Good Practice Review on Cash Assistance in Contexts of High Inflation and Depreciation

CASE STUDY YEMEN
– July 2021

SPACE

german humanitarian assistance
DEUTSCHE HUMANITÄRE HILFE

CaLP

This case study accompanies the CaLP Network Good Practice Review on Cash Assistance in Contexts of High Inflation and Depreciation. It is intended to illustrate the process of situational analysis, response analysis and response option selection presented in the GPR. The learning from this case study has also actively contributed to the good practices documented in the review. It should be noted that the case study represents a snapshot in time of a continuously evolving situation. This case study was authored by Calogero di Gloria (DG ECHO), supported by Emma Holden-Maillard and Calum McLean (working for the FCDO-GIZ SPACE initiative).

1. CONTEXT

The Yemeni conflict, now in its sixth year, has evolved into the **largest humanitarian crisis in the world**. An estimated 80% of the population require some form of humanitarian or protection assistance, according to the Humanitarian Response Plan (HRP) 2021,[21] **almost 21 million people need some form of assistance**, 12.1 million of them are in acute need and 3.6 million people are currently displaced. The ongoing conflict has devastated communities, where displaced populations near the frontlines have little to no access to basic services, and the **economic collapse and depletion of services has resulted in worsening socio-economic vulnerabilities**.[2] The humanitarian situation was aggravated in 2020 by escalating conflict, the COVID-19 pandemic, disease outbreaks, torrential rains and flooding, a desert locust plague, economic collapse, a fuel crisis across northern governorates and reduced humanitarian aid.

In the Yemen context, which is highly volatile due to political, security and economic complexity, **cash programming takes place at a large scale**. While the large-scale programming is an achievement, its **effectiveness and outreach capacity is hindered by fragmentation and lack of harmonization**. Humanitarian and social protection systems have weak coordination mechanisms and collaboration potential, causing duplication of efforts and overlapping of beneficiary caseloads. Under the Grand Bargain and the Common Donor Approach for humanitarian cash programming, aid organizations and donors have committed to ensuring that effective coordination, delivery and monitoring, and evaluation mechanisms are in place for cash assistance and where cash is deemed feasible and appropriate – scaling-up its adoption.[3]

Yemen's **cash infrastructure is based on two factors: (1) reliance on remittances and (2) national social protection systems**. Historically, as the CaLP Case Study explores, Yemen had a long-standing reliance on cash-based remittances, with remittances forming, at various times, up to 70% of Yemen's GDP.[4]

With the increasing magnitude of needs due to the compounded crisis, donors such as DG ECHO have decided to support humanitarian organizations **streamlining cash and voucher assistance (CVA) interventions through Multipurpose Cash Assistance (MPCA)** for the most vulnerable conflict-affected households in Yemen. The **Cash Consortium of Yemen (CCY) aims to deliver a harmonized MPCA through a coordinated approach** to effectively meet the critical needs of vulnerable conflict-affected households. In parallel, the existing attempts to link humanitarian and social protection programmes, as well as the evolution of both programmes, provide best practices and lessons learned for the process of harmonization and scale-up.

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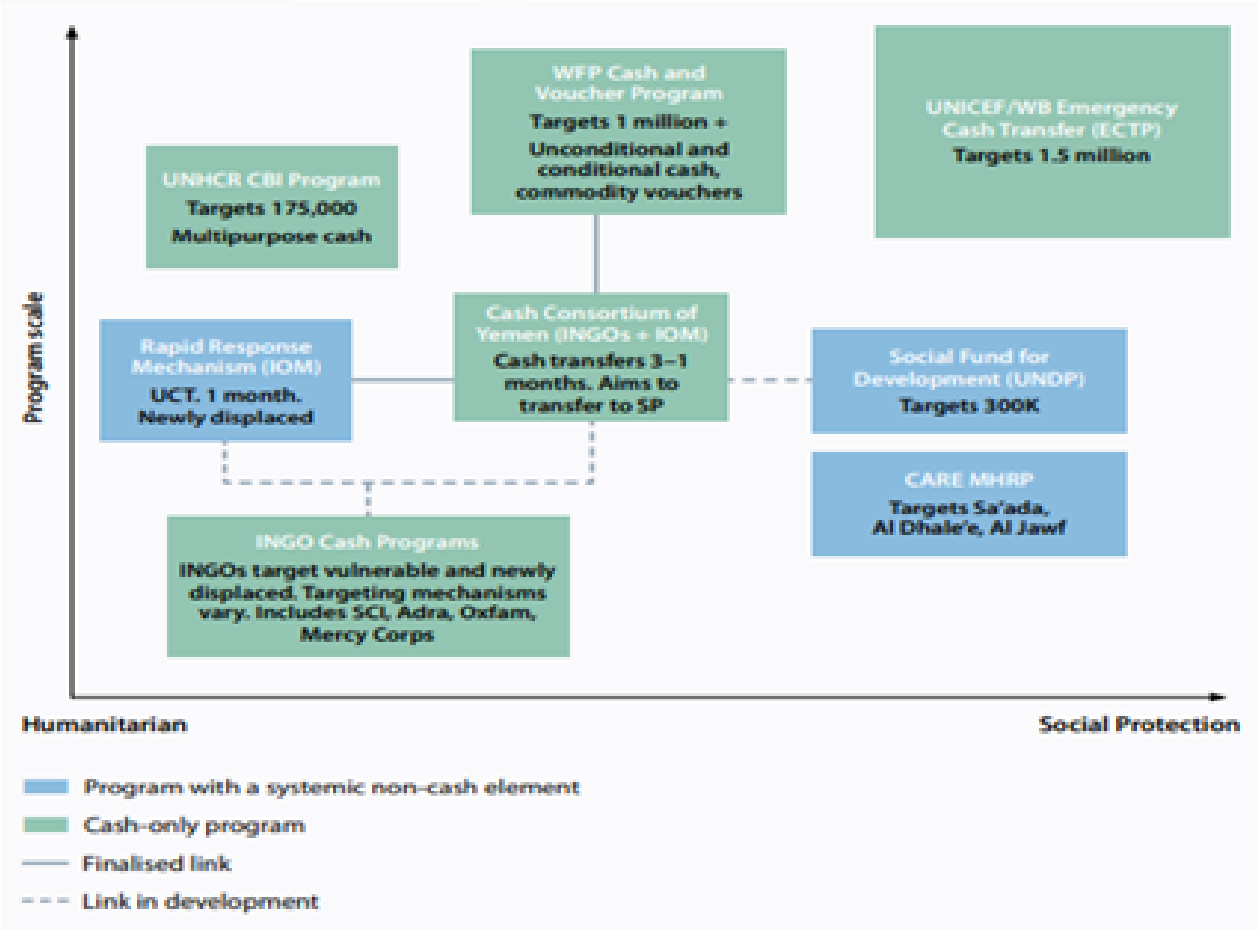
[1]OCHA (2021). Yemen Humanitarian Response Plan 2021 (March 2021). Retrieved from https://reliefweb.int/report/yemen/yemen-humanitarian-response-plan-2021-march-2021-enar

[2]OCHA (2020). Yemen Humanitarian Response Plan Extension, June–December 2020. Retrieved from https://reliefweb.int/report/yemen/yemen-humanitarian-response-plan-extension-june-december-2020-enar

[3]The United Nations Common Cash System was launched in December 2018. Signatories include OCHA, UNICEF, UNHCR and WFP. CaLP (2019). Joint Donor Statement on Humanitarian Cash Transfers https://www.calpnetwork.org/publication/joint-donor-statement-on-humanitarian-cash-transfers/

[4]Ruta Nimkar (2021). Humanitarian Cash and Social Protection in Yemen CALP Case Study. Retrieved from https://www.calpnetwork.org/publication/humanitarian-cash-and-social-protection-in-yemen/

Figure 1: Humanitarian and social protection programmes in Yemen



The recent establishment of a Donor Working Group on cash (co-chaired by DG ECHO and FCDO) and a reinvigorated Cash and Market Working Group (CMWG) also present opportunities to harmonize cash programming and strengthen linkages to social protection systems. Donors and implementers working more closely together to promote harmonization and more coordinated approaches should also extend their efforts into management of currency depreciation and inflation in Yemen, including more donor flexibility and advocacy at higher levels.

2. SITUATION ANALYSIS

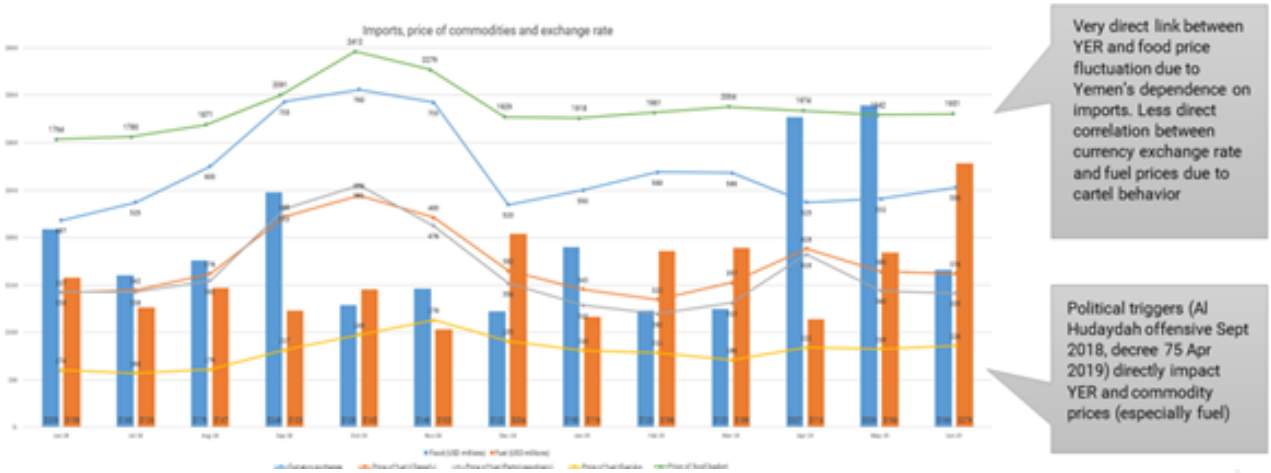
a. What is happening to prices?

The **depletion of foreign currency reserves and depreciation are driving up inflation**, reducing households' purchasing power and their ability to meet basic needs, which results in increased levels of food insecurity. Sources of foreign currency inflow in Yemen – especially oil exports, humanitarian funding and bilateral financial support – remain constrained. Although **food imports will continue, food prices are expected to follow the exchange rate and are therefore likely to increase** and diverge among different geographic areas of control.

Exchange rate instability causing price volatility and challenges accessing credit are therefore the major cost drivers of food prices.[5] The increase in food prices since 2015 is primarily a result of the drop in the value of the rial (YER). Yemen is reliant on imports (for 88% of its food supply), making it highly exposed to currency fluctuations. The three main sources of food import financing and currency stability – remittances, the Saudi-funded letters of credit, and foreign aid (which accounts for 20% of wheat imports according to ACAPS estimates) – are all declining. **Competition to control import financing by both parties to the conflict also adds to the cost of food**. Competing letters of credit systems, divergent monetary policy, and attempts to control fuel supply chains all add to the complexity of food supply chains. Higher operating costs are passed on to consumers as higher prices.

Efforts to address the rise in market prices will likely be meaningless unless a course of action is adopted that results in stabilizing the YER or supporting incomes that keep pace with inflation, and/or significant investments by the international community.

Figure 2: Value of imported commodities[6]



[5]ACAPS Analysis Hub (2020). Thematic report: Yemen Food Supply Chain, 16 December 2020. Retrieved from https://www.acaps.org/sites/acaps/files/products/files/20201216_acaps_yemen_analysis_hub_food_supply_chain.pdf

[6]ACAPS Analysis Hub (2020). Volatility of the Yemeni Riyal, 16 December 2020. Retrieved from https://www.acaps.org/sites/acaps/files/products/files/20200129_acaps_yemen_analysis_hub_drivers_and_impact_of_yer_volatility_0.pdf

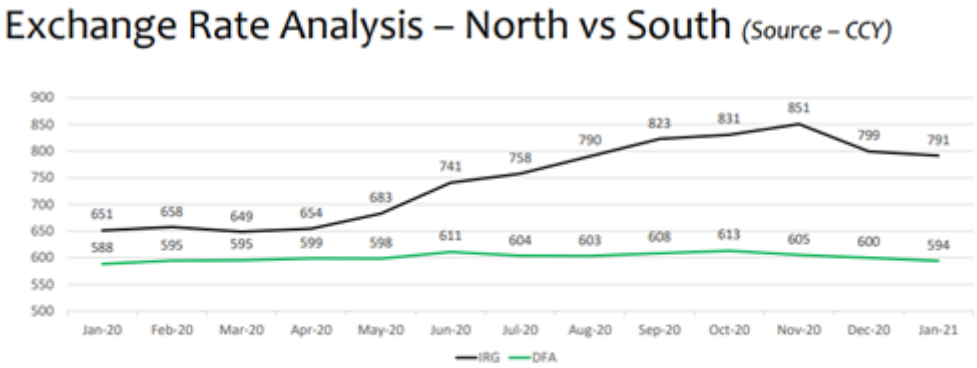
b. What is happening to the currency and what are the implications for programming?

With the country's economy, banking and financial systems in free fall, **the reasons for the Yemeni currency crisis are manifold:** hurdles in the peace process; depletion of foreign reserves; lack of interaction between the Aden and Sana'a branches of the Central Bank of Yemen (CBY); printing of currency by CBY without adequate foreign exchange cover; significant delays in the approval of letters of credit to importers; **high import dependency against dwindling exports and thus a widening balance of payment deficit**. All these factors, the result of enacted policies by parties to the conflict, are exacerbated by the lack of fiscal control by the CBY over money exchange dealers and their reported collusion, unregulated injection of YER into the system, and the increased demand for USD by importers (food and fuel).

Since the division of the CBY in Aden and the CBY in Sana'a, the country has been suffering from detached and contradicting monetary policies. In effect, two currencies are in place, and the divergence between them further increased to more than 200 YER during the second week of 2020.

Since January 2021, **the rial in Internationally Recognised Government (IRG)-controlled areas has resumed a steady depreciation**, following a temporary appreciation in December 2020 related to the announcement of a new cabinet and the release of funds from the Saudi deposit to cover letters of credit for the import of basic commodities. The value of the rial in December 2020 increased to YER 640 per 1 USD; it then started to depreciate again up to YER 860 per 1 USD in January 2021, from an average of YER 778 per 1 USD throughout 2020. **The value of the rial in the Houthi-controlled North remained stable at around YER 595 per 1 USD in January 2021, in line with the average in 2020.**

Figure 3: Yemen exchange rate analysis: North vs South



	Jan-20	Feb-20	Mar-20	Apr-20	May-20	Jun-20	Jul-20	Aug-20	Sep-20	Oct-20	Nov-20	Dec-20	Jan-21
IRG	651	658	649	654	683	741	758	790	823	831	851	799	791
DFA	588	595	595	599	598	611	604	603	608	613	605	600	594

The announcement in March 2021 of a donation by the Kingdom of Saudi Arabia contributed to a brief appreciation of the rial in IRG-controlled areas. The day following the announcement, the exchange rate of the new rial banknotes used in IRG areas decreased from YER 892 throughout March to YER 830 per 1 USD. In the Houthi-controlled North, the rial value averaged at YER 603 per USD 1 for the entire month of March 2021 – in line with the previous month – although it began to increase at the beginning of April. The bilateral support by the Kingdom of Saudi Arabia to the IRG, which contributes to the stability of the rial in Yemen, is likely to be affected by a UN Panel of Experts' report highlighting a lack of transparency, allegations of corruption, and misuse of the Saudi deposit by the Central Bank of Yemen (CBY) in Aden (UNSC 25/01/2021). This could also push the IRG towards significant reforms within CBY Aden, aimed at improving transparency and possibly encouraging foreign financial support, which could potentially contribute to currency stability.

If the current situation continues, however, dwindling foreign currency reserves will continue to drive up inflation, affecting people's ability to afford food and other basic commodities. The escalation of conflict since the beginning of February in Marib – the main source of oil and liquefied gas in Yemen – could significantly disrupt oil and gas facilities and extraction operations, affecting IRG revenues and currency stability. IRG revenues from oil exports are also expected to remain limited by further decreases in global crude oil prices at the end of March, along with limited exports from Yemen. The continued risk of limited access to fuel also affects essential services, including the production and transport of food.

3. Implications for CVA Programmes

a. Implications for recipients

The decline of Yemen's economy due to conflict has had a **major impact on people's well-being**. Since the conflict in 2015, food prices have doubled and the cost of basic living, measured by the Survival Minimum Expenditure Basket (SMEB) has increased fourfold. **Food is available in markets, but few Yemenis are able to afford it due to loss of purchasing power**. This leads to the adoption of negative coping strategies, such as reducing food intake, borrowing food or requesting help from friends and relatives, and relying on less expensive food. In the long term, these behaviors are likely to have a detrimental effect on people's health, making them more vulnerable to food insecurity, malnutrition, and disease outbreaks.

Economic competition between the North and South has impacted heavily on prices, particularly for fuel. The price of fuel (diesel, gas, and petrol) normally increases or decreases following a change in the value of the YER. As with food, fuel is one of the main imported commodities in Yemen. There is a less direct correlation between YER depreciation and fuel prices compared to food prices due to fuel cartel behavior and IRG CBY policies around fuel import. **Although the price of fuel itself may not increase significantly, any increase in fuel prices has a direct impact on households' purchasing power, ability to access basic services, and mobility**. For instance, when the price of fuel increases, local water corporations are unable to afford pumping costs for the piped water networks. Yemeni households, therefore, try to supplement their water supply with trucked and bottled water with very high transportation costs. Higher costs of fuel mean higher transportation costs as well as constraints in accessing markets and services; this also affects electricity to run schools and health facilities.

b. Implications for humanitarian agencies and donors

Poor exchange rates ultimately mean less Yemeni rials disbursed to beneficiaries. The main problems organizations face due to currency volatility are:

- **Unpredictable underspending in some budget periods**, with the obligation to return donor funds, resulting in expensive disallowances. As programme budgets are in USD or other foreign currencies, the reduction in the value of USD leads to underspending by humanitarian actors.
- **Lack of confidence from local communities** who may receive lower amounts than specified at the beginning of a project due to currency volatility. Humanitarian organizations plan cash transfer programmes in USD but disburse YER to beneficiaries. If the YER appreciates, there will be less YER disbursed for the same amount of USD on which the programme is designed/based as market prices closely reflect the trend of exchange rates, and vice versa in the case of depreciation.
- **Limited capacity of partner financial institutions due to market panic affecting liquidity rates may result in the imposition of limitations on the amount that organizations give to beneficiaries** (to avoid overspending, or changes in the amount of money disbursed due to fluctuation).

- Sometimes, even though the YER devaluates, **UN agencies and INGOs may not be able to add beneficiaries to their list** (e.g. if these are based on the previous Social Safety Net) **or to adapt the size of transfer in a timely way** (e.g. if coordination structures are not harmonized in their decision making).

Foreign aid is also an important source of hard currency that the private sector relies on to finance food imports. Any reduction in the foreign aid could put further upward pressure on food prices, both by reducing the supply of food coming into the country, and by reducing the availability of hard currency in the financial system to fund food imports.

4. Response Analysis

In 2020, the **CMWG has been strongly engaged in enhancing collaboration on cash and market interventions in Yemen** as well as working to scale up CVA through sectoral interventions, multipurpose cash assistance and hybrid approaches, with the overarching aim of harmonizing interventions across the humanitarian response.

In order to support humanitarian actors with the harmonization of price monitoring among all cash actors in Yemen, the CMWG launched the **Joint Market Monitoring Initiative (JMMI), which incorporates information on market systems, including price levels and supply chains.** The basket of goods to be assessed includes ten non-food items, such as fuel, water and hygiene products. The JMMI tracks all components of the WASH and Food SMEB as well as other food and non-food items. Also, in light of the current COVID-19 pandemic, the JMMI has been adapted to begin assessing the potential impact of the pandemic on markets and on respondents' businesses.
Meanwhile, ACAPS launched the Yemen Economic Tracking Initiative (YETI),[7] **aiming to provide a platform to track key economic trends, developments and risks to support economic policymaking for Yemen**. This new platform brings together real-time data from a range of sources to provide a greater overall and comparative understanding of the current political-economic situation in Yemen.

In August 2020, the CWG produced a guidance note on *Issues Around Use of Foreign Currency for Designing Assistance Packages in Yemen*, which concluded that the use of USD was not viable. Other analysis processes underway are an **FSP assessment conducted by REACH, and various efforts to track remittances** (e.g. by the CCY and ACAPS). The CCY also produces a **weekly Exchange Rate Flash update** which is an essential resource for tracking depreciation and the implications for purchasing power.

In 2021, further advocacy is required to ensure **consistency and sustainability in coordination mechanisms and to strengthen links between sector-specific cash and voucher assistance, MPCA and social protection**. Such coordination is essential to address the inflation and depreciation challenges in a harmonized way.

See: https://yemen.yeti.acaps.org/

5. Response Options

a. Policy solutions

The protracted crisis context in Yemen requires a system that provides a reliable, predictable and effective response to the increasing basic needs of the country's poorest and most vulnerable. Given the current lack of state capacity and domestic financial resources, achieving a coherent approach to programming will require **focusing on governance capacity, maintaining technical functions and strengthening the integration of the whole service delivery system**.

There is also a need to **strengthen the accountability, transparency and tracking system of financial flows and address the obstacles to financing food and fuel imports.** At macroeconomic level, further efforts are required to stabilise financial reserves, facilitate access to accounts and foreign currency frozen abroad, and create safer and more efficient pathways for remittance transfers. Economic stability would also depend upon the suspension of competing monetary, fiscal and economic policies that are politicizing and dividing the economy and distorting local markets in Yemen.

Advocacy measures are expected to reduce transport and logistical costs of the supply chain, including facilitating more stable and transparent access to fuel, intervening in markets to lower war risk insurance costs, reducing delays on food inspection mechanisms and investing in infrastructure at Yemen's ports. To help alleviate pressure on market functionality and cope with the exchange rate volatility, the **main stakeholders have also been advocating for adequate transfer values. This would help stabilize the purchasing power of vulnerable Yemeni households**. Ideally, cash transfers should be supported by investments in sustainable livelihoods and linking humanitarian interventions with longer-term social protection systems.

b. Programming solutions

In 2020, an ad hoc **SMEB Technical Working Group (TWG) was launched to review and deliberate on the commodities price trends and provide recommendations to the CMWG for final endorsement**. On 30 September 2020, the SMEB list of commodities was agreed with all clusters, CMWG and Humanitarian Country Team, including donors, and the whole process took a year to finalize. The increase in commodity prices is not a trigger for a fully-fledged SMEB revision. The **inflation serves as a trigger for amendments in transfer values only**. The overall recommendation of the TWG was to consider the following triggers for revision/updating of SMEB transfer value (TV): **once the market prices reach 95% of the prevailing SMEB TVs, this should act as a trigger to initiate the 20% top up in the prevailing SMEB TVs** with a formal TWG meeting deliberation and endorsement. This is documented in a guidance note on *SMEB and Setting the Transfer Values*.

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[28] World Bank (2021). US$246 Million to Support Poor and Vulnerable Lebanese Households and Build-Up the Social Safety Net Delivery System. Press Release, 12 January 2021. https://www.worldbank.org/en/news/press-release/2021/01/12/us246-million-to-support-poor-and-vulnerable-lebanese-households-and-build-up-the-social-safety-net-delivery-system

[29]Bassem Mroue (2021). Lebanese parliament approves World Bank loan to help poor. Associated Press. 12 March 2021. https://apnews.com/article/health-lebanon-coronavirus-pandemic-financial-markets-beirut-b93ab83c784de07a1c576cb77c78e442

The SMEB TWG convened in January and February 2021 to gather more evidence to inform decision-making, based on the analysis related to currency exchange rates, and the cost of the SMEB. In both locations the SMEB was above 95% of the prevailing SMEB transfer value. **The decision was therefore made to maintain two transfer values for North and South, and top up both by 20%**. This decision is due to be reviewed in April 2021.

Figure 4: Recommendation: Revision in transfer values

- Recommended Transfer Values from the TWG SMEB meeting held on 1st February 2021 are given below:

REGIONS	SOUTH	NORTH
SMEB 2020 TV	117,000	101,000
Trigger Threshold (95% of SMEB 2020 TV)	111,150	95,950
Buffer (20% of SMEB 2020 TV)	23,400	20,200
Revised Value Formula	(117,000) + (20% of 117,000)	(101,000) + (20% of 101,000)
Revised Transfer value	140,400	121,200
Recommended Rounded Off Value	141,000	122,000

6. Conclusions and Lessons Learned

Harmonization and guidance. In the context of a rather fragmented cash programming environment, the CMWG has been providing overarching guidance and harmonization guidelines on CVA across all actors and clusters. This helped to strengthen the capacity to respond to the volatile context through the development of alert systems and triggering mechanisms able to react to price inflation and erosion of purchasing power capacity.

Adaptation of the SMEB and transfer values. The SMEB TWG working group is playing a key role in informing the design of MPC for all sectors, based on monitoring of market prices and currency fluctuations. The TWG has produced clear recommendations for the review of the transfer value, which served as a trigger for amendments in transfer values. The overall analysis of 'SMEB transfer value' as a package helped decision-making to adapt MPCA programming and cope with the economic volatility.

Coordination. Efforts continue to improve the coordination of donors, UN agencies and NGOs through the CMWG and the Donor Working Group on cash. It is increasingly apparent that close strategic and technical coordination is essential to optimize programming in a context of political instability and currency volatility. Standard operating procedures, monitoring and triggering systems and preparedness will only be effective if implemented with strong coordination between partners and across programmes and platforms. Further investments in time and funding are needed in order to sustain the momentum gained.