen, engaging in illicit activities such as smuggling, currency speculation, and the imposition of informal levies. These dynamics have severely distorted the structure of the national economy and intensified the hardships experienced by ordinary citizens.

This study seeks to analyze the major economic challenges facing areas under the authority of the internationally recognized government, with particular emphasis on the “war economy,” its dynamics, manifestations, consequences, and its impacts on state institutions, society, the economy, and essential services. It also explores the interplay of political, administrative, and economic factors that have collectively undermined state functions and paralyzed its institutions.

The analysis aims to understand the nature of Yemen's economic crisis within its broader context and interconnected dimensions—especially as the country remains engulfed in a war that has persisted for more than a decade.

Presidential Measures to Address Economic Challenges

In late October, Yemen's Presidential Leadership Council (PLC) approved a set of economic measures and reform-oriented decisions aimed at stabilizing the national economy and advancing the ongoing reform agenda. The package included tighter oversight of land, sea, and air entry points; the expansion of digital and networked systems for administering sovereign revenues; and efforts to enhance the efficiency of public spending across all sectors.

The Council reaffirmed its support for the government in implementing these measures and securing full access to public revenues. It also emphasized the need to equip the Central Bank with the tools required to manage monetary policy, curb currency speculation, and stabilize the national currency. In addition, the PLC called for stronger coordination among state institutions to ensure the timely and systematic implementation of the approved reform matrix.

These decisions came after a series of high-level meetings focused on Yemen's worsening economic and fiscal conditions, assessing progress on the government's economic recovery plan and reform commitments. The discussions also reviewed efforts to strengthen the national currency, mobilize domestic and external revenues, and restore confidence among international donors—steps considered essential for enabling the government to meet its obligations, address budget deficits, and improve public service delivery.

It is evident that these measures are intended to address the structural imbalances that have worsened Yemen's financial and economic decline, particularly following the suspension of oil exports in October 2022—a development that significantly reduced state revenues. However, concerns remain regarding the feasibility of implementing these decisions amid the continued weakness of central institutions and the rising influence of local power centers, including those located in resource-rich regions.

In July, the government formed the National Committee for the Regulation and Financing of Resources to enhance transparency in economic resource management and direct foreign currency flows into the official banking sector. At the time, government actions included tightening controls on foreign currency exchanges, prohibiting the use of foreign currencies in local transactions, and revoking the licenses of exchange companies suspected of manipulating the currency. These steps contributed to a noticeable rise and stabilization in the value of the Yemeni rial.

Key Economic Challenges

According to the International Monetary Fund (IMF), Yemen — after years of conflict — has become one of the most fragile countries in the world, facing a severe humanitarian crisis and a deeply weakened macroeconomic structure. The real GDP has contracted by roughly 27% since the war began, while per capita income has sharply declined. The decrease in currency value and inflation has suppressed real incomes. After Houthi attacks on oil facilities that halted exports in 2022, Yemen became a full importer of oil for the first time in decades.

The IMF noted in its latest report that more than half of Yemen's population now requires urgent humanitarian assistance due to widespread food insecurity, limited access to clean water, disease outbreaks, and large-scale displacement. Despite the significant efforts of international aid agencies, the scope of the crisis far exceeds available resources.

The IMF Mission also reported that government revenues under the internationally recognized administration have declined by more than eight percentage points of GDP since 2022. This drop is primarily attributed to the suspension of oil exports and the redirection of trade toward Houthi-controlled northern ports. In addition, smuggling activities have intensified, and local authorities have increasingly withheld revenues from the central government.

Additionally, competition among governorates over port activity has led to inconsistent taxation rates and customs tariffs, further reducing potential fiscal revenue. Consequently, government spending has declined by 5.4 percentage points of GDP, and fiscal financing has increasingly relied on treasury overdrafts. The Central Bank has attempted to sterilize these withdrawals by using Saudi deposits to sell foreign currency reserves and control money supply growth and inflation.

Similarly, the World Bank reported that Yemen's economy remains under severe pressure as the ongoing conflict, institutional fragmentation, and shrinking external support exacerbate the crisis. The Bank's data shows that real GDP per capita has fallen by 58% since 2015, while inflation in government-controlled areas exceeded 30% in 2024, a year marked by significant depreciation of the Yemeni Rial — from 1,540 to 2,065 Rials per US dollar, before partially recovering to 1,600 in late July 2025.

In its recent report titled "Persistent Fragility amid Rising Risks," the World Bank highlighted the continuing Houthi blockade on oil exports, which has reduced government revenues (excluding grants) to 2.5% of GDP in 2024. The report warned that Yemen's economic landscape remains highly fragile, with the country effectively divided into two distinct economic zones — each with separate institutions, monetary authorities, and exchange rates. This division, it argued, exacerbates disparities and undermines efforts to coordinate national economic policy.

According to the report, recent tensions in the Red Sea have severely disrupted trade routes through the Bab al-Mandab Strait, resulting in higher shipping costs, while at the same time social and economic conditions have deteriorated.

The Most significant manifestations of economic deterioration

Among the most significant manifestations of economic deterioration (in areas controlled by the internationally recognized government) are:

- **The depreciation of the national currency**, which has led to sharp increases in the prices of basic goods and essential services. This has been compounded by a monetary divide, as different currencies circulate in areas controlled by the Houthis.
- **A widening fiscal deficit and shrinking revenues**, particularly after the suspension of oil and gas exports — the state's main source of income. As a result, the government has been unable to pay public sector salaries on a regular basis, relying instead on foreign assistance and deposits (mainly from Saudi Arabia) to support the budget and stabilize the currency.
- **A worsening humanitarian crisis**, marked by deepening food insecurity, soaring poverty and malnutrition rates, and an increasing dependence among households on negative coping mechanisms such as debt and child labor.
- **The spread of corruption and the entrenchment of the war economy**, characterized by the squandering of public resources and the growing dominance of informal financial networks.
- **The decline in essential public services**, particularly electricity and water.

The War Economy: Fragmented State Functions and the Rise of Parallel Interests

- The term “ war economy “ refers to economic activities that emerge or flourish during periods of conflict, when production, trade, and resources shift from serving development and stability to serving the interests of armed groups and power brokers.
- In such contexts, state authority weakens, financial and legal institutions lose influence, and parallel networks thrive amid chaos and fragmentation. In Yemen, the *war economy* has become one of the most dangerous byproducts of the ongoing conflict. Its defining features can be outlined as follows:

• **The emergence of new financial power networks**, as some local officials and faction leaders exploit weak oversight and divided authority to build private economic interests through the control of ports, border crossings, and local taxation.

- **The decline of the State's role as the sole source of economic legitimacy**, with each region or military formation establishing its own financial and administrative system. This has led to the fragmentation of the overall economic system and the diminishing authority of the central bank and other revenue institutions.
- **The expansion of the black market**, which has become a major parallel economy driven by scarcity, speculation, and informal trade.
- **The collapse of the middle class and widening social inequality**, as public sector wages lose value and poverty deepens, while wealth accumulates in the hands of a small elite benefiting from the war economy.
- **Severe humanitarian consequences**, reflected in widespread food insecurity, rising poverty rates, declining public services, and increasing dependence on humanitarian aid.

In essence, Yemen's *war economy* represents the transformation of conflict into a self-sustaining system — one that fuels political fragmentation, institutional paralysis, and social disparity, while turning public resources into private profit for those who thrive in instability.

War Economy: An Informal System Dominating State Resources

The war economy in Yemen has evolved into an *informal economic system* born out of prolonged conflict, political fragmentation, and institutional collapse. It now controls a substantial portion of the country's resources and financial activities—largely outside the framework of the official state apparatus.

The government's economic role has significantly diminished, having lost control over much of its revenue base due to the suspension of oil and gas exports, administrative fragmentation, and the rise of competing financial channels. At the same time, new networks of political, military, and economic interests have emerged across different regions, benefiting from the continuation of the war through commodity monopolies, currency speculation, and the control of ports and border crossings.

Consequently, Yemen's economy is marked by profound structural distortions: local production has sharply declined, the national currency has fallen to record lows, and poverty and unemployment have risen to unprecedented levels.

Main Impacts of the War Economy on Public Conditions

The entrenchment of the war economy has triggered a catastrophic deterioration across nearly all aspects of life in Yemen. The following are the most significant effects:

- **Humanitarian disaster and aggravation of poverty** :Poverty rates have increased dramatically, with reports indicating that nearly 90% of the population is now below the poverty line and millions have reached advanced stages of starvation.

- **Economic and financial collapse.**

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- **The degradation of infrastructure and public services**, including the destruction of vital facilities and the collapse of essential utilities such as electricity and water.

The Suspension of Oil and Gas Exports

Since late October 2022, Yemen's crude oil exports from the *Ashahihr* and *Al-Nashimah* terminals have been halted following Houthi drone attacks on ports in Hadramout and Shabwa. Oil revenues accounted for more than 70% of the legitimate government's resources and nearly 60% of total public revenues ;thus ,the halt represented a significant financial and economic shock ,especially in the absence of productive and economic alternatives.

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Politically ,the suspension of oil exports has eroded the government's legitimacy ,as its inability to pay salaries or deliver basic services has fueled public discontent and weakened its authority—while simultaneously strengthening the influence and power of local actors.

Corruption and Nepotism Networks

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institutions revenue and financial its ,2015 in Aden to relocated government Yemeni the Since institutional and war escalating With .weaknesses oversight and administrative faced have collected been have revenues and ,down broke system collection revenue the ,fragmentation become has environment This .oversight central without level governorate the at spent and institutions state in trust public eroding ,nepotism and corruption financial for ground fertile .resources scarce already its manage to ability s'government the undermining and

The most prominent forms of financial corruption and nepotism include:

- **Dual and overlapping revenue collection centers :** Multiple entities—including local authorities ,security forces ,the military ,sovereign bodies ,and armed groups—collect taxes and customs duties from the same ports or checkpoints .This fragmentation leads to dispersed revenues that never reach the Central Bank's unified account.
- **Illegal levies and extortion :** Various military or security groups impose unauthorized fees under different pretexts and without legal basis .These collections are funneled into private accounts or used to benefit specific factions or influential actors.
- **Nepotism-based appointments :** Many financial and administrative posts in key revenue-generating institutions are filled on the basis of political or regional loyalty rather than merit, competence, or integrity. This practice has fostered conflicts of interest, weakened management efficiency, and entrenched clientelism.
- **Lack of transparency and accountability:** Independent oversight bodies such as the Central Organization for Control and Auditing and the Anti-Corruption Authority have been largely sidelined or rendered ineffective, with their work obstructed and staff intimidated or dismissed.
- **Failure to Deposit Revenues into the Central Bank:**

The failure to deposit financial revenues into the central bank—as one form of financial and administrative corruption—has led to shrinking state resources and worsening economic and humanitarian crises. All sovereign revenues are supposed to be deposited into the Central Bank in Aden for proper management.

Consequently, several issues have emerged:

- **Loss of a unified treasury system** :Most revenue-collecting agencies now retain funds locally and spend them directly ,bypassing central oversight mechanisms.
- **Proliferation of unofficial and parallel accounts** :Several government offices have opened private accounts in commercial banks to manage funds outside the formal financial system. This has stripped the Central Bank of its supervisory authority over monetary flows ,effectively placing the state's cash movement beyond its control.
- **Weak capacity of the central bank to manage monetary policy** ,due to scarce resources and multiple revenue centers . The central bank has become unable to finance government expenditures or cover public employee salaries ,having lost its tools to regulate currency markets and stabilize the exchange rate.

In short ,financial corruption and the failure of revenue institutions to deposit funds with the central bank have not only weakened revenues but also fragmented the economic and financial structure of the legitimate state itself ,resulting in increased economic burdens ,including currency collapse ,salary disruptions ,and a severe decline in essential public services.

Duality in State Administration

The duality in State administration—including within key revenue institutions—has become one of the most visible manifestations of Yemen's fractured governance under the internationally recognized government .This phenomenon was most clearly illustrated last month when *Aidaros Al-Zubaidi*, member of the Presidential Leadership Council (PLC) and head of the Southern Transitional Council (STC), issued a series of unilateral appointment decrees. These included deputy ministers, provincial governors, and heads of critical revenue-generating authorities—all affiliated with the STC.

The move sparked a new wave of internal disputes within the PLC, prompting Saudi Arabia, the main backer of the government and the council, to intervene and broker a settlement. The compromise resulted in the suspension of Al-Zubaidi's decrees, except for one appointment that was approved by mutual agreement. In turn, Al-Zubaidi demanded the suspension of the government's decision to appoint *Salem Al-Awlaki*—a senior STC figure—as head of the General Authority for Land and Real Estate Affairs.

It can be noted here that this duality led to widespread appointments based on loyalty and nepotism, with each faction in power seeking to consolidate its position by appointing loyalists to sensitive posts. This has turned the administrative apparatus into a network of personal loyalties, ignoring standards of merit or integrity. Duality has also led to overlapping powers: although the government is responsible for economic policy, some of its decisions are sometimes blocked or canceled by powerful, armed actors, as occurred with the aforementioned appointment of Salem Al-Awlaki. As a result, government decisions—particularly economic ones—have become hostage to political bickering, rather than the outcome of a unified vision.

There is no doubt that duality in administration has had negative consequences, foremost among them: weakening the unity of economic decision-making, paralyzing planning and oversight institutions, impeding the management of natural resources, exacerbating corruption, and politicizing the economy by using resources to reward loyalists, purchase allegiances, and pursue political recruitment. This has meant the decline of accountability and merit in favor of networks of loyalty and personal benefit, weakened the state's ability to control resources, reinforced the war economy, and eroded public trust in state institutions.

In short, dual governance has produced a fragmented, distorted economy controlled by competing centers of power, rendering the government incapable of formulating a coherent economic strategy or effectively confronting the challenges of a prolonged war.

Absence of External Support

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The impact of the absence of external support is evident in the sharp decline in foreign financial inflows ,which created a severe shortage of foreign currency reserves and deepened the hardship faced by citizens .The halt in external assistance also led to a reduction in humanitarian aid and in funding for the health ,education ,and basic services sectors .This decline has been reflected in rising levels of poverty ,hunger ,and unemployment.

Ultimately ,the withdrawal of foreign aid has placed the government in a difficult economic situation :deprived of adequate domestic resources and unable to sustain financial stability or meet even the most basic needs of the population .The result is a state caught in a cycle of dependency ,fragility ,and eroding public trust.

Major Social and Humanitarian impacts of the War and Economic Deterioration

The consequences of economic deterioration have deeply affected every aspect of social and humanitarian life, most notably in the following areas:

-Health system:

material declining to due supplies and staff of shortage a from suffering been has sector This ,personnel medical of migration the to led support of lack and salaries of halt The .capabilities epi- deadly of spread the to addition in ,supplies medical and medicines of shortages severe many of destruction the and water clean of lack a to due ,measles and cholera as such demics .networks sewage

-Education:

Student dropout and deprivation of millions of children from their right to education ,due to difficult living conditions that pushed them away from schools and forced them to work .Also, irregular payment of teachers 'salaries led to the stoppage of education in many areas.

-Violence and social disintegration:

The war and economic deterioration forced millions of Yemenis into internal displacement)about 4.5 million ,(living in harsh conditions lacking even the simplest necessities of life. This ,in turn ,led to the spread of negative coping mechanisms such as violence ,violence, child labor ,and the recruitment of children by warring factions .The prolonged conflict has also triggered a surge in mental health disorders — particularly among children — alongside the spread of disease and social instability.

Conclusion

The economic challenges facing areas governed by the internationally recognized government extend far beyond a temporary fiscal crisis .They reflect a deeply rooted structural breakdown driven by the intersection of political ,military ,and administrative factors.

The halt of oil and gas exports ,the spread of corruption ,fragmented governance ,and the decline in external support have collectively accelerated economic deterioration and further weakened state institutions.

The rise of a” war economy “has produced a parallel system dominated by local power networks that exploit resources for personal and factional benefit at the expense of the state and society .This dynamic has fueled rising poverty ,worsening public services ,and a growing erosion of trust in government institutions.

Without far-reaching reforms to restore the state’s economic role and dismantle the illicit networks that have flourished during the war ,Yemen’s structural collapse will continue .Moving beyond this phase requires a comprehensive national vision that upholds the principles of economic justice ,ensures transparent and accountable management of public resources ,and establishes the foundations for sustainable political and economic stability.



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مركز أبعاد للدراسات والبحوث منظمة مجتمع مدني غير ربحي مرخص ، من وزارة الشؤون الاجتماعية اليمنية رقم (436) في 18 أكتوبر 2010م ، يهتم بالقضايا السياسية والفكرية والاعلامية كقضايا الديمقراطية والانتخابات والأحزاب وقضايا الأمن والإرهاب ونشاطات الجماعات الابدولوجية والحريات السياسية والفكرية والصحفية إلى جانب القضايا الاقتصادية والاجتماعية والإنسانية ذات الارتباط بالمتغيرات السياسية.