UNLOCKING THE POTENTIAL OF THE PRIVATE SECTOR IN YEMEN

AUGUST 2023

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Economic Development Initiatives

HSA Group is committed to contributing impactfully and meaningfully to the development of our home market in line with our newly launched Economic Development Initiatives. The initiative aims to support the development of long-term sustainable solutions to the country's most pressing issues and guides our work with all stakeholders to bring about prosperity and hope for the communities we serve in our beloved Yemen.

Acknowledgements

This study is a result of a collaboration between HSA Group's Economic Development Initiatives and DeepRoot Consulting. The study team includes Adeeb Qasem (project lead), Rafat Al-Akhali and Professor Ethan Kapstein (main co-authors), Mansour Al-Bashiri and Raiman Al-Hamdani (researchers), Adra Elazzouzi and Carrie Bell (copy editors), and Mohamed Masry (art director). We would like to thank all the individuals who contributed to this study as part of the key informant interviews for their valuable contributions and insights. We are also deeply grateful to the study team members whose dedication and hard work allowed the study to emerge in its current format. Finally, the views and opinions expressed in this study do not necessarily reflect the official position of HSA Group.

ECONOMIC DEVELOPMENT INITIATIVES

FOREWORD

UNLOCKING THE POTENTIAL OF THE PRIVATE SECTOR IN YEMEN

By Nabil Hayel Saeed
Managing Director – HSA Group – Yemen

The past eight years of conflict in Yemen have resulted in a humanitarian tragedy of almost overwhelming scale. Alongside the hundreds of thousands of deaths as a result of the conflict, 17 million people are estimated to be suffering from food insecurity and 2.2 million children under the age of five suffering from acute malnutrition.

As the world struggles to alleviate this suffering, their efforts also put the spotlight on the national developmental tragedy engendered by the ongoing conflict. Although pre-conflict Yemen was riven by political and economic issues and challenges, we were a people working to free ourselves from decades of instability and insecurity to build a positive future. The conflict has brought that development to a halt and left many Yemenis dependent on vital, though necessarily short-term international aid.

Yemen's private sector, which ranged from the micro-businesses to large scale corporations, was part of that struggle for a positive future. Yemeni businesses grew the economy, created jobs, and invested in critical infrastructure. In many cases, it was also the private sector that stepped up where the public sector could not, supporting local communities with the provision of basic goods and services, including healthcare and education.

Throughout the conflict, the private sector has continued in this role, extending it yet further in many cases through philanthropy. Moreover, it has preserved the country's critical infrastructure and services, averting a collapse of the Yemeni market, and protecting lives and livelihoods. Today, as a range of stakeholders – including governments, international donors, and NGOs – strive to alleviate this humanitarian crisis and rebuild Yemen, it is time to empower Yemenis themselves through the private sector. By doing so, we can unlock prosperity for Yemen's people through focusing on long-term solutions that will resolutely address Yemen's challenges and facilitate growth.

Naturally, there are obstacles – not least the long-standing conflict, the solution to which must be a sustainable peace that moves Yemen forward on a journey to reconstruction and rehabilitation. However, others can be addressed through concerted collaboration among local authorities, the international community, NGOs, aid donors, and the private sector. This study by HSA Group's Economic Development Initiatives aims to identify solutions to these obstacles and put forward proposals that will enable Yemen's economic recovery, put an end to the strife faced by millions across the country, and give hope to its communities even in this time of despair.

With this study, we provide not only a wide-ranging analysis of the conflict's impact on Yemen's private sector, but also offer specific recommendations to local authorities, regional and international donors, and the Yemeni private sector itself to tackle challenges holding back the country's development. We also aim to foster open engagement and dialogue between all these stakeholders and ensure a coherent, concerted, and coordinated response that ultimately empowers Yemenis for the long-term.

At HSA Group, we have been operating in Yemen for 85 years. We have proudly conducted our business as well as engaging in a wide-range of philanthropic and CSR activities to support local communities. In this time, we've carried on working through social, political and economic turbulence and we're proud to be trusted by our customers, partners, and the communities we serve. The past eight years have been no different – most recently we spearheaded the International Initiative on COVID-19 in Yemen (IICY) to support Yemen's response to COVID-19.

Throughout this history, we have consistently harnessed the power of partnership and collaboration to drive sustainable development that benefits the lives and livelihoods of the Yemeni people. We are proud to publish this study and trust that our analysis and insights will inform policy discussions and make a positive and enduring impact in our home market for our people.

YEMEN'S RESILIENT PRIVATE SECTOR

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How to grow the private sector in developing economies is an area of increasing focus in academic literature and policy analysis. As a key source of innovation and productivity growth, the private sector plays a crucial role in poverty reduction and economic growth – when it is given scope to operate.

Improving access to credit and providing technical assistance are among interventions that the international community has emphasised in its efforts to catalyse private sector development. When applied to fragile and conflict-affected situations (FCAS), however, some of the assumptions guiding the previous literature and policy engagement either do not apply or must be significantly modified. Yemen, in particular, has been understudied in academia and within international development policy circles, with research challenges further amplified by the ongoing conflict.

This study is a collaboration between practitioners and experts with a breadth of academic knowledge of private sector development (PSD) and private sector engagement (PSE) in FCAS coupled with deep practical knowledge of Yemen. The study provides an analysis of the current state of Yemen's private sector, including PSD and PSE efforts, and practical recommendations for the way forward. This is guided by a rigorous analytical framework based on evidence from the academic and policy literatures in economics and international development.

Priority Interventions

- Focus on PSD interventions now, not later in the recovery process
- Engage with the private sector as a key partner, not only as a supplier, beneficiary, or a revenue source
- Consider PSD needs of MSMEs and large firms
- Address capital market failures and the quality of state institutions, while taking into consideration the political economy

The study explores four tensions facing stakeholders working on private sector issues in Yemen. The first tension relates to differing views on the timing and sequencing of PSD interventions in the conflict and recovery process. While traditional approaches have followed a phased, discrete sequence of efforts that start with relief and humanitarian assistance and turns to economic development interventions (such as PSD) at later stages, academic evidence shows that PSD interventions can and should be implemented at the very beginning of a recovery process. This is increasingly reflected, at least on paper, in the strategies and models adopted by leading development agencies such as the German Agency for International Cooperation and the United States Agency for International Development (USAID) and the UK's Department for International Development (now the Foreign, Commonwealth and Development Office - FCDO). In Yemen, foreign aid allocated to PSD categories by traditional donors has

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been less than 1% of total annual aid since 2016. Our study argues that it is time to prioritise and scale up funding of PSD interventions by government authorities and the donor community.

The second tension relates to who the target beneficiaries of any PSD interventions should be: should the focus be on informal, micro enterprises; on the 'missing middle' of small and medium-sized enterprises (SMEs); or on large firms? Analysis of donor-funded PSD projects in Yemen since 2015 shows an overwhelming concentration on micro enterprises, primarily positioned from a livelihoods improvement perspective (rather than a PSD lens). We argue that a balanced approach is required that also takes into account the PSD needs of large firms that play a leading role in supply chains and distribution networks of various sectors. These firms are more likely to innovate, upskill the workforce, and lower the cost of production through economies of scale and scope. They can also adopt 'best practices' in management and training through their linkages with the global economy, while disseminating these best practices to domestic micro, small and medium-sized enterprises (MSMEs) that provide them with goods and services.

The third tension we observe pertains to the type of PSD interventions required: should these interventions tackle capital market failures, improve the quality of a nation's institutions, or address political economy aspects? Should the interventions target the macro level (i.e., business environment or investment climate reforms), the meso level (i.e., markets and sectors, as well as intermediary organisations offering services to businesses), or be more interventionist at the enterprise level? Compared to other, primarily humanitarian programming, PSD programmes have been quite limited in Yemen. Of those programmes that address PSD, many donor interventions have primarily focused on addressing capital market failures by providing grants and/or supporting microfinance. While there have been some emerging meso-level interventions, especially related to value chain support, and a few macro-level interventions, there tends to be an overemphasis on micro-level interventionist-type support for enterprises versus both meso and macro interventions. We believe a more comprehensive approach should address the quality of the nation's institutions, particularly challenges to property rights, and address political economy concerns. It should also aim to collaborate closely with the private sector to improve the business environment and work to establish a minimum level of regulatory predictability in areas of priority to private sector operations.

The fourth tension is where the relevant stakeholders score the lowest: how can government and donors genuinely engage with the Yemeni private sector as a partner in the design, implementation, and evaluation of policies and programmes in Yemen across the humanitarian-development-peace (HDP) nexus. The international community has traditionally defined PSE in terms of engagement with multinational corporations with little focus on engagement with local firms. Interviews with private sector representatives in Yemen indicated significant frustration and a perception of an increasingly exploitative approach by the authorities towards the private sector. Interviews with all stakeholders also revealed a mutual lack of trust among the private sector, government, and donors, either due to the absence of a 'partnership' mentality or the lack of capacity to achieve it. We propose that this could be an area for quick wins if the right interventions are designed and implemented, leading to significant improvement in the response to the challenges facing Yemenis.

The study suggests that despite being severely impacted, Yemen's private sector remains vibrant and is a potential partner for the government and international community to addressing the country's challenges and initiating the recovery process. Throughout the conflict, the private sector has been the primary source of employment and economic activity, as well as playing a vital role in supporting millions of Yemenis through philanthropic and charitable activities. Moreover, it has preserved the critical infrastructure and services that prevent the markets from collapsing entirely. Our study aims to emphasise the essential role of the Yemeni private sector and encourage increased efforts to scale up PSD and PSE in Yemen.

EXECUTIVE SUMMARY

The conflict in Yemen has reversed decades of development progress, fracturing already weakened state institutions. Despite facing years of violent conflict, the private sector in Yemen has somehow managed not only to survive, but to play a crucial role in keeping the economy afloat and addressing what could have been a much worse humanitarian disaster. While Yemen's conflict is now classified as a protracted one, it is moving towards much lower levels of armed violence, presenting opportunities to support and engage the private sector more effectively, to catalyse economic activity, and help the country transition away from dependency on humanitarian relief.

While the private sector is the main source of employment and tax revenue in the country, it also plays a crucial role in supplying essential goods, upskilling the workforce, driving innovation, and providing critical infrastructure. Therefore, as in any other conflict-affected situation, the private sector in Yemen is critical to overall economic stabilisation and its growth appears to be a prerequisite for post-conflict recovery. Even during the conflict, the majority of private sector firms surveyed were able to retain their employees, with large and medium-sized businesses being the most capable of creating and sustaining jobs. Maintaining existing jobs and creating new ones is critical not only for livelihoods during the ongoing conflict but also for preserving workforce skills which are a key requirement for post-conflict recovery.

As well as the contributions of the private sector through their business operations, the study highlights the philanthropic role carried out by private sector-funded charitable and development foundations such as food distribution, infrastructure rehabilitation, funding the construction and/or operation of public education, health, and water facilities, and funding for training programmes, particularly for youth and women. Local private firms have also collaborated with the international community to establish such crucial institutions as the Yemen Food Bank and the Yemen Medicine Bank.

Furthermore, the private sector's deep connections to local communities and its long-term driven strategies provide it with local legitimacy and trusted networks that run deep across governorates, villages, tribes, and markets. This provides a seldom tapped potential for the private sector to play an important role in ongoing peacebuilding efforts. It has done so in a few cases in Yemen, such as the mediation efforts by private sector actors in relation to the FSO Safer oil tanker crisis, the advocacy for food security in light of the Ukraine crisis, and the behind-the-scenes efforts to de-escalate and contain the impact of the diverging and sometimes conflicting policies in the banking sector.

This study provides a comprehensive analysis of private enterprise during Yemen's long-standing conflict since 2015. It traces the impact of the conflict on Yemeni firms, while highlighting their ongoing contributions to the economy. Given the collapsing public sector capacity due to the conflict, private sector firms have stepped in and are playing a larger role in provision of services such as health, education, and electricity. But perhaps the most critical role played by the private sector has been its role in preventing widespread famine. Not only has the vast majority of food been imported to Yemen by the private sector (estimated at 85% of imported food in 2020), but the private sector has sustained the whole food value chain: from banks striving to maintain international banking relations to pay suppliers, to shipping companies navigating the complex shipping requirements to the ports of Yemen, to transport firms adapting to mounting challenges of inland transportation, to food manufacturers and processors maintaining their operations, and finally to the wholesale and retail sectors keeping food on the shelves across the country.

Still, the private sector in Yemen faces diverse challenges even as violence abates. Clientelism, crony capitalism, capital market failures, judicial shortcomings, and corruption have traditionally been major concerns and continue to impact the private sector in Yemen. Stability and predictability of the regulatory environment and enforcement of the rule of law is key for the private sector to function effectively and attract investments, but this is largely absent in Yemen due to the fragmentation of state institutions along conflict lines which makes coherent policy planning and execution near impossible and presents a significant challenge to private sector operations. The central bank and tax authorities, in particular, are now competing across the different regions of control in the country, resulting in double taxation and two separate currencies, further complicating private sector activities. Another major challenge constraining private sector potential in Yemen documented in this study is the mutual lack of trust between the private sector on one hand, and the public sector and the international donors on the other hand.

The study highlights the strong perception of private sector representatives of the absence of tangible efforts by public authorities to understand and attempt to address the challenges facing the private sector since the conflict started. The relationship between the public sector and private sector was perceived by interviewees as a breakdown of dialogue and a prevalence of mistrust, with private enterprises feeling constantly under pressure from formal and informal taxes and levies by different authorities and groups in power. The absence of a structured, consistent, and credible process of engagement has led to an overwhelming sentiment among private sector representatives of a lack of genuine 'desire' within the public sector to engage with the private sector, or to treat it as a credible partner in the development process in Yemen.

On analysing the PSD efforts of international donors, it is clear that international aid has focused almost exclusively on humanitarian relief since the beginning of the conflict in Yemen. Evidence shows that at its highest (in 2022), foreign aid allocated to PSD categories represented only 0.99% of total foreign aid to Yemen. The majority of donor-funded programmes have primarily focused on direct support to microenterprises, providing them with capacity building and access to finance services. This has left a gap in addressing business environment challenges, tackling political economy considerations, and addressing the needs of large enterprises which play a critical role in creating jobs and sustaining economic activity.

When it comes to PSE, and despite a few programmatic attempts, international donors lag behind in this area and there is room for significant improvement in engaging with the Yemeni private sector as partners to jointly analyse challenges facing humanitarian and development efforts, co-design possible solutions, and co-implement these solutions.

This study provides the following recommendations to the various stakeholders engaged with PSD and PSE in Yemen:

To Government Authorities:

- Avoid escalatory and polarising economic measures
- Establish a clear process for public-private dialogue (PPD)
- Develop a clear strategy towards economic stabilization, recovery and development, and towards incentivizing the private sector to invest and curb the outflow of local capital
- Focus on what is actionable within existing legal and institutional frameworks
- Identify key infrastructure projects that can be invested in by the private sector
- Assess the feasibility of re-launching some of the industrial zones

To the Private Sector:

- Organise effectively to make demands on the government and international community
- Prioritise and scale up efforts to influence international aid policy towards Yemen
- Make tangible improvements in corporate governance and compliance policies and practices
- Continue and better organise the private sector's leading role in humanitarian relief and development efforts

To Regional and International Donors:

- Prioritise and scale up PSD interventions
- Engage actively with the private sector
- Follow a balanced approach addressing MSMEs as well as large firms
- Leverage the array of institutions and instruments available to support private sector
- Work at both national and local levels
- Improve understanding of the Yemeni economy through deploying and scaling up analytical tools, methodologies, and frameworks to guide interventions

INTRODUCTION

Private Sector Development (PSD) and Private Sector Engagement (PSE) have become the object of growing attention from the international donor community in recent years, given their role in generating jobs and tax revenues and in promoting innovation, which in turn fuels productivity and growth. Academic research and policy experience, however, suggest that the barriers to PSD and PSE can prove daunting in some country settings.[3] Beyond the small size of the market that characterises many developing countries, and the various domestic and international barriers that still impede participation in the global economy, companies may face such political-economic impediments as clientelism or 'crony capitalism', capital market failures, judicial shortcomings, and the ever-present threat of corruption.

In fragile and conflict-affected states (FCAS), such as Yemen, the challenges to the private sector are likely to be even more acute, starting with threats to security and property rights which may influence not only the investment decisions of entrepreneurs but also the geographic scope of business activity and the allocation of labour.

While not enough empirical research exists on the behaviour of firms in the Yemeni context, it is evident that the ongoing conflict since 2015 has severely impacted all economic activities in the country. The weakening and fragmentation of public sector institutions due to the conflict has significantly reduced their contribution to the economy, while the private sector has been facing tremendous conflict-related challenges to continue operations. This study aims to provide insights into how conflict has affected the industrial organisation of firms in Yemen, and what the implications of this are for government and donor programming that seek to support PSD and PSE in the country. The study also seeks to provide vital information and actionable policy recommendations for a range of stakeholders in order to unlock the full potential of the private sector within the constraints of the current fragile context.

In this study we emphasise the role of the formal as opposed to the informal sector of the economy. While we recognise that the informal sector employs many more people in developing countries around the world, particularly in FCAS like Yemen, our focus stems from the fact that it is formal firms that are likely to be the major drivers of growth, innovation, and productivity, along with being major contributors to tax revenues, and credible counterparts for engagement efforts. For that reason, this study also highlights the role of large firms, a relatively understudied topic in the relevant literature, and a generally overlooked stakeholder among humanitarian and development agencies with the exception of Development Finance Institutions (DFIs) such as the International Finance Corporation (IFC).

The specific objectives of the study are to:

- Document, analyse, and evaluate the role of the private sector in job creation, economic stabilisation, and addressing the humanitarian crisis in Yemen since 2015.
- Develop an analytical framework based on the academic and policy literatures to assess the impacts of conflict at an enterprise level, and to evaluate approaches to PSD and PSE in FCAS.
- Provide in-depth analysis of the impact of the conflict on firms in Yemen, and the key barriers limiting the private sector from reaching its potential in participating in Yemen's economic stability, recovery, and development.
- Identify and analyse government-led and donor-led efforts in the field of PSD and PSE in Yemen.
- Based on the context in Yemen and lessons from experiences in similar FCAS, identify key sectors and opportunities for PSD and PSE, and develop concrete, practical, and feasible recommendations to key stakeholders (government entities, international community, private sector) on how to realise these opportunities and unlock private sector potential in Yemen on the short, medium, and long term.

3 Mary Hallward-Driemeier and Lant Pritchett, "How Business Is Done in the Developing World: Deals versus Rules," Journal of Economic Perspectives 29, no. 3, 2015: 121–40.

The main sources of information used in this study include primary and secondary data. Secondary data was collected through a review of available literature on topics of PSD and PSE in Yemen and in FCAS. The data included online and offline Arabic and English reports, policy papers, and data sets, among others. Primary data was collected through 26 key informant interviews (KIIs) conducted between November 2022 and January 2023 with local and international specialists, representatives of government authorities, representatives of the private sector, members of relevant local and international development organisations, as well as other stakeholders.

This study is divided into two parts. Part 1 consists of six sections. Section 1 highlights private sector contributions to Yemen's economy since 2015, including to jobs, humanitarian relief efforts, and to preservation of critical markets such as food, banking, and telecommunications. In section 2, the key challenges facing the private sector in Yemen are summarised, while section 3 presents the impact of the conflict at an enterprise level in Yemen. Section 4 maps donor-led and public sector-led efforts in PSD in Yemen since 2015. Section 5 provides an assessment of donor-led and public sector-led PSE efforts in Yemen. Section 6 concludes with key recommendations to public sector authorities, private sector firms, and international development agencies and donors.

Part 2 presents the analytical framework underpinning this study. It captures key findings from academic research and policy analysis on the private sector in FCAS, understanding the impact of conflict at enterprise level, traditional foreign assistance approaches to PSD especially in conflict-affected situations, and the different definitions of PSE internationally

PART 1:

UNDERSTANDING THE PRIVATE SECTOR IN YEMEN

1. Role of the Private Sector in Yemen since 2015

As the major generator of jobs and, at least in cases where firms are formalised, tax revenues, the private sector plays a key role in producing not just private goods, but the resources needed for improving the well-being of society as a whole. Indeed, training programmes, innovation, and infrastructure, among other aspects of ongoing business operations, contribute not just to the firm's bottom line, but to societal well-being more broadly. Therefore, because of its role in employment, innovation, tax revenues, public goods and, in the case of export-oriented industries, foreign exchange generation, the private sector is critical to overall economic stabilisation in conflict-affected situations, and its growth seems to be a pre-condition for any post-conflict recovery. Beyond these economic outcomes, the private sector's deep connections to local communities and its long-term driven strategies provides it with local legitimacy and trusted networks that run deep across society. It therefore has the potential to play a crucial and direct role in 'supporting the state's peacebuilding efforts' and strengthening 'the state's legitimacy…'.[4] In the following sections, we explore the diverse contributions of the private sector in Yemen since the beginning of the conflict.

1.1 Overall contribution to the Gross Domestic Product (GDP)

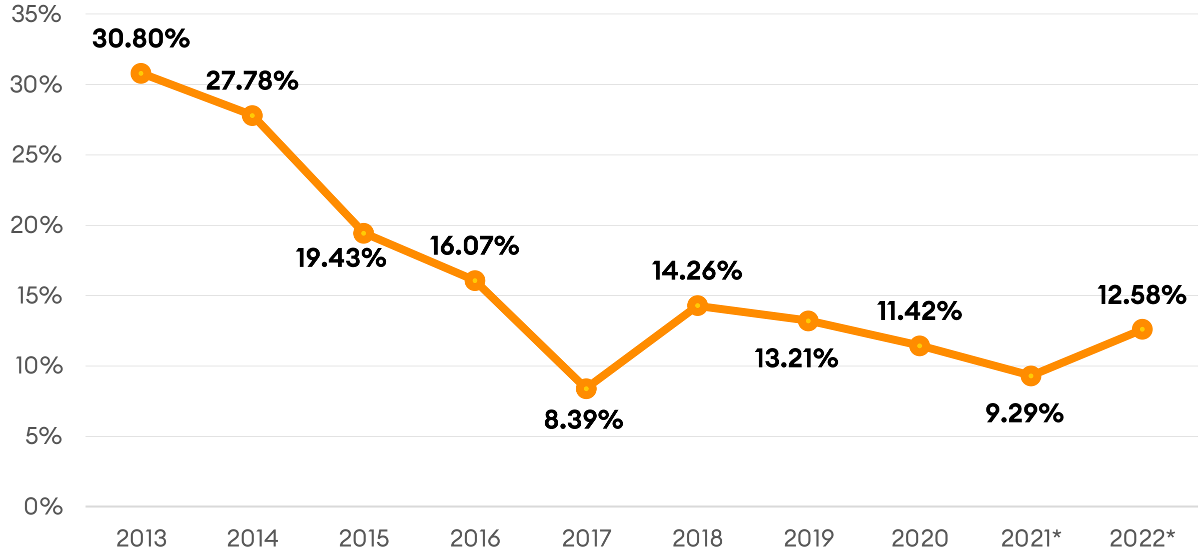
Despite the constraints on the private sector in Yemen and the impacts of the ongoing conflict (which are explored in later sections of this study), the contribution of the private sector to the economy continues to be significant. Prior to 2015, it is estimated that Yemen's private sector generated approximately 70% of all jobs in the country and generated more than 50% of the GDP.[5],[6] While exact and verified data is difficult to obtain, estimates from a number of sources show that the contribution of the private sector to the GDP has increased by approximately 15% relative to government contribution (reaching over 70%). Figures 1 and 2 present the GDP data from the International Monetary Fund (IMF) and the Yemeni Central Statistics Office, and Table 1 presents the percentage of private sector contribution to main economic sectors at constant prices.

4 William Robert Avis, "Private Sector Engagement in Fragile and Conflict-Affected Settings", GSDRC Helpdesk Research Report 1331. January 2016. http://gsdrc.org/publications/private-sector-engagement-in-fragile-and-conflict-affected-settings/

5 "Yemen Labour Force Survey 2013-2014", International Labour Organisation. 2015. https://www.ilo.org/wcmsp5/groups/public/---arabstates/---ro-beirut/documents/publication/wcms_419016.pdf

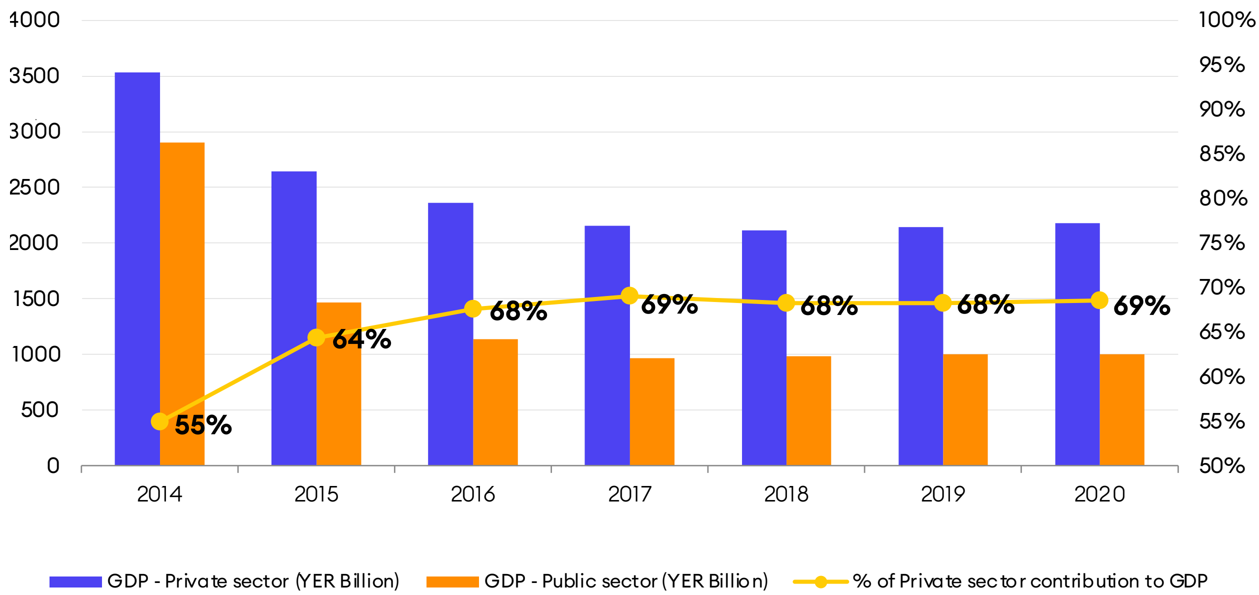
6 Nasser Amal, "Beyond the Business as Usual Approach: Private Sector Engagement in Post-Conflict Yemen", Rethinking Yemen's Economy. Development Champions. August 2018. https://devchampions.org/uploads/publications/files/Rethinking%20Yemen's%20Economy%20No3.pdf

Figure 1 Government expenditure as % of GDP



Source: IMF Website. 'World Economic Outlook Database.'
** 2021 and 2022 data reflect projections while other years are actuals*

Figure 2 Private sector contribution to real GDP (YER Billion & %)



Source: Central Statistics Office. 'National Accounts Book 2020.'

Table 1 Private sector contribution to main economic sectors at constant prices (%)

Description/Year		2014	2015	2016	2017	2018	2019	2020
Agriculture, Forestry and Fishing	Public sector	0	0	0	0	0	0	0
	Private sector	100	100	100	100	100	100	100
Manufacturing	Public sector	10	9	9	9	9	9	9
	Private sector	90	91	91	91	91	91	91
Construction	Public sector	36	30	30	27	27	27	32
	Private sector	64	70	70	73	73	73	68
Services	Public sector	40	33	33	30	30	30	30
	Private sector	60	67	67	70	70	70	70

Source: Central Statistics Office. 'National Accounts Book 2020.

1.2 Contribution to jobs

In addition, the non-payment or non-regular payment of public sector salaries has become a major issue due to the ongoing conflict in Yemen, and therefore the vast majority of meaningful jobs available are those in the private sector (from microenterprises to jobs generated by small, medium, and large enterprises). This is reflected in the results of a 2020 survey which showed that as many as 61.6% of the private sector enterprises that participated in the survey had retained their employees and avoided any layoffs, and an additional 21.2% reported increasing the number of permanent employees, with large and medium enterprises being the most capable of creating and sustaining jobs.[7] Retaining existing jobs and creating new ones are not only critical to livelihoods during the ongoing conflict, but are also key to preserving workforce skills which are a key requirement for post-conflict recovery.

1.3 Contribution to humanitarian relief efforts

Beyond their contribution to economic activity and jobs through their business operations, many private sector enterprises have played a significant part in addressing the humanitarian situation in Yemen through philanthropic initiatives, whether through informal charitable donations that almost all business people in Yemen engage in, or through formalised charitable organisations set up by some of the businesses such as the Hayel Saeed Anam Charitable Foundation, the Bazara Charitable and Development Foundation, Al-Khair Foundation for Social Development[8], Al-Naqeeb Charitable and Development Foundation among many others. This contribution is acknowledged by international donors, with one donor representative stating that 'without the direct contributions of the private sector, the humanitarian situation in Yemen would have been much worse',[9] and the World Food Programme (WFP) country director stating that 'when you feed 20 million people, you are deeply in bed with the commercial sector'.[10] Initiatives implemented by private sector-funded charitable and development foundations include food

7 SMEPS, "Yemen Business Climate Survey Report 2020," The Social Fund for Development, Yemen and Foreign, Commonwealth & Development Office, UK, 2020. https://smeps.org.ye/upfiles/posts/SMEPS_File_17-12-2020-8842.pdf

8 Established by the Universal Group of Companies.

9 Interview with Foreign Aid official, Yemen, Feb 20, 2023.

10 Chloe Sorvino, "Skirting Russian Black Sea Blockade To Feed The World's Hungriest Is Mission Of Yemen's Biggest Company." Forbes Magazine, June 7, 2022. https://www.forbes.com/sites/chloesorvino/2022/06/07/skirting-russian-black-sea-blockade-to-feed-the-worlds-hungriest-is-mission-of-yemens-biggest-company/?sh=17d124223bee

basket donations, rehabilitation of infrastructure, funding the construction and/or operation of education, health and water facilities, and funding of training programmes especially for youth and women. Philanthropic and charitable work is seen as an integral value to many private sector actors in Yemen, but there is little literature evaluating this work, its impact, and how to improve it, which could be due in part to the majority of private sector actors adopting traditional approaches to charity which does not necessarily prioritise impact.

In addition to the efforts and contributions by individual private sector-funded foundations, the past few years has witnessed a number of successful collaborative initiatives bringing together multiple private sector enterprises for humanitarian and development purposes. These initiatives include the Yemen Food Bank and the Yemen Medicine Bank which are presented in detail below. Another innovative example is the International Initiative on COVID-19 in Yemen (IICY) convened by HSA Group. The initiative was a private sector-led collaborative partnership of Yemeni and multinational businesses and international organisations that has supported Yemen's response to COVID-19.[11] IICY was launched in just 3 weeks, a testament to the ability of the private sector to deploy its resources and know-how to respond rapidly in moments of crisis.

Table 2 The Food Bank and the Medicine Bank in Yemen

	Food Bank	Medicine Bank
Year of establishment	2017	2018
Mandate and scope of operations	An independent humanitarian, non-profit, developmental, neutral, and civil society organisation. It was established under the Ministry of Social Affairs and Labour. It works to combat hunger.	A non-profit charitable institution that aims to provide emergency, health and drug services for the most vulnerable groups, as well as ensuring their access to these services.
Number of beneficiaries	865,728 (to date)	137,486 (to date)
Project value ($)	637,000 (in 2022 alone)	1,245,099 (to date)
Relevant projects	To date, the Food Bank has undertaken 19 projects with 250 volunteers. Example projects include the Ramadan Community Kitchens, food baskets for the displaced, and school sandwiches for students to help combat child malnutrition.	To date, the Medicine Bank has undertaken 6 projects. Example projects include an education, water, and environmental sanitation programme, a nutrition programme, a medical services programme, a capacity-building programme and an awareness and health education programme.
Relevant partners	The Chambers of Commerce and Industry in Sanaa, The Federation of Yemen Chambers of Commerce, Nestlé, Tayseer Arar Food Industries, and The International Red Cross, among others.	The Bazara Foundation, the Hayel Saeed Foundation, the Al-Khair Foundation, and the Yemeni Doctors Union in Germany, among others.

Source: KIIs; Food Bank and Medicines Bank websites.[12]

11 IICY webpage, "International Initiative on COVID-19 in Yemen." https://www.iicyemen.org/

12 See https://yemenfoodbank.org/ and https://yemenmedicinebank.org/

1.4 Contribution to preservation of markets and services

Perhaps the most significant contribution of the private sector in Yemen during the conflict has been preserving the sinews of the economy: the critical infrastructure and services that prevent the complete collapse of markets. For example, businesses, citizens, and humanitarian relief efforts continue to benefit from mobile telecommunication services largely provided by private operators. In addition, when the Public Electricity Corporation (PEC) was no longer able to supply electricity, private operators filled the gap and provided electricity directly to consumers, and to the PEC. In the health and education sectors, the private sector owned over 60% of the country's health facilities in 2014, while over a quarter of students (83,177 out of 310,340) were studying in private higher education institutions in 2014.[13] Although updated statistics are not available, the share of the private sector in the health and education sectors is expected to have increased since the beginning of the conflict due to the challenges facing public health and education facilities especially related to payment of public salaries.

But perhaps the role of the private sector in preserving markets has been most critical in the food sector, which presents an inspiring story of private sector resilience and its significant role in averting famine in Yemen, a story often overlooked in media coverage related to the ongoing humanitarian crisis which predominantly focuses on international humanitarian efforts. Despite the increased presence of international humanitarian NGOs and UN agencies in Yemen since 2015, the Yemeni private sector remains the dominating actor in the food sector in the country. For example, in 2020, the private sector is estimated to have imported approximately 85% of the 6.1 million tonnes of food reaching Yemen, with the remaining 0.9 tonnes (mostly wheat) imported by humanitarian agencies, which remain reliant on the private sector to store, distribute, or mill wheat.[14]

The private sector in Yemen has contributed significantly towards addressing the different dimensions of the food insecurity challenge.[15] Commercial banks have managed to maintain international banking relationships, which has allowed Yemeni food importers to continue making payments to their international suppliers. The shipping sector has been able to navigate the complex and constantly changing requirements for goods to reach Yemen. The inland transport sector has been adapting to mounting challenges from damaged road infrastructure, to skyrocketing fuel prices, to checkpoints controlled by different authorities, and to illegal levies by security factions. The food manufacturing sector has continued to operate and supply the market despite the multiple security, taxation, transportation, and macroeconomic challenges. Finally, the wholesale and retail sector has avoided collapse, maintaining food on the shelves across the country.

13 Ministry of Planning and International Cooperation, "Yemen Socio-Economic Update", Issue 35, July 2018. https://reliefweb.int/report/yemen/yemen-2018-socio-economic-update-issue-35-july-2018

14 Edward Thomas, "Food Security in Yemen: the private sector and imported food," ODI, February 2022. https://cdn.odi.org/media/documents/Food_security_in_Yemen_1_-_the_private_sector_and_imported_food_uTu5YXS.pdf

15 HSA Group, "Responding to Yemen's Food and Security Crisis: Insights and Perspectives from the Private Sector," HSA Group, November 2022. https://www.hsayemen.com

Box 1 Manufacturing in Yemen The first major shift in the manufacturing sector in Yemen started in the 1970s. The government encouraged private sector investments in large scale manufacturing and protected the sector by imposing import restrictions and high tariffs on foreign goods. As a result, the size and scope of manufacturing businesses began to increase throughout the 1970s and 1980s. However, by the mid 1990s, there was a significant change in the industrial strategy as the government liberated trade, lifted restrictions on import licenses, and reduced tariffs in an attempt to integrate into the global economy. The industrial sector was left to fend for itself, hindering its growth and development. Liberalization didn't happen with the needed support for local manufacturers to stay competitive given the poor incentive framework and weak institutions which constrained manufacturing activities, along with weak infrastructure (power, roads, water), high production costs, and weak legal and judicial systems.[16]

While the manufacturing sector contributes 10% to Yemen's GDP, the ongoing conflict has further exacerbated the challenges it faces. Manufacturing capabilities have been eroding with some factories damaged or forced to close, jeopardizing existing industrial capacity and hindering potential recovery, and impacting development agendas. The business environment, standards, and regulatory frameworks have suffered due to the ongoing conflict. Cumulative economic losses in the sector between 2015 and 2020 amounted to approximately US$4.5 billion for private actors.[17]

The structure of the manufacturing sector is characterized by the predominance of small businesses, which represent about 89% of the sector, compared to about 9% for medium-sized enterprises and only about 2% of large ones. However, it is large enterprises that contribute the bulk of the sector's output (65.3%), and employ about 36% of the total workforce in the sector. [18]

Yemeni manufacturers confront several obstacles that hamper their competitiveness. More specifically, distorted market dynamics, logistical constraints, fuel prices, and shipping and transportation challenges contribute to increased inputs and manufacturing costs. In addition, opportunistic import practices, including dumping, increases in the volume of imports, an influx of cheap and low-quality products that target vulnerable Yemeni consumers with reduced purchasing power, all harm local industries.

While Yemen exports have plummeted by 90%, primarily due to the cessation of oil exports, imports have rebounded to pre-conflict levels and continue to grow. Major import categories include food and agricultural goods, textiles, and vehicles.[19]

Meanwhile, the regional competitive landscape is changing, with other countries in the region focusing on their industrial strategies by developing special economic zones and offering a wide-range of incentives for investors in a bid to improve their competitiveness and substantially boost their exports, further increasing pressure on local manufacturing capacity in Yemen.[20]

Having a strong manufacturing industry is, now more than ever, crucial for Yemen's economic recovery, stability, and growth. Industrialization and manufacturing contribute to economic growth and sustainable development, poverty reduction, and increased stability in fragile and conflict-affected states. Today, Yemen's manufacturing sector is at a critical juncture, facing a decline or the potential for revitalization to support the country's economic recovery. Therefore, addressing structural challenges, protecting local industries from unfair competition, and promoting investment in manufacturing are essential for long-term economic development in Yemen.

In addition to the above, the role played by the Yemen Banks Association and the leaders of private banks in Yemen has been critical in de-escalating the conflict in the banking sector in the country between the competing central bank administrations in Sana'a and Aden.

16 Aamer, Ammar, (2015), "Manufacturing in Yemen: Challenges and Obstacles", Academic Journal of Research in Economics and Management, 7,119-142.

17 (2022), "Indicators of the performance of the industrial sector in Yemen in light of conflict and war", Federation Of Yemen Chambers of Commerce and Industry, (FYCCI)

18 Ibid

19 The Atlas of Economic Complexity (harvard.edu)

20 In 2022 KSA launched its "Saudi National Industry Strategy", similarly UAE launched its industrial strategy "Operation 300bn" in 2021, and Oman in 2019. All have strong focus on exports and along with strong incentive packages through special economic zones.

While not all the details of this important mediation and de-escalation role have been made public due to the sensitive nature of the topic, these efforts can serve as an example of the significant but undervalued role of the private sector in peacebuilding efforts in Yemen.

2. Constraints Facing Yemen's Private Sector

The deteriorating situation in Yemen since the beginning of the conflict has been clearly reflected in the business environment. Yemen ranked 187 out of 190 countries in the World Bank's 2020 'Doing Business' report, with only Venezuela, Eritrea and Somalia having worse rankings.[21] Figure 3 presents the deterioration of Yemen's ranking in the 'Doing Business' report between 2012 and 2020.

In the interviews conducted for this study, all private sector interviewees ranked their highest challenge as the fragmentation of state institutions along conflict lines, most notably the central bank and tax authorities, and the resulting conflicting policies and regulations set by these competing institutions which have subsequently led to, among other things, double taxations and two separate currencies in the country. Ranked also as highly in the interviews were the security challenges and illegal levies by multiple authorities, especially for commercial goods that need to be transported between cities.

The results from the interviews are in line with a business climate survey conducted by the Small and Micro Enterprise Promotion Service (SMEPS) of the Social Fund for Development (SFD) and the UK's FCDO in 2020 which surveyed 3,613 businesses in 14 governorates.[22] Respondents to the 2020 survey identified more than 30 constraints that businesses face, which the survey authors categorised into seven categories. Table 3 below presents these categories and the corresponding percentage of respondents to the 2020 survey who classified them as a major constraint. Categories 2 and 6 correspond to what was classified by interviewees for this study as state fragmentation, while categories 4 and 5 correspond to what was classified by interviewees for this study as security challenges and illegal levies. It is worth noting that 'change in demand' and 'supply distortion' which featured highly in the 2020 survey were not mentioned by interview respondents for this study . This could either be due to differences in the sample or that enterprises have now adapted to the new levels of demand and the supply distortions and no longer think of them as constraints. It is also worth noting that access to finance was ranked last in the 2020 survey with only 28.7% of the respondents classifying it as a major constraint, and was not mentioned in the interviews conducted for this study.

2.1 Mutual lack of trust as a major constraint

An additional constraint expressed by the interviewed respondents was a lack of mutual trust between the private sector, the public sector, and international donors. In the absence of a 'partnership' mentality within public authorities, there are many missed opportunities for public-private collaborations therefore private sector representatives stressed on the need to unlock the power of partnership and explore opportunities for public-private collaborations, which can deliver the investment, development and services that are essential for economic growth and recovery. This same perception is expressed by private sector representatives regarding the international donor community, which seems to view the private sector through a lens of a service provider, and at worst perceived to be competing with the private sector according to interviews. Research and interviews revealed that there is currently no active platform for PSE in humanitarian and development efforts, such as a regularly convened forum that brings together key private sector stakeholders and international donors and their implementing partners to jointly analyse challenges facing humanitarian and development efforts, co-design and co-implement possible solutions.

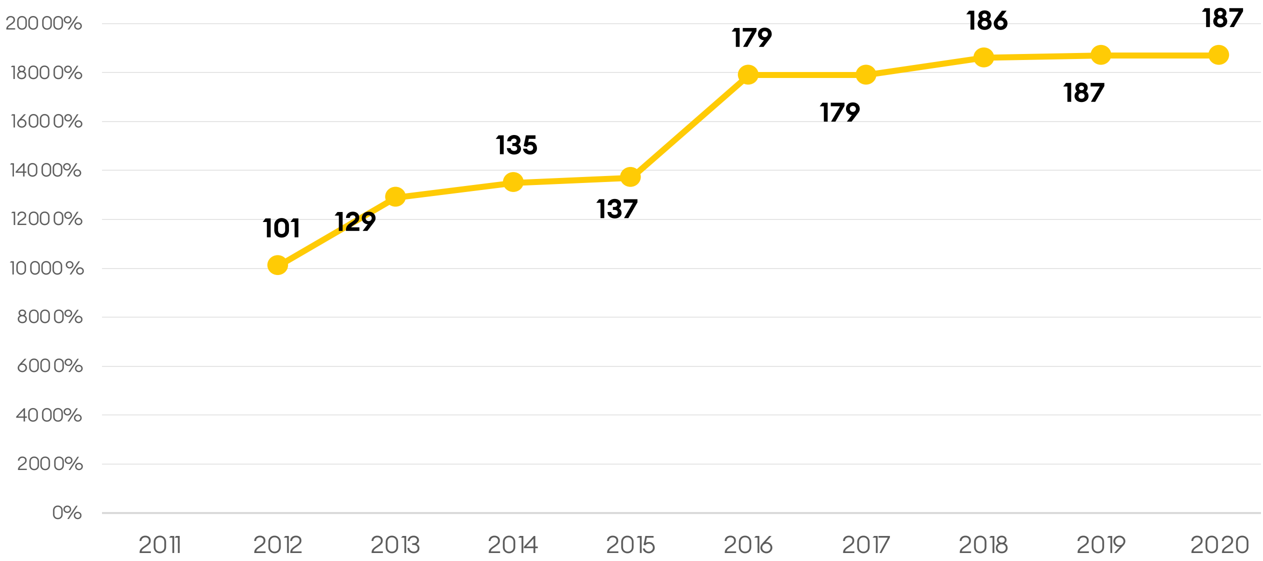
21 World Bank, "Doing Business Report 2019: Training for Reform," World Bank, 16th Edition, 2019. https://www.worldbank.org/content/dam/doingBusiness/media/Annual-Reports/English/DB2019-report_web-version.pdf

22 SMEPS, "Yemen Business Climate Survey Report 2020," The Social Fund for Development, Yemen and Foreign, Commonwealth & Development Office, UK, 2020. https://smeps.org.ye/upfiles/posts/SMEPS_File_17-12-2020-8842.pdf

Table 3 Constraint categories (%)

No.	Categories of Constraints	% Respondents listing as a major constraint
1.	Change in demand	50.2
2.	Economic warfare (local currency bifurcation, banking sector, exchange rate instability)	38.3
3.	Supply distortion	36.3
4.	Import restrictions (land and seaport closures, increased transport costs, import bans)	36
5.	Conflict (physical damage, loss of documents, lack of electricity, infrastructure damage, security, checkpoints)	31.4
6.	State fragmentation	30.6
7.	Access to finance	28.7

Figure 3 Yemen's rank in the World Bank's 'Doing Business Index 2012-2020'



Source: World Bank Website. 'Doing Business Index 2012-2020'. www.doingbusiness.org

3. Impact of the Conflict at Enterprise Level in Yemen

As defined by our analytical framework (Annex 1 of this paper), the impact of the conflict in Yemen at enterprise level can be analysed along the four dimensions shown in Figure 4.[23] Given the scarcity of quantitative surveys in Yemen, the study has relied primarily on analysing the results from two quantitative surveys conducted in 2019 and 2020 by the World Bank and SMEPS, respectively, to quantify the impact of the conflict at enterprise level, and to find new insights based on the analytical framework, the interview results, and supplementary data from other sources such as the General Investment Authority.

Figure 4 Impact of conflict at enterprise level

3.1 Impact on level of investment

One of the major channels through which violent conflict may limit firms' activities and economic growth is via reduced investment. A World Bank 2019 survey showed that only 13.5% of firms had made investments since the outbreak of the conflict in Yemen in 2015.[24] Data from the General Investment Authority in Yemen confirms this trend of falling investment. As shown in Figure 5, 142 investment projects were registered in 2013, but only 31 projects were registered in 2020.[25]

However, the breakdown of investments by firm size shows a significant disparity, with over 56.3% of large firms making investments, compared to only 6.1% and 14.8% of small and medium firms respectively making investments according to a 2019 survey.[26] These data show that large firms have better capabilities to withstand the challenges presented by the conflict and continue to find opportunities in the country, thus creating jobs and sustaining economic activity, and therefore play an important role that should be supported by PSD and PSE efforts in the country.

3.2 Impact on size of firms

Looking at the impact on size of firms, data from Yemen confirms the findings from the literature that larger firms are better able to adapt to a conflict situation and survive, as noted in the previous section. Of the 140 enterprises surveyed in 2012 and again in 2018, only one downsized from large to medium, while 21 downsized from medium to small, and 42 downsized from small to micro.[27] This trend is confirmed by another survey which shows that 23.7% of micro businesses reported a positive change in capital between 2017–2019, compared to 27.9% of small businesses, 33.9% of medium-sized businesses, and 42.1% for large enterprises. The survey concludes that 'this indicates that the larger the business, the better they are able to weather the storms which the business environment has thrown at them and leverage their networks to grow'.[28]

23 Part 2 provides a detailed description of the analytical framework.

24 Sami Sofan, "Yemen Bringing Back Business Project: Risky Business - Impact of Conflict on Private Enterprises," World Bank, 2019. https://openknowledge.worldbank.org/handle/10986/32048?locale-attribute=en

25 General Investment Authority Yemen, "General Investment Authority 2006–2020".

26 Sami Sofan, "Yemen Bringing Back Business Project: Risky Business - Impact of Conflict on Private Enterprises," World Bank, 2019. https://openknowledge.worldbank.org/handle/10986/32048?locale-attribute=en

27 Sami Sofan, "Risky Business – Impact of Conflict in Private Enterprises," 2019.

28 SMEPS, "Yemen Business Climate Survey Report 2020," The Social Fund for Development, Yemen and Foreign, Commonwealth & Development Office, UK, 2020. https://smeps.org.ye/upfiles/posts/SMEPS_File_17-12-2020-8842.pdf

3.3 Impact on location of firms

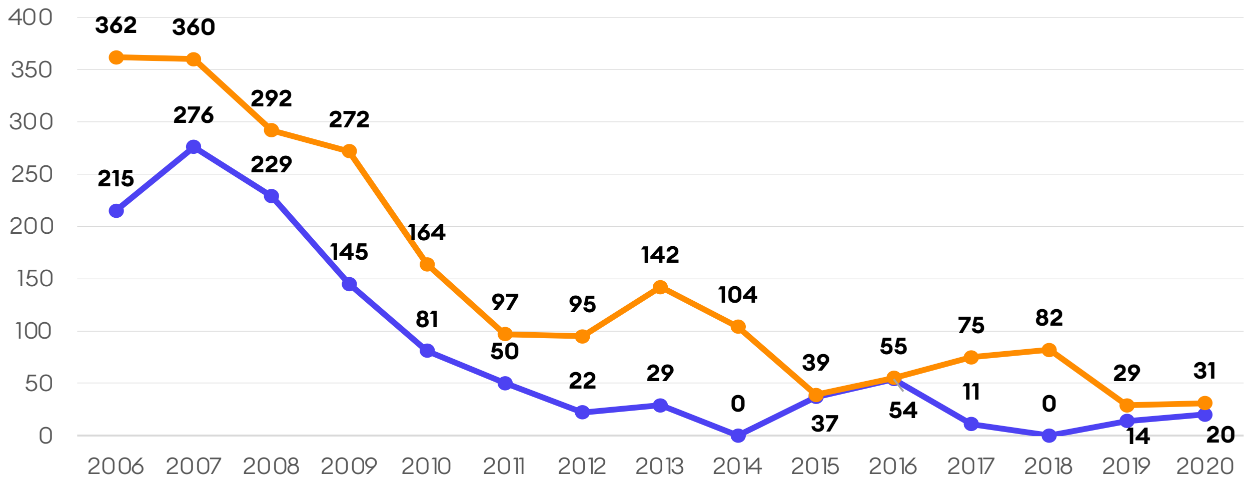
Despite pockets of relative stability in the country, private sector representatives interviewed for this study did not have a strong preference for investment in one region of Yemen over another, repeatedly citing different types of challenges faced in each of the regions/governorates, including criminal violence, exorbitant levies and taxation, violent conflict, corruption and lack of a supporting environment by public authorities, and shortage of scale of demand and economic activity.

Data from a number of surveys provide further nuance to statements made by this study's interviewees. The data show that 17% of surveyed firms have been forced to relocate within Yemen, citing security issues in conflict zones, economic recession, and financial problems. They also show that in some stable governorates (such as Ibb), surveyed firms were actually able to grow from small to medium or medium to large, while 40.9% of firms in Aden and 26.3% of firms in Hadramout boosted investment.[29] Surveys also show that while only 23% of businesses have been able to raise capital to sustain and expand their businesses, 'firms located in Sana'a (Amanat Al-Asima) and Hadramout faired best, in part due to relative stability and a bigger base of customers possessing a comparatively higher purchasing power than in other regions.'[30]

3.4 Impact on allocation of labour

Finally, with regards to allocation of labour and investment away from production and into protection, data shows that 26.2% of surveyed enterprises observed an increase in the costs of security, of which 56.7% noted an increase of over 50%. Additionally, 20.6% of firms suffered further losses from theft and vandalism.[31] This was also confirmed by the interviews conducted for this study. For example, one interviewee highlighted that inland transportation now consumes 12 to 15% of the total cost of manufactured goods in Yemen due to the security situation, while it would normally range between 1 to 2%, clearly displaying the 'misallocation' of resources from production to protection of assets.

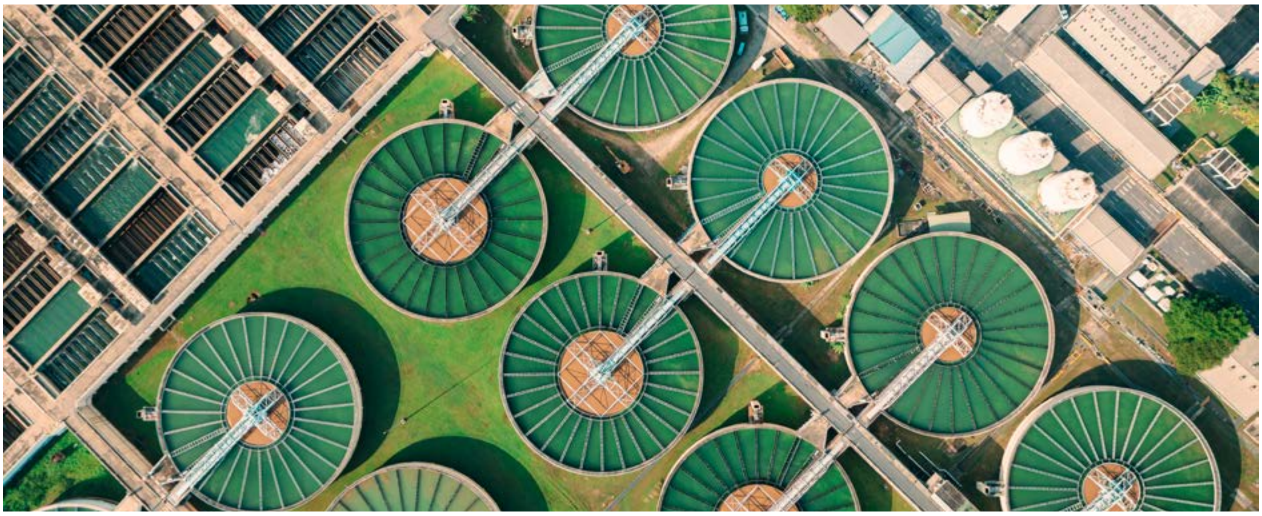
Figure 5 Projects registered and implemented/under implementation at the General Investment Authority 2006-2020



29 Sami Sofan, "Yemen Bringing Back Business Project: Risky Business - Impact of Conflict on Private Enterprises," World Bank, 2019. https://openknowledge.worldbank.org/handle/10986/32048?locale-attribute=en

30 SMEPS, "Yemen Business Climate Survey Report 2020." https://smeps.org.ye/upfiles/posts/SMEPS_File_17-12-2020-8842.pdf

31 Sami Sofan, "Risky Business – Impact of Conflict in Private Enterprises," 2019. https://openknowledge.worldbank.org/handle/10986/32048?locale-attribute=en



Source: General Investment Authority

4. Private Sector Development (PSD) in Yemen

PSD is defined by the Donor Committee for Enterprise Development (DCED) as the range of strategies that aim to establish markets that function vibrantly and fairly, providing economic opportunities of quality to poor people at scale.[32] The following sections will assess government-led and donor-led approaches to PSD in Yemen, guided by the analytical framework detailed in Annex 1.

4.1 Public sector-led efforts in the field of PSD

Interviews with private sector representatives, government officials, and other economic specialists revealed a gap between expectations and reality as it relates to the efforts by public authorities to understand and address the challenges facing the private sector since the conflict started, such as access to manufacturing inputs, movement of goods, access to markets, and other challenges. The majority of private sector representatives report being constantly under pressure from formal and informal taxes and levies by different authorities and groups in power. In addition, some sectors (such as banking and telecommunication) have increasingly become the target of escalatory and retaliatory actions between the two authorities in Sana'a and Aden.

Conversely, there have been some notable measures announced by the different authorities. For example, in 2019, the Yemen Customs Authority in Aden announced the launch of the 'Authorised Economic Operator' programme with support from USAID which facilitates faster processing at ports for goods imported by certified companies. Since 2018, the Central Bank of Yemen (CBY) in Aden has dedicated a Saudi deposit to cover the foreign currency needs of Yemeni food importers. In May 2020, the authorities in Sana'a proclaimed two decrees waiving custom taxes on production inputs for manufacturing of medicines and medical appliances and manufacturing of renewable energy generation equipment, as well as waiving custom taxes on renewable energy systems components and electric/hybrid cars.[33] Also in May 2020, a further decree was announced in Sana'a waiving profit tax on small and micro enterprises who have less than 20 million Yemeni Rials (YER) in annual revenues as well as waiving salaries tax on their employees. In 2018, the Ministry of Industry and Trade in Sana'a launched a single window system, streamlining the registration process for entrepreneurs and start-ups.[34]

Despite these examples, complicated procedures, ineffective implementation, and the mutual lack of trust between the private and public sectors overshadow any positive impact from these initiatives.

32 DCED, "Synthesis Note: Private Sector Development," Donor Committee for Enterprise Development, March 2019. https://www.enterprise-development.org/wp-content/uploads/PrivateSectorDevelopment.pdf

33 Government of Yemen, "Issuance of a law on exempting pharmaceutical production inputs and renewable energy from fees and Law No. (41) of customs tariff amendment," Yemen Customers Authority, Government of Yemen, 2020. https://customs.gov.ye/news/Details/1050

34 Spark, "One Window System: Entrepreneurs become tax exempt in Yemen," Spark, June 5, 2018. https://spark.ngo/one-window-system-entrepreneurs-become-tax-exempt-yemen

4.2 Donor-led efforts regarding to PSD in Yemen

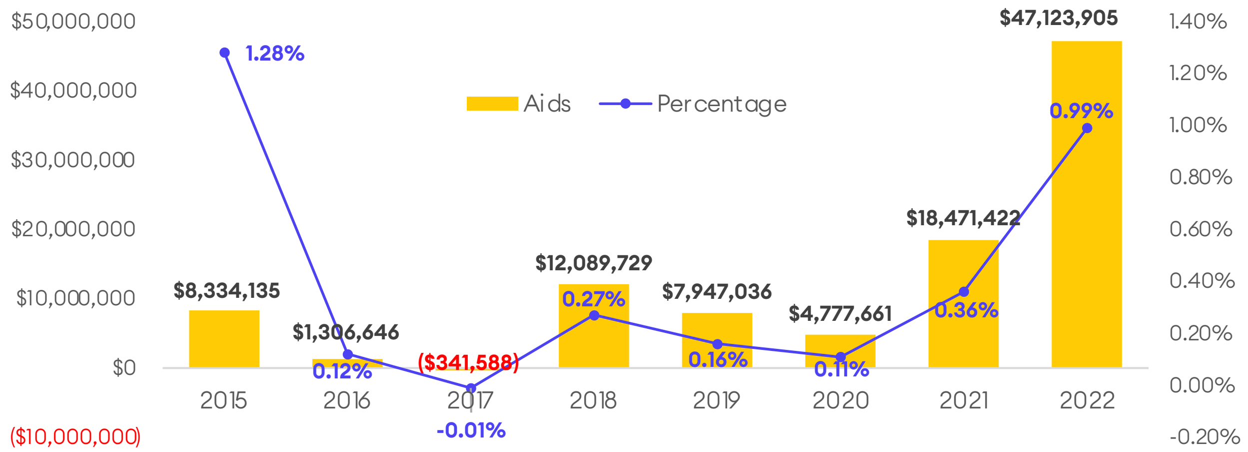
Since the outbreak of the conflict in Yemen, international aid has focused almost exclusively on humanitarian relief to respond to the rapidly deteriorating humanitarian crisis in the country. Using data reported on the International Aid Transparency Initiative's (IATI) d-portal,[35] Figure 6 shows that at its highest (in 2022), foreign aid allocated to PSD categories reached 0.99% of total foreign aid to Yemen.[36]

The aid funding allocated to PSD sectors in Yemen is distributed across macro activities (e.g. targeting business environment improvements, monetary stability, and the banking sector), meso (targeting value chains of certain sectors and intermediary organisations providing services to businesses) and micro/interventionist activities (e.g. providing direct support to entrepreneurs including through financing, employment, and training programmes). Annex 1 provides a mapping of all donor programmes that could be considered as contributing to PSD in Yemen since the outbreak of the conflict based on the primary and secondary research conducted for this study.

It is worth noting that the majority of aid funding that ends up supporting PSD in Yemen is not usually provided specifically for PSD. For example, the large foreign currency deposits provided by Saudi Arabia to the CBY to cover the imports of basic commodities achieved its primary objective of stabilising food prices and ensuring continued availability of food in the market (a humanitarian objective), but it also played a critical role in PSD as the food importers benefited from it in sustaining their operations. Similarly, many of the micro/interventionist programmes have a livelihoods objective (providing income-generating opportunities) although they end up providing PSD support especially to micro enterprises.

The mapping of donor-funded programmes reveals an overemphasis on supporting microenterprises. The only programme that has some activities providing support to medium and possibly large enterprises is USAID's Economic Recovery and Livelihoods Program (ERLP),[37] and the only direct in vestment by DFIs[38] with large private sector firms in Yemen is the IFC/FMO line of credit extended to the HSA Group, which is IFC's first investment of this kind in Yemen in the last decade (see Annex 1).[39]

Figure 6 Percentage aid funding to PSD



35 The International Aid Transparency Initiative (IATI) brings together over 90 governments, multilateral institutions, private sector, and civil society organisations and others to increase the transparency and openness of resources flowing into developing countries. 1500 organisations publish their data on IATI, and some donors such as the UK, Netherlands, and Belgium have mandatory rules for organisations receiving their aid to report their spending to IATI.

36 Authors calculations using data on d-portal. The aid sectors used to calculate the PSD funding are: Banking & Financial Services, Business & Other Services, Fishing, Industry, Trade Policies & Regulations. It is worth noting that d-portal does not contain aid data from regional donors (GCC countries) to Yemen.

37 USAID, "USAID Yemen Economic Growth, Recovery, Livelihoods and Agriculture Fact Sheet." USAID. https://www.usaid.gov/yemen/fact-sheets/economic-growth-recovery-livelihoods-and-agriculture

38 OECD defines national and international development finance institutions (DFIs) as 'specialised development banks or subsidiaries set up to support private sector development in developing countries. They are usually majority-owned by national governments and source their capital from national or international development funds or benefit from government guarantees. This ensures their creditworthiness, which enables them to raise large amounts of money on international capital markets and provide financing on very competitive terms'. https://www.oecd.org/development/development-finance-institutions-private-sector-development.htm

39 IFC, "IFC Partners with HSA Group to Bolster Food Security in Yemen," IFC, August 10, 2021. https://pressroom.ifc.org/all/pages/PressDetail.aspx?ID=26564

5. Private Sector Engagement (PSE) in Yemen

PSE policies and approaches recognise that firms are critical stakeholders in planning and designing sustainable interventions and are also well-placed to execute on a wide array of projects, particularly those that have humanitarian and developmental consequences. Therefore, PSE is defined as an approach to planning and programming through which governments and/or international development agencies consult, strategise, align, collaborate, and implement with the private sector for greater scale, sustainability, and effectiveness of development or humanitarian outcomes.[40]

In Yemen, public and private sector engagement has traditionally been a contentious issue. Interviews conducted for this study revealed a high level of mistrust between the private sector and government authorities. Many interviewees indicated that effective engagement by the government and by donors with the private sector has been limited in the development and economic policy-making space in Yemen. The following sections will assess government-led and donor-led approaches to PSE in Yemen, guided by the analytical framework detailed in Annex 1.

5.1 Public sector-led efforts in the field of PSE in Yemen

Following the protests of 2011 and the change in government that followed, partnership with the private sector was one of the priority areas identified by the government and its international partners. The Mutual Accountability Framework (MAF) agreed between the Government of Yemen and its international partners in September 2012[41] included a commitment by the government to develop a public-private partnership (PPP) legislation.[42] While progress was made in drafting the PPP law and submitting it to parliament, the escalation of the conflict towards the end of 2014 prevented further progress on this front. Another key activity during the transitional period post-2011 was signing a Memorandum of Understanding (MoU) in November 2014 between the government and the private sector with the main purpose of "support[ing] both the Government of Yemen and the Yemeni private sector to identify a clear path for PSE in economic growth and sustainable development".[43] The MoU outlined a formal dialogue mechanism between government and private sector, the creation of a Joint Committee on SMEs, and PSE in value chain development. It also called for reforms to reduce corruption, protect private property, and provide the requirements of a suitable investment environment for the

40 USAID, "Private-Sector Engagement Policy," USAID.
https://www.usaid.gov/sites/default/files/2022-05/usaid_psepolicy_final.pdf

41 World Bank, "Donors Support Yemen's Transition with US$6.4 Billion," World Bank Press Release, September 4, 2012.
https://www.worldbank.org/en/news/press-release/2012/09/04/donors-support-yemens-transition-six-point-four-billion-dollars

42 The Executive Bureau, "Q2 Status Report. Mutual Accountability Framework (Pledges and Reforms)," The Executive Bureau, Yemen, June 22, 2014.
https://overseas.mofa.go.kr/ye-ko/brd/m_11248/down.do?brd_id=9432&seq=1082626&data_tp=A&file_seq=2

43 Government of Yemen, "Memorandum of Understanding Between Government of the Republic of Yemen and Yemeni Private Sector," The Ministry of Planning and International Cooperation Yemen. November 18, 2014.
http://www.pdf-yemen.com/PDF/CIPE_Laws/Memorandum%20of%20Understanding%20FINAL%20English%2018%20Nov%202014.pdf

private sector that would be attractive for local and foreign investment.[44] Again, the escalation of the conflict shortly after this MoU was signed prevented any further progress in implementing it.

The National Dialogue Conference (NDC) which was held between March 2013 and January 2014 in Yemen also concluded with a number of recommendations related to PSE. For example, one of the recommendations was the 'Issuance of laws and legislations that promote and encourage the contributions of the private sector to comprehensive development'. Another recommendation was 'Issuing a decision to establish a social economic board as an institutional framework for the partnership between the private sector, the government, and the civil society organisations throughout the country and the governorates'.[45] Efforts to implement these and other NDC recommendations were stopped by the eruption of the conflict.

Since the conflict started, a number of ad-hoc meetings have been held between government authorities (in Aden and Sana'a) and the private sector to discuss and consult on different topics, from banking and electricity to customs and taxes. However, due to the lack of a structured and consistent process of engagement, both before and since the conflict started, a common message that surfaced in the interviews was the overwhelming sentiment by private sector representatives that there continues to be an absence of real 'desire' within the public sector to engage with the private sector as a credible partner in the development process in Yemen.

A number of recent negative experiences have contributed to this sentiment. For example, in July 2021, the government in Aden raised the exchange rate used for customs valuation by 100% (from 250 YER to 500 YER). The decision was taken without consulting the private sector, which led to the Chamber of Commerce in Aden rejecting the decision and protesting against it.[46] Although the government eventually enforced the decision, it led to an additional crack in the already deteriorated relation between the public and private sector. In a continuation of this trend, the government in Aden implemented a second increase in the exchange rate for customs valuation in January 2023 from 500 YER to 750 YER. This was done again without consulting the private sector, causing additional breakdown in the relationship between the public and private sector.

In another instance, this time in Sana'a, the authorities announced in September 2022 a new law banning Riba (usury) and submitted the law to parliament for ratification.[47] This caused significant concerns for the private sector including the banking sector, investors, and even Islamic banks and microfinance institutions as the law also banned "Murabaha," which is the key sharia-compliant product offered by Islamic banks and microfinance institutions in Yemen. The law was announced by the Cabinet in Sana'a and submitted to parliament without adequate consultation with the private sector. Multiple meetings and events have taken place since then to try and dissuade the authorities from proceeding with this law.[48],[49] However, the parliament in Sana'a approved the law in March 2023.

One encouraging step in institutionalising the engagement of the private sector has been the establishment of the National Committee for Trade Facilitation by the Council of Ministers in Aden in May 2022. The committee is chaired by the Minister of Industry and Trade and includes in its membership deputy ministers and heads of relevant public authorities, as well as representatives from the federation of chambers of commerce, the federation of customs clearance brokers, and shipping and insurance companies. The committee is tasked with developing a national strategy for trade facilitation in addition to supervising the implementation of policy reforms related to trade, contributing to the improvement of the business environment, and advising on legislations and regulations related to policies adopted at air, land, and sea ports. However, progress has been slow in activating this committee and it only convened its first meeting on 22nd December 2022, seven months after it was established. Without effective implementation and progress with this committee, the anticipated positive impact on PSE could be limited. Another encouraging step in private sector engagement in Sana'a has been

44 Mathew Godwin, "An Historic Agreement: Public-Private Partnership to Safeguard Yemen's Future," Center for International Private Enterprise, December 11, 2014.
https://www.cipe.org/blog/2014/12/11/an-historic-agreement-public-private-partnership-to-safeguard-yemens-future/

45 "National Dialogue Conference Outcomes Document." Comprehensive National Dialogue Conference. 2014. https://www.peaceagreements.org/masterdocument/1400

46 "The Chamber of Commerce in Aden rejects Yemeni government's decision to raise the price of the customs dollar." CNBC Arabia, September 9, 2022.
https://www.cnbcarabia.com/86489/2022/09/14/غرفة-التجارة-في-عدن-ترفض-قرار-الحكومة-اليمنية-رفع-سعر-الدولار-الجمركي

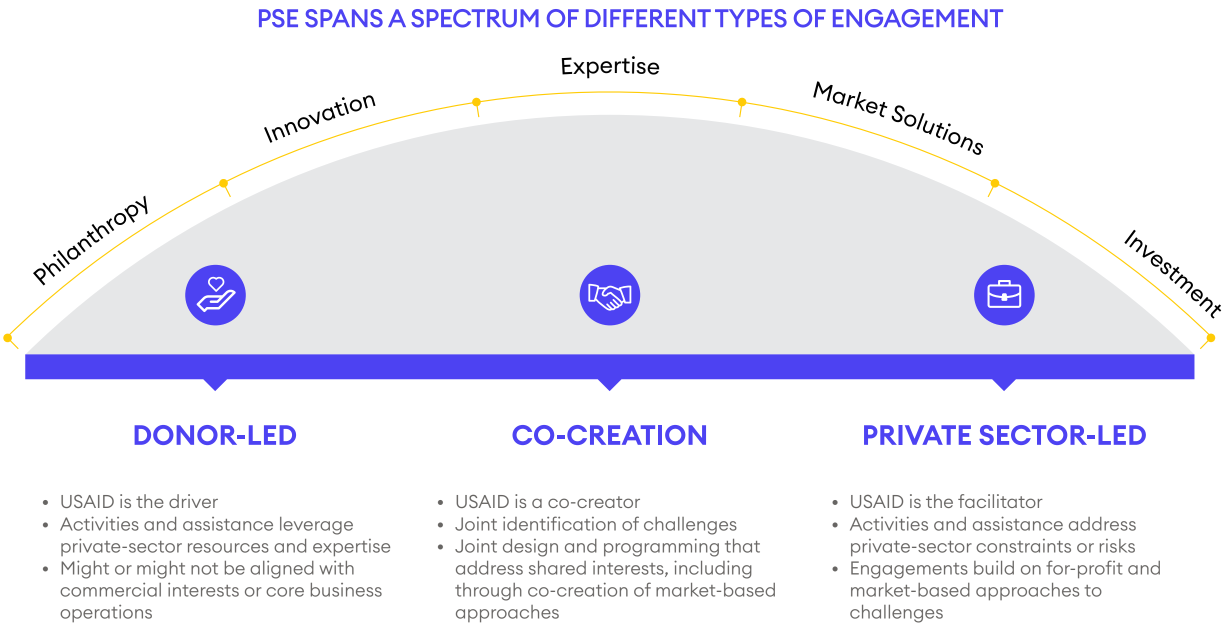
47 Yemen Press Agency, "The Council of Ministers Approves a Draft Law to Prevent Usurious Transactions," Yemen Press Agency, September 5, 2022. http://www.ypagency.net/474114

48 Yemeni Banks Association, "Recommendations of the Panel Session on the Draft Law to Prevent Usurious Transactions," Yemeni Banks Association, December 6, 2022. https://yemen-yba.com/13361/

49 Fouad Al-Fattah, "The Private Sector is Discussing a Draft Law to Prevent Usurious Transactions and Stresses the Importance of Including Articles to Improve the Business Environment," Projects Magazine, September 25, 2022. https://magzenprojects.com/news.php?id=673

the Investment Forum which convened four times between September 2022 and March 2023. In each forum, senior representatives from private and public sector met to discuss challenges and explore opportunities in critical sectors such as public private partnerships, electricity sector, transport sector, and agriculture sector. While this forum has provided a much-needed space for important dialogue between the public and private sector and ensured the engagement of senior decision-makers, it is not yet clear whether any concrete steps have been implemented based on the forum's discussions.[50]

Figure 7 Spectrum of PSE



Source: USAID Private-Sector Engagement Policy[51]

5.2 Donor support to PSE in Yemen

Donor engagement with the private sector can span a wide spectrum, as shown in USAID's definition presented in Figure 7. In Yemen, the majority of donor engagement with the private sector is primarily under the 'donor-led' category of the spectrum, with donor activities and assistance focused on leveraging private sector resources and expertise primarily through a contracting process.

There are only three known examples in Yemen of private sector-led engagements, where donors are the facilitator and activities and assistance address private sector constraints or risks. The longest-running initiative aimed at engaging and strengthening private sector voices in Yemen's priorities is the Economic Reforms Team (ERT) supported by the Center for International Private Enterprise (CIPE).[52] The ERT has brought together influential business leaders since 2012 with the mission 'to work with members of the greater business community, economic experts, and civil society organisations to present visions and economic solutions as partners, supporters, and advocates augmenting and informing government efforts to improve the economic policies in Yemen'.[53] Since its establishment and until now, the ERT has issued multiple position papers and policy briefs, engaged with government and donors, and advocated for different policy initiatives. Members of the ERT feel that the presence of clear and effective PSE processes could have made their efforts much more impactful.

The second example is the Private Sector Cluster (PSC). With support from the World Bank (and later from the UK's FCDO), the PSC was established and launched in January 2019 with the aim of aligning and coordinating the efforts of the Yemeni private sector in the ongoing humanitarian, development, recovery and reconstruction efforts and giving it a voice in economic decision

50 Investment Forum, https://www.facebook.com/invest4um

51 Ibid.

52 CIPE, "Yemen: Private Sector Solutions During Conflict." CIPE. https://www.cipe.org/projects/yemen/

53 Yemeni Economic Forum, "About Economic Reforms Team (ERT)," Yemeni Economic Forum. http://www.yemenief.org/en/en-Page.aspx?page_id=3

making.[54] The cluster is composed of representatives of the major private sector entities including the chambers of commerce from all regions of the country and key business management associations. The objectives setup by the PSC provides a good indication of private sector views towards what PSE should entail in Yemen (see Box 2).

Box 2 Objectives of the Yemen private sector cluster

Engaging the private sector in economic policymaking

- Involving the private sector cluster in key roles of developing the economic file and ensuring its participation in the negotiations around it.
- Coordinating with the cluster to neutralize economic enterprises from the effects and repercussions of the ongoing conflict.
- Coordinating with the private sector to be represented on the boards of key official economic and productive institutions which are relevant to the private sector.

Enhancing the role of the private sector in humanitarian and development efforts

- Involving the private sector cluster in the decision making process on aid interventions such as designing humanitarian programs and projects submitted by donors and official bodies before their adoption and implementation.
- Aid programs should contribute to the promotion and revitalisation of the economy and markets and should not cause harm to the private sector. This can be done through promoting local procurement of aid items and service delivery to revitalise the economy.

Engaging the private sector in recovery and reconstruction programs and efforts

- The private sector requests to be a key and influential partner in drawing up strategies, policies, and programs for the recovery and reconstruction phases and establishing investment and development funds that will contribute to reconstruction and recovery. These funds will be managed by an independent body with a representation from the private sector.

Unfortunately, it seems that the PSC has been facing significant challenges in establishing and sustaining an effective role as a representative of the voices of private sector in Yemen. According to interviews conducted for this study, the inclusivity aimed for by the PSC became a disadvantage, making it difficult to progress and achieve consensus of all its members under the increasingly polarised political context and the interventions by the conflict parties. However, the lessons learned from this experience can be useful for any future processes or mechanisms for engagement with the private sector in Yemen.

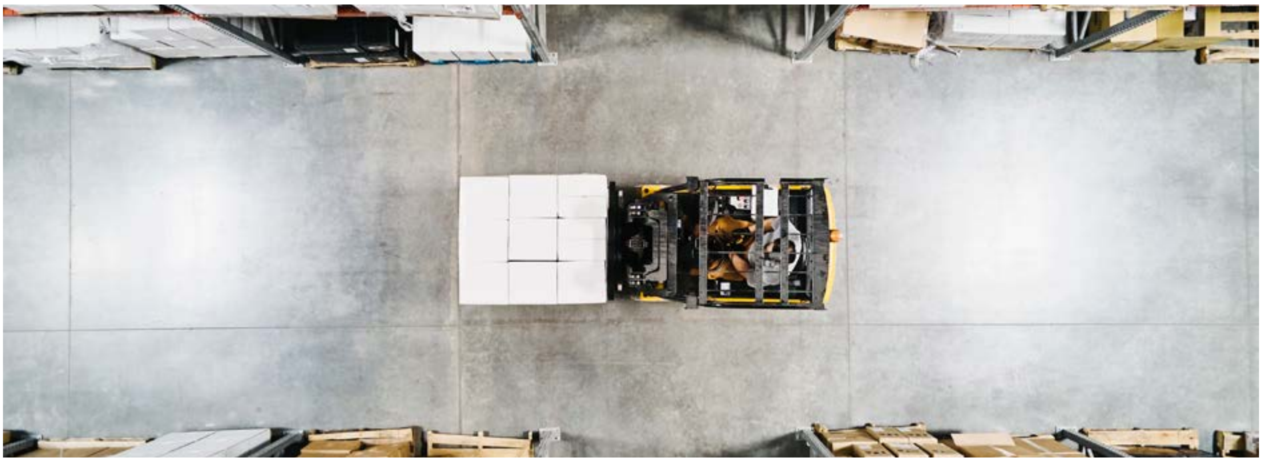
The third example is the case of the FSO Safer oil tanker crisis.[55] When negotiations between the Office of the Special Envoy of the Secretary General and the authorities in Sanaa failed to enable the inspection of the decaying FSO Safer tanker and transfer of the oil it contained, the Fahem Group, a Yemeni firm, proposed a solution. Their proposal ultimately unlocked an agreement that was signed by the UN, the Fahem Group, and the authorities in Sanaa.[56] Later, HSA Group became the first private sector entity to contribute US$1.2 million to support the UN's emergency appeal to implement the agreement.[57] This contribution presents a unique model in engaging the private sector in peacebuilding efforts that can possibly be scaled up and replicated in Yemen or in other contexts.

54 YPSC webpage, "Yemen Private Sector Cluster." Yemen Private Sector Cluster. https://yemen-psc.org

55 Ed Caesar, "The Ship That Became a Bomb," The New Yorker, October 4, 2021. https://www.newyorker.com/magazine/2021/10/11/the-ship-that-became-a-bomb

56 "Memorandum of Understanding," Abdulla Mohamed Fahem & Co, The Supervisory Committee for the Implementation of the Urgent Maintenance Agreement and the Comprehensive Evaluation of the Safer Floating Tank, United Nations, March 5, 2022. https://yemen.un.org/sites/default/files/2022-06/MOU-%20FSO%20Safer-March%205.pdf

57 "HSA Group Pledges US$1.2 Million to Support the UN's Emergency FSO SAFER Appeal – Yemen," UN Resident and Humanitarian Coordinator in Yemen, August 25, 2022. https://reliefweb.int/report/yemen/hsa-group-pledges-us12-million-support-uns-emergency-fso-safer-appeal



6. Key Recommendations

A paradigm shift is needed to unleash the potential of the Yemeni private sector as a driver of economic growth and recovery and therefore as a key stakeholder in peace and stabilisation efforts in Yemen. Government authorities as well as international development actors need to consider the private sector in Yemen as a crucial partner in addressing the humanitarian and development challenges facing the country, rather than viewing it as either a beneficiary or a provider of goods and services (by international development actors) or as a revenue source (by government authorities). While there are credible arguments for maintaining the focus on relief interventions given the dire humanitarian situation, there is a growing realisation by international development agencies, government authorities, private sector, and Yemeni citizens of the need to transition to more sustainable economic development interventions. The following section provides practical recommendations to various stakeholders to effectively support and engage with the private sector, taking into account the current local context.

6.1 Recommendations to government authorities

Avoid escalatory and polarising economic measures that affect the macro economy and impact the commercial sector and Yemeni citizens across the country. In addition, avoid politicising private sector activity and shield the private sector from being engaged in the political conflict.

Establish a clear process for PPD, led by the highest level of leadership from the public sector to signal commitment towards engaging the private sector. PPD can help create a more predictable regulatory environment, increase transparency and trust among stakeholders and identify key reforms and interventions that can improve the business environment and attract investment. In a World Bank survey of PPD practitioners, 63% of respondents believed that PPD contributed to peacebuilding.[58]

To be successful, the PPD process should be action-oriented, ensure continuity (not a one-time event), be based on a jointly developed dialogue agenda that is updated regularly, and follow a clear mechanism to monitor and report on agreed actions. It should also ensure inclusivity of the issues facing different types of private firms by size (from micro to large) and by sector. The national-level PPD process should be mirrored by governorate-level PPD processes that can address the realities of diverse local contexts in each governorate.

Develop a clear strategy towards economic stabilization, recovery and development that could help engage and guide private sector investments. Such strategy should focus on immediate and short-term practical quick wins, as it is difficult to develop long-term plans under the extremely unpredictable conflict context. It is critical to incentivise private sector investments to curb the outflow of local capital, especially in the face of ever-increasing regional competitiveness, contrasting with the complicated and challenging local reality.

Focus on what is actionable within existing legal and institutional frameworks. Some public authorities tend to be discouraged from pursuing private sector initiatives, such as PPP, due to the lack of specific laws that govern them. While there is unlikely to

58 "Public-Private Dialogue in Fragile and Conflict-Affected Situations," World Bank, 2014. https://documents1.worldbank.org/curated/en/108301474484504825/pdf/911830WP0Box380TC0PPD0in0FCS0Report.pdf

be sufficient governmental capacity to issue, implement and enforce new laws in the current national context, there is plenty of room for growth within the current legal frameworks (such as the existing investment law and Special Industrial Zones decree), and in some cases public authorities can resort to regulation by contract.[59]

Identify key infrastructure projects for private sector investment. While private investments in infrastructure projects are risky under the current conflict situation, there are certain sectors and certain regions in the country that are likely to attract investments, especially from the Yemeni diaspora investors or investors from neighbouring Gulf region. One example is utility-scale and mini-grid renewable energy projects which are already attracting some investment interest.[60] Another example is the Build-Operate-Transfer (BOT) agreement signed with a UAE-based investor to develop a minerals-export port.[61] The General Investment Authority in Sana'a also presented a number of infrastructure projects in the transport sector for investments under a PPP model at the Investment Forum in January 2023.[62] Once a list of potential infrastructure projects is identified, government authorities should establish a special taskforce to remove any bureaucratic obstacles and accelerate these projects to completion.

Assess the feasibility of re-launching some of the industrial zones. Previously planned before the outbreak of the conflict or establishing new ones. Yemen has worked on the concept of establishing industrial zones since the mid 1990s. In 2005, Republican decree no. 79 was issued to regulate the establishment, management, and supervision of industrial zones.[63] By 2014, 13 industrial zones had been announced,[64] with feasibility studies, detailed designs, environmental studies, and investment promotion materials completed for three of them in Aden, Hodeidah, and Hadhramout.[65] In Hodeidah, a private developer was awarded a Build-Operate-Own (BOO) contract to develop the industrial zone in 2011,[66] and the industrial zone land was transferred to the company in 2014 before the conflict erupted. [67] While such investments might entail high risk, certain regions of the country are stable enough to attract the attention of specific investors with ties to those regions. Given the ongoing conflict, clear measures should be taken to ensure the integrity and transparency of the investment award process to avoid such industrial zones falling captive to vested interests.[68] Special Economic Zones and Industrial Parks have played a positive role in post-conflict recovery and economic growth in countries such as South Korea and Taiwan.[69]

6.2 Recommendations to the Yemeni private sector

Organise effectively to make demands of the government and international community. The private sector must strengthen its efforts to present a coherent front that can provide information and articulate the case for reasonable public policies and regulations. While there needs to be adequate space for diverse views, without an active and meaningful private sector voice - especially on issues that affect all private sector actors - it will be difficult for other stakeholders to pursue coherent and efficient policies that will help to rebuild Yemen's economy. Efforts by the Federation of the Yemen Chambers of Commerce and Industry and the individual Chambers, the ERT, and the PSC are a good start in this direction and should be strengthened.

Prioritise and scale up efforts to influence international aid policy towards Yemen. This goes beyond direct engagement with the diplomatic community and international aid agencies in Yemen. Business organisations such as the chambers of commerce as well as individual firms should aim to become more active by participating in relevant events (such as the World Bank/IMF

59 PPPLRC, "Regulation by Contract," PPPLRC webpage, World Bank. https://ppp.worldbank.org/public-private-partnership/regulation-contract

60 MoEE, "Tenders for supply, installation, testing, commissioning, operating & maintenance solar power plant under Build-Own-Operate-Transfer (BOOT) model," Ministry of Electricity and Energy, 2020. https://moee-ye.com/site-ar/897/

61 Mohammed Hatem, "Yemen Plans $130 Million Port, Road in Mahra to Move Millions," Bloomberg, Jan 3, 2023. https://www.bloomberg.com/news/articles/2023-01-02/yemen-plans-130-million-port-road-in-mahra-to-move-minerals

62 General Investment Authority, "The Transport Sector as a Model: Special Report", General Investment Authority Facebook, Jan 24 2023. https://www.facebook.com/permalink.php?story_fbid=pfbid023pGapWwWXmZriFVSZqBWd2QwLAJMukuK4idpPXo3b9KcnZ8jQySVBaL8G-2TEauS4l&id=100064892942444

63 "Dalil Tarweej: al-Mantiqa al-Sina'iyah – Hadhramaut." Translation: Promotion guide, Hadramout Industrial Zone. Ministry of Industry and Trade, 2005. https://www.moit.gov.ye/moit/sites/default/files/دليل%20حضرموت%20للعرض.pdf

64 Al Thawrah, "The Ministry Of Industry Prepared Summaries For 13 Industrial Zones In Yemen, Covering All Regions", Al Thawrah News, May 22, 2014. https://althawrah.ye/archives/83517

65 Jamal Mujahid, "Yemen plans to establish nine industrial zones", Almotamar Net, January 13, 2011. https://www.almotamar.net/pda/87777.htm

66 TYE, "Inauguration of Tihama Company for the development and operation of the industrial zone in Hodeidah", The Yemeni Economist, February 10, 2011. https://www.yemeneconomist.com/10181/2011-02-10-18-47-22

67 Al Thawrah, "Signing An Agreement To Hand Over The Land Of The Nucleus In The Industrial Zone In Hodeidah To The Tihama Company", Al Thawrah News, January 19, 2014. https://althawrah.ye/archives/69301

68 AfDB, "Special Economic Zones in Fragile Situations: A Useful Policy Tool?" African Development Bank, Transition Support Department. January, 2015. https://www.afdb.org/fileadmin/uploads/afdb/Documents/Generic-Documents/SEZ_anglais_SEZ_anglais.pdf

69 Aradhna Aggarwal, "Social and economic impact of SEZs in India," Oxford Univ Press, 2012.

Annual and Spring Meetings and World Economic Forum), and develop a leadership-level strategy for engaging with and influencing key donor countries at headquarter level.

Make tangible improvements in corporate governance and compliance policies and practices in order to attract international partners and increase investment (either from development finance institutions or private sources). This is especially important in the event that public sector institutions remain fragile and fragmented, in which case private sector firms will need to take on the burden of regulation by implementing higher standards that meet international requirements and possibly exceed equivalent local laws and regulations. This could help in addressing and mitigating parts of the risk associated with operating in Yemen's business environment.

Continue and better organise the private sector's leading role in humanitarian relief and development efforts. These efforts have not only mitigated and alleviated tremendous suffering in Yemen but have also highlighted the role that the private sector plays in the life of Yemeni citizens. Private sector actors should organise regular meetings and forums to strategise and better frame their contributions at the humanitarian-development-peace nexus, learn lessons from the different activities in this field, and explore opportunities for collaboration and synergies among themselves and with other stakeholders such as civil society organisations and international humanitarian and development actors.

6.3 Recommendations to regional and international donors

Prioritise and scale up PSD interventions. Academic evidence shows that PSD interventions can and should be implemented at the very beginning of a recovery process.[70] While some donors in Yemen have started including interventions that address private sector needs in the country, the majority of these interventions are at small scale and typically take a livelihoods approach rather than a PSD approach. Regional and international donors should establish a clear baseline for their current aid financing allocated to PSD programming, and aim to scale it up while providing clear monitoring and reporting. This is especially relevant for regional donors who are the largest aid partners for Yemen and who are increasingly shifting towards market-based approaches in their foreign aid strategies.

Engage actively with the private sector. The international community should establish a clear process for active engagement with the Yemeni private sector across different thematic topics. This engagement should not wait for the emergence of a 'unified' representative body of the private sector as it is not justifiable, and likely not feasible, to expect such a body to emerge under

70 USAID, "Guide to Economic Growth in Post-Conflict Countries," Office of Economic Growth, USAID, 2009. https://www.calpnetwork.org/wp-content/uploads/2020/01/a-guide-to-economic-growth-in-post-conflict-countries.pdf

the current context. Instead, engagement processes should be designed flexibly to be open for firms and business organisations of different sizes and from different sectors to self-select and participate in engagement activities. Regional and international donors should adopt a private sector lens when designing their interventions, to ensure that it facilitates rather than hinders market system dynamics and paves the way for future investment by private sector. In addition, donor agencies should shift towards co-creation of programs and interventions jointly with the private sector, and eventually for private sector-led design of programming, instead of the current heavily donor-led programming approach.

Engage actively with large firms to support market linkages and augment its impact. To date, the international development actors have mainly emphasised catalysing MSMEs, especially microenterprises, in their interventions in Yemen. This is important but needs to be balanced with addressing the needs of large firms as well. As shown in this study, large firms have capabilities and competencies that smaller firms may lack, and that are critical for generating jobs and kickstarting economic recovery and growth in the country. Further, by promoting 'linkage' strategies, the international community can also make use of large firms as an instrument for MSME creation and strengthening.

Leverage the array of institutions and instruments available to support the private sector. While there has been an increasing realisation of the critical role of DFIs in FCAS,[71] there has only been a single DFI investment in Yemen over the past decade (see project no. 18 by IFC and FMO in Annex 1). DFIs and their shareholding governments should actively explore investment opportunities in private sector projects in Yemen, especially building on the success of the IFC/FMO investment. A first step could be convening a meeting for DFIs to learn more about the situation in Yemen and explore available opportunities. In addition, donors should promote and mobilise different financing instruments beyond grants, such as trade finance, venture capital, guarantees, development impact bonds, challenge funds, syndicated loans, and lines of credit.

Work at both national and local levels. The levels and types of conflict and operational challenges vary across Yemen, creating opportunities and entry points for subnational interventions. Donor-funded programmes should be designed flexibly to allow for pursuing opportunities to support reforms and/or implement PSD programming at regional, governorate, or district levels. The EU-funded Strengthening Institutional and Economic Resilience in Yemen (SIERY) programme and the US-funded ERLP programme (see projects no. 8 and 11 in Annex 1) provide good examples of flexible designs that can be replicated and scaled-up.

Improve understanding of the Yemeni economy. Yemen presents a challenging environment in which to operate, with a constantly changing context due to the ongoing conflict. The lack of in-country presence by donor agencies (due to the security situation) negatively impacts their ability to design responsive programmes. Therefore, international donors should consider deploying and scaling up a number of tools and methodologies to improve their understanding of the Yemeni economy and guide their economic recovery and development interventions including PSD and PSE. These tools and methodologies include:

- **Political economy analysis** to understand the level of political commitment to various reforms and interventions at each level of government, protect against the risk of donor programmes falling captive to vested interests, identify institutional champions in the public and private sectors that can drive and manage economic recovery processes, understand drivers, incentives, legal traditions, policy history and cultural factors that are likely to influence any planned interventions, and identify potential winners and losers from any required reforms.

- **Large-scale digital data**, such as nightlights and cell phone metadata, which are increasingly being used by scholars as proxy measures of economic activity. Recent advances have shown how phone data can be used to reconstruct accurate, fine-grained estimates of poverty and wealth. For example, cell phone data have been used to explore private sector activity in Afghanistan, interacting these data with the available violence data from that country to assess how violent activity influences firm behaviour.[72] Donors should support such tools in combination with better economic data collection at national and subnational level to improve understanding of evolving economic activity in Yemen.

- **The Growth diagnostic framework**, which appears to be best suited to conflict-affected environments, can provide a more detailed analysis of the cause-and-effect relationships behind the constraints to growth, and can be easily combined with a political economy approach. It can both inform what types of programming are likely to be most effective and identify issues for the design process.[73]

71 DFI Fragility Forum webpage. https://www.dfifragilityforum.org

72 Joshua Blumenstock et al, "Insecurity and Industrial Organization: Evidence from Afghanistan." Policy Research Working Paper No. 8301, World Bank, January 2018. https://openknowledge.worldbank.org/handle/10986/29211.

73 Lisa Curtis et al, "Private sector development in conflict-affected environments: Key resources for practitioners," The Donor Committee for Enterprise Development, October 2010.

PART 2:

ANALYTICAL FRAMEWORK

- **Value chain analysis** which is currently the most widely used tool in donor-funded economic interventions in Yemen. It is helpful in guiding the prioritisation of particular sectors for intervention.

- **Making Markets Work for the Poor (M4P)** is a broader approach than value chains as it focuses more broadly on markets. By addressing market systems, scale, and sustainability, the M4P approach finds ways to increase the incomes of poor people while promoting the accessibility of other products and services they require.[74] If grounded in comprehensive political economy and conflict analysis, M4P is particularly well suited to post-conflict environments because it involves a market diagnostic process to account for market dynamics and stakeholders, it is sufficiently flexible to deal with the dynamic and volatile nature of post-conflict environments, and it incorporates risk management in order to avoid exacerbating conflict.[75]

In order to assess the current context of the private sector in Yemen and evaluate government and donor-led interventions in supporting it, an analytical framework was designed to distil knowledge from academic and policy literature on the private sector in fragile and conflict-affected situations (FCAS), in order to apply the framework findings to the case of Yemen.

The analytical framework first looks at industrial organisation and the determinants of firm survival to understand the structure of firms in FCAS. It explores the debate on the importance of micro and small informal enterprises versus large firms and the 'missing middle' in economic development in FCAS.

The second part of the analytical framework assesses the constraints facing the private sector in FCAS and presents a set of indicators to understand the impact of conflict at enterprise level.

The third and fourth parts of the analytical framework evaluate donor-led approaches to PSD and PSE in FCAS.

It is important to emphasise that the policy (and, for that matter, the academic) literatures on the private sector in FCAS is still considered nascent and continues to evolve. While the existing body of scholarship and policy analysis attempts to offer generalisations based on a handful of case studies, any conclusions drawn from such literature should be studied carefully and compared to the context being considered before being applied or used to guide interventions in that context.

1. Industrial organisation in FCAS

A large strand of literature focuses on industrial organisation and the determinants of firm survival in developing countries more generally, and the findings from this work have only recently started to be applied to FCAS.[76] Research on 'the survival of formal firms has important implications for development strategies. In order for the private sector to act as an 'engine of growth' and advance the development process, it is necessary for firms to survive and grow'.[77] As just noted, while generally

74 Tracey Gustle and Laura Meissner, "Practice Note 1: Market development in conflict-affected contexts," International Alert. https://www.international-alert.org/wp-content/uploads/2021/09/Economy-Peacebuilding-Essentials-Practice-Note-1-EN-2010.pdf

75 Katie McIntosh and Joanna Buckley, "Economic development in fragile and conflict-affected states: Topic guide," GSDRC, 2015. https://assets.publishing.service.gov.uk/media/57a0899040f0b6497400014a/Econdevfragilestates1.pdf

76 See, for example: Joshua Blumenstock et al, "Insecurity and Industrial Organization: Evidence from Afghanistan," Policy Research Working Paper, No. 8301, World Bank, January 2018. https://openknowledge.worldbank.org/handle/10986/29211

77 Leora Klapper and Christine Richmond, "Patterns of Business Creation, Survival and Growth: Evidence from Africa," Labour Economics 18, Supplement 1, 2011: 533.

not written specifically in the context of conflict settings, the theories and findings of research in industrial organisation can help generate hypotheses regarding the structure of firms in such environments.[78] As Cefis and Marsili put it, 'The growth and survival of firms will depend on their ability to successfully adapt their strategies to changing environments' and this is no less true in places that become violent.[79]

The determinants of the industrial organisation and size distribution of firms is of potential importance to the competitiveness and even growth of a nation's economy. One of the main claims that scholars have made in this regard is with respect to the so-called 'missing middle' in firm size across the developing world.[80] To put this in the traditional terminology of development economics, there is a 'dual economy' with relatively high-performing large firms on the one hand and many small firms on the other. Scholars have made various arguments as to why this missing middle occurs.[81] First, it could arise because of the costs of regulation and taxation: large firms can bear these costs (or either evade them or become exempt from them owing to special treatment) while small firms simply choose to remain small (and informal) in order to avoid the cost burden. Second, SMEs may lack access to capital that large firms already have, and small informal firms do not seek. Third, the distribution of firm size may reflect the available human capital: large firms (including multinational enterprises) can outbid SMEs for the services of the (few) high-skilled workers. Fourth, trade regimes may disproportionately protect the few large firms in the country. Finally, large firms may be better able to engage in the risk management techniques needed to survive in volatile economies.

Development agencies have generally accepted the existence of a missing middle and have devoted much of their programming to overcome it. As Beck, Demirguc-Kunt and Levine[82] point out in the developing world context, bilateral and multilateral aid agencies have sought to promote the MSME sector through various programmes and subsidies for three inter-related reasons: first, MSMEs contribute to competition and innovation; second, MSMEs are often more productive than large (particularly state-owned) firms; third, MSMEs generate employment.[83] For these reasons, MSMEs can also contribute to growth and poverty reduction.[84] While Beck, Demirguc-Kunt and Levine find a strong correlation between economic growth and the size of the MSME sector in cross-country regressions, they do not find causal evidence in support of a poverty-reducing role. However, they do note that in specific country cases MSMEs may have that effect.

While not directly related to the issue of firm size (though this would make for a nice extension of their research), Hallward-Dreimeier and Pritchett find a substantial difference between 'fast' and 'slow' firms in developing countries in terms of the time it takes them to overcome various regulatory hurdles, like getting a construction permit.[85] They interpret these results to infer that some firms are 'favoured' over others, due to 'political connections, family ties, influence activities, or corruption'.[86] A crucial point that arises from their work is that it is not necessarily capital market failures that impede firm operations, but rather political economy considerations. We would suppose that these might be even more acute in violent settings where the issues at stake could be the very existence of the firm and the lives of its owners and employees. This is in line with Douglass North's Nobel Prize-winning work which has argued that the roots of differing growth rates around the world can be explained by the quality of a nation's institutions, and in particular its adherence to strong property rights regimes. During periods of political instability and

78 For a review see: Yue Li and Martín Rama, "Firm Dynamics, Productivity Growth, and Job Creation in Developing Countries: The Role of Micro- and Small Enterprises," World Bank Research Observer 30, No. 1, 2015.

79 Elena Cefis and Orietta Marsili, "Survivor: The Role of Innovation in Firms' Survival," Research Policy 35, Issue 5, 2006: 2.

80 See: James R. Tybout, "Manufacturing Firms in Developing Countries: How Well Do They Do, and Why?" Journal of Economic Literature 38, No. 1, 2000: pp. 11–44.

81 And Hsieh and Olken 2014 dispute its existence altogether, but based on only three country cases, namely India, Indonesia, and Mexico. See: Chang-Tai Hsieh and Benjamin A. Olken, "The Missing 'Missing Middle," Journal of Economic Perspectives 28, no. 3, 2014.

82 Thorsten Beck, Asli Demirguc-Kunt and Ross Levine, "SMEs, Growth, and Poverty: Cross-Country Evidence," Journal of Economic Growth 10, no. 3, 2005.

83 Yue Li and Martín Rama, "Firm Dynamics, Productivity Growth, and Job Creation in Developing Countries: The Role of Micro- and Small Enterprises," World Bank Research Observer 30, No. 1, 2015.

84 Again, for a skeptical view of programming that targets SMEs vs. large firms, see Chang-Tai Hsieh and Benjamin A. Olken, "The Missing 'Missing Middle," Journal of Economic Perspectives 28, no. 3, 2014.

85 Mary Hallward-Driemeier and Lant Pritchett, "How Business Is Done in the Developing World: Deals versus Rules." Journal of Economic Perspectives 29, no. 3, 2015: 121–40.

86 Ibid

violent conflict, authorities may find it especially costly to enforce property rights, especially in regions that are beyond their military control. Authorities may also actively erode a firm's property rights and profits through their own corrupt and predatory practices. In fact, the conflict itself may be, at least in part, about who gets to define and enforce the property rights regime.[87]

In short, the literature on the private sector in the developing world (and its extension to FCAS) has highlighted the 'missing middle' and explored a range of possible reasons for its existence: from capital market failures to the quality of a nation's institutions to political economy considerations. As the debate over the missing middle suggests, however, there is still a great deal that scholars have yet to learn about industrial organisation and private sector behaviour in FCAS.

In particular, one thing that is 'missing' from much academic and policy analysis is the role of large firms (generally defined as those with over 100 employees[88]) in FCAS, which seems to be one of the major gaps both in research and policymaking. But as a recent World Bank report argues, 'large firms are different than other firms in low- and middle-income countries. They are significantly more likely to innovate, export, and offer training and are more likely to adopt international standards of quality'.[89] Further, and of fundamental importance to economic growth, large firms have 'productivity advantages – that is, their ability to lower the costs of production through economies of scale and scope but also to invest in quality and reach demand. Across low- and middle-income countries with available business census data, nearly six out of ten large enterprises are also the most productive in their country and sector'.[90] Not surprisingly, greater productivity translates 'into improved outcomes not only for their owners but also for their workers and for smaller enterprises in their value chains. Workers in large firms report, on average, 22 percent higher hourly wages in household and labour surveys from 32 low- and middle-income countries – a premium that rises considerably in lower-income contexts'.[91] Large firms are also more likely to offer 'upskilling' opportunities to workers, and with formalisation they are likely to provide a better benefits package along with greater job security.

Large firms are also most likely to be 'linked' to the global economy.[92] These linkages enable large firms to import and export, effectively expanding the size of the local market. Further, these linkages tend to also spur 'best practices' in management and training, particularly if large local firms work with multinational corporations (MNCs) that demand high quality from their suppliers. These linkages, in turn, can 'trickle down' from the large, local firm to domestic MSMEs which, in turn, provide it with goods and services.

2. Constraints to the private sector in FCAS

Studies show that firms in FCAS face innumerable barriers beyond those confronting innovative business leaders in industrial economies. Given the relatively small market size of most FCAS, trade is essential for growth, but tariff and non-tariff barriers may discourage firms in FCAS from trying to sell in foreign markets. The consequence is important constraints on firm growth from the outset, making it more difficult for these firms to obtain financing from either bank or non-bank sources.

87 Douglass C. North, John Joseph Wallis, and Barry R Weingast. Violence and Social Orders: A Conceptual Framework for Interpreting Recorded Human History," Cambridge University Press 2009; Ethan B. Kapstein, "Seeds of Stability: Land Reform and U.S. Foreign Policy," Cambridge University Press, 2017.

88 Alastair McKechnie et al, "MSME-led private sector development in contexts of conflict, fragility and displacement," ODI, October 2022. https://cdn.odi.org/media/documents/ODI_MSME-led_private_sector_development_in_contexts_of_conflict_B91hmI5.pdf

89 Ciani, Andrea, Marie Caitriona Hyland, Nona Karal- ashvili, Jennifer L. Keller, Alexandros Ragoussis, and Trang Thu Tran, "Making It Big: Why Developing Countries Need More Large Firms," World Bank, 2020. https://thedocs.worldbank.org/en/doc/717891604534837739-0090022020/original/110520MakingItBigWhyDevelopingCountriesNeedMoreLargeFirms.pdf

90 Ibid

91 Ibid

92 Ethan B. Kapstein, "Exporting Capitalism: Private Enterprise and U.S. Foreign Policy," Harvard University Press, 2020.

Beyond these small markets at home, firms may need to overcome such additional and inter-related hurdles as clientelism or 'insider-outsider' problems, making it difficult for those on the 'outside' of government power to operate; capital market failures which make it challenging to access the funds needed to operate (e.g. trade credit) and grow; policy uncertainty in light of domestic economic instability (a problem that is especially acute for mono-culture, price-taking economies); institutional failures including judicial shortcomings and weak property rights; and corruption and rent-seeking, which may be especially acute in resource-rich economies.

As if these barriers were not enough to discourage would-be entrepreneurs, shortages of key inputs, like electricity, are often cited as another barrier (often the main barrier, in fact) by firms, as reported in World Bank/IFC Enterprise Surveys.[93]

Figure 8 Impact of conflict at enterprise level

While many of the above challenges also apply to firms in developing countries in general, firms in FCAS are likely facing all the above challenges at a much higher intensity, alongside additional severe institutional challenges and depleted physical, financial, and human capital stocks.[94] When conflict erupts as it often does in FCAS, firms face additional impacts. Much of the work that has been done to date in the specific literature on the private sector in conflict zones has tried to understand and isolate the impact of violence on investment decisions (after all, there could be other reasons beyond conflict that stymies investment, such as poverty, weak infrastructure, and an absence of good business opportunities; of course, all of these could be exacerbated by the presence of violence). As shown in Figure 8, the analytical framework developed for this study assesses the impact of conflict at enterprise level by looking at the levels and types of investment, the size of firms, the locations where firms operate, and the allocation of labour.

One direct impact on firms operating in FCAS might be to discourage investment, as entrepreneurs are wary of putting too much capital at risk. A study by the UN University argues that 'It is clear that violent conflict is bad for business and bad for entrepreneurship. Destroyed infrastructure, insecure property rights or falling consumer demand all increase transaction costs and the ease of doing business. It also diminishes productivity, increases the constraints underlying entrepreneurial decisions and hinders international entrepreneurship, which depends on reliable access to transport and logistical infrastructure that are often the first to be damaged in a war."[95]

In turn, violence might also be expected to affect the size of firms. Large, productive firms, for example, are likely to be both the targets of 'predation' (by government and rebel forces alike, not to mention bandits) and the most capable of devoting resources to protection.[96] Small firms, in contrast, might strive to stay 'below the radar screen' of predators; indeed, this might be one reason for widespread informality in FCAS. Given the possibility of a bimodal distribution of firms, one could hypothese that the entrepreneurs who are most likely to suffer are those who seek to build SMEs, as they are 'caught in the middle.' They have neither sufficient assets to devote a substantial share to protection nor are they so small that they can evade predation. In short, the 'missing middle' which has been so frequently observed across the developing world, might be particularly intractable in FCAS because of the predatory setting (although, for a sceptical view of the missing middle, see Hsieh and Olken 2014[97]). From a policy standpoint, this line of argument suggests that donor efforts to promote SMEs in a conflict setting may flounder in the absence of security.

93 Enterprise Surveys, "Enterprise Surveys Indicators Data - World Bank Group," World Bank, https://www.enterprisesurveys.org/en/enterprisesurveys

94 Mary Porter Pesckha, "The Role of the Private Sector in Fragile and Conflict-Affected States," World Development Report 2011 Background Paper, World Bank, 2011. https://openknowledge.worldbank.org/handle/10986/27316

95 Wim Naudé, Philip Verwimp and Tilman Brück, "Business and the Barrel of a Gun: Understanding Entrepreneurship and Violent Conflict in Developing Countries," United Nations University Press, April 17, 2013. https://collections.unu.edu/view/UNU:2945

96 Joshua Blumenstock et al, "Insecurity and Industrial Organization: Evidence from Afghanistan," Policy Research Working Paper 8301, World Bank, January 2018. https://openknowledge.worldbank.org/handle/10986/29211

97 Chang-Tai Hsieh and Benjamin A. Olken, "The Missing 'Missing Middle," Journal of Economic Perspectives 28, no. 3, 2014.

Relatedly, conflict may influence the locations where firms operate. In nearly all countries, even the most violent ones, some regions tend to be safer than others. The distribution of violence in Afghanistan and Iraq, for example, was not evenly spread out across the country, and this is the case in Yemen as well. In particular, we could hypothesise that firms are less likely to be present in violent areas (or they may have been present only to leave such areas when violence erupts) and we would expect them to employ fewer workers in such regions. Regions with less violence, in contrast, will 'benefit' to the extent of having a (relative) concentration of economic activity.

Firms may further need to reallocate labour in conflict-affected countries from production to protection. In a paper that makes use of the World Bank Enterprise Surveys, Besley and Mueller focus on the costs of protection that firms incur in insecure environments.[98] Firms in such countries face the risk of predation and as a consequence reduce investment and (mis) allocate labour to the provision of security, suffering output losses as a result. They find that 'large firms appear to be more susceptible to predation,' a finding also consistent with that of Crost and Felter,[99] who examine rebel predation of banana plantations in the southern Philippines during periods when the price of export bananas is rising. These papers do not, however, seek to explain the evolution of industrial organisation in such countries, although implicit in both is the argument that large firms with more assets are better equipped to cope with the costs associated with predation.

While much of the relevant academic literature has unsurprisingly focused on the downsides of conflict for an economy, some agents are likely more capable than others to survive or even thrive in such environments, owing either to the lack of competition or their ability to channel violence to profitable ends. As noted previously, large, established firms might hire security guards to protect their plants and workers. Mines, oil wells, and other capital-intensive operations, often managed by multinational enterprises, can continue to function even in the heat of violent conflict, as they seem capable of establishing 'zones of peace' around the firm. In short, firms that are able to protect themselves in conflict zones can earn rents from their unique ability to manage in such environments.[100] Drawing on the case of Liberia, McDougal finds that some firms are better than others at adapting their supply chains in response to violence.[101] They have networks that enable them to change suppliers quickly, thus maintaining their ability to function.

3. Donor-led approaches to PSD in FCAS

The international donor community is devoting increasing attention and resources to FCAS. The 2016 UK Aid White Paper, for example, states: 'the government will…allocate 50% of DFID's budget to fragile states and regions in every year of this parliament'.[102] Similarly, USAID is devoting an increasing share of its resources to fragile states; Afghanistan was the largest single recipient of American foreign aid, and the Middle East and North Africa has been overall the largest region. This section reviews some of the policy literature on PSD in FCAS and examines to what extent it has been informed by academic research and the findings to date of the donor community.

Donor commitment to PSD begins with the 'broad consensus that creating economic opportunities is critical to addressing fragility and conflict and that economic recovery is a vital aspect of state building.'[103] But what does the international community mean by PSD, particularly in the context of FCAS? PSD interventions in FCAS are overwhelmingly focused on support for MSMEs. As a recent report by the Overseas Development Institute (ODI) puts the conventional wisdom, 'development agencies…increasingly see MSMEs as channels to promote employment, value chain development, innovation, economic and social inclusion, and

98 Timothy Besley and Hannes Mueller, "Estimating the Peace Dividend: The Impact of Violence on House Prices in Northern Ireland," American Economic Review 102, no. 2, 2012.

99 Benjamin Crost, Joseph H. Felter and Patrick B. Johnston, "Conditional cash transfers, civil conflict and insurgent influence: Experimental evidence from the Philippines," Journal of Development Economics 118, issue C, (2016):171-182

100 Massimo Guidolin and Eliana La Ferrara, "Diamonds Are Forever, Wars Are Not: Is Conflict Bad for Private Firms?" American Economic Review 97 no. 5, 2007.

101 Topher L. McDougal, "How Production Firms Adapt to War: The Case of Liberia," WIDER Working Paper Series wp-2010-069, World Institute for Development Economic Research (UNU-WIDER), 2010.

102 "UK Aid: Tackling global challenges in the national interest," HM Treasury and DFID, 2015. https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/478834/ODA_strategy_final_web_0905.pdf

103 William Robert Avis, "Private Sector Engagement in Fragile and Conflict-Affected Settings", GSDRC Helpdesk Research Report 1331, January 2016. http://gsdrc.org/publications/private-sector-engagement-in-fragile-and-conflict-affected-settings/

resilience in FCAS'.[104] This is premised on the prevailing assumption among governments and development practitioners that, by providing jobs and underpinning economic prosperity, MSMEs can contribute to peace, or at least create disincentives for conflict. Since MSMEs account for the largest share of employment and, sometimes, most of the economic activity in fragile situations, this dominant narrative suggests that expanding the MSME sector can contribute to peace. Indeed, PSD tends to be defined as support for MSMEs. This leads to the policy question, 'what do MSMEs need in order to thrive?' Large firms in FCAS are almost entirely left out of the ensuing discussion.

How best to support PSD remains contested within the donor community, although as we will see most donors tend to focus on finance as the great shortfall facing the MSME community. Mac Sweeney usefully distinguishes between two broad approaches that donors have adopted to date, which she labels 'interventionist' and 'investment climate';[105] Datzberger and Denison borrow the economic terms 'micro' and 'macro' to define these approaches.[106] Interventionist or micro approaches refer to those programmes that provide direct support to entrepreneurs or the business community, including through financing, employment and training programmes, the development of business associations, and programmes aimed at linking local firms to regional and international markets. Investment climate or macro programming, in contrast, emphasises such things as the quality of the legal and regulatory environments, the strengthening of financial institutions and central banks, and the promotion of foreign direct investment. To be sure, both types of programming are potentially important and in fact complimentary. But which one has proved most effective?

A 2016 study by the IFC aimed to assess that question by evaluationg 56 PSD projects in FCAS. Overall, it found direct interventions to be 'most successful,' particularly those designed to support small and medium-sized enterprises (SMEs). In contrast, 'projects to improve the business environment and support intermediaries in financial sectors had the lowest overall ratings for effectiveness...'[107] Similar findings emerge from a study prepared by Germany's GIZ who define three possible levels of PSD interventions in an economy: '(1) the macro level, usually addressing policies and framework conditions and the business environment; (2) the meso level, usually addressing markets and sectors, as well as intermediary organisations providing services to businesses; and (3) the micro level, usually focusing on the enterprise dimension.' They conclude that macro-level interventions should be avoided in situations of open conflict, and that 'the most promising area for intervention is the micro level...[which] offers significant potential. For instance, local business support offers opportunities for immediate effects in job and income generation, potentially becoming a stimulus for local economic development.'[108]

Note that these findings are puzzling in some respects, at least at first glance. It would seem very difficult to promote the fortunes of individual businesses if the overall business climate is hostile to entrepreneurship. For example, it is challenging for firms – especially small firms – to succeed if property rights and the legal regime are weak, and/or if the government is corrupt. Larger firms might be more capable of handling these challenges.

Part of the puzzle may lie in the definitions of 'success' or 'effectiveness,' and the time horizon over which outcomes are expected to be realised. As a report for Germany's GIZ states, results in conflict-affected states tend to be 'achieved slowly, and a realistic theory of change and timeline for implementation are needed.'[109] A programme designed to provide microfinance to women

104 Alastair McKechnie et al, "MSME-led private sector development in contexts of conflict, fragility and displacement," ODI. October 2022.
https://cdn.odi.org/media/documents/ODI_MSME-led_private_sector_development_in_contexts_of_conflict_B91hml5.pdf

105 Naoise Mac Sweeney, "Private Sector Development in Post-Conflict Countries: A Review of Current Literature and Practice," Donor Committee for Enterprise Development, 2008. https://www.enterprise-development.org/wp-content/uploads/PostConflict_PSD_EN.pdf

106 Simone Datzberger and Mike Denison, "Private Sector Development in Fragile States," Economics and Private Sector Professional Evidence and Applied Knowledge Services to the DfID, September 2013.
https://assets.publishing.service.gov.uk/media/57a08a2ced915d622c0005cf/Private_Sector_Development_in_Fragile_States.pdf

107 Chaoying Liu and Emily Harwit, "The Effectiveness of Private Sector Development Interventions in Fragile and Conflict-Affected Situations: Evidence from Evaluations Report," Development Impact Dep[artment, International Finance Corporation, November 2016.
https://openknowledge.worldbank.org/handle/10986/28497

108 Urs Schrade, Birgit Seibel, Christine Weinreich and Susanne Reichenbach, "Is there a Case for Private Sector Development Interventions in Contexts of Open and Sustained Violence? Discussion paper," GIZ, February 2017.
https://www.enterprise-development.org/wp-content/uploads/GIZ-CFAE-PSD-in-Open-Sustained-Violence.pdf

109 Ibid.

entrepreneurs, for example, may 'succeed' in helping to buy sewing machines over the short-run, even if it has little impact on macro-outcomes over the long-term like poverty reduction (including reducing the poverty of the borrowers). More generally, altering a country's investment climate is a much more complicated task than rolling out a small-scale, targeted programme, and surely one that cannot be completed in a similar time-frame.

Taking a very different but nonetheless fully appropriate approach to success and failure, the GIZ research team emphasises the management and implementation capacities of the donors as being crucial variables. In particular, given the threat of violent conflict, donors must be adaptable and learn to manage projects from a distance if they are to succeed. All-too-often, rigid bureaucratic constraints on operations pose conditions that make it difficult for foreign aid workers on the ground to carry out their programmes in light of rapidly changing conditions (Schrade et.al. 2016). Realistically but nonetheless problematically, this report seems to suggest that the definition of a programme's success or failure may need to be adjusted in light of conditions on the ground.

For its part, a study done on behalf of DFID on PSD in so-called 'transition countries' – those that are attaining middle-income status but risk rapid back-sliding because, for example, of a heavy dependence on commodity prices – argues that donors must consider support beyond money. In particular, the study forthrightly recommends that donors engage governments directly on political economy issues (something that many have been hesitant to address in the past); that they act as facilitators between foreign multinationals and local enterprises in order to develop synergies between them; and that they engage more across their own governments both in the interest of seeking relevant expertise (e.g. calling upon agricultural experts housed in that specialised ministry) and the reduction of policy incoherence.[110]

A 'meta-evaluation' of EU development programming in the area of PSD undertaken on behalf of the European Commission's Directorate-General for International Cooperation and Development (Devco) provides an additional perspective that is quite important in the context of donor activities in FCAS.[111] This study observed that disagreements over what constitutes effective programming within the EU (e.g. should such programmes be 'top-down versus bottom up') were shaped in large measure by the absence of rigorous monitoring and evaluation (M&E) projects which could provide a more solid evidence base for policy discussions. This evaluation recommends that M&E be incorporated at the design stage of donor programming, a view that is increasingly expressed across the donor community if not always adopted once the costs become apparent. Indeed, uptake of that idea is lagging, not only because of the costs associated with M&E, but also due to the logistical difficulties associated with continuing M&E work once a project is completed and the relevant staff withdrawn.

4 Donor-led approaches to PSE

In addition to its efforts aimed at developing private enterprise, international donors are now actively seeking to engage with existing firms as well. This policy of PSE recognises that firms in developing countries are critical stakeholders in planning and designing sustainable interventions and are also well-placed to execute on a wide array of projects, particularly those that have humanitarian and developmental consequences. Local firms have the supply chains, distribution networks, and political and social networks needed to get goods and services to the population, an effort that would be far more challenging for foreign firms or humanitarian/development agencies without this local knowledge and infrastructure. Making intensive use of local firms, therefore, seems obvious from an efficiency and effectiveness standpoint, yet it is only recently that the international development community has thought about it in a more reflective manner.

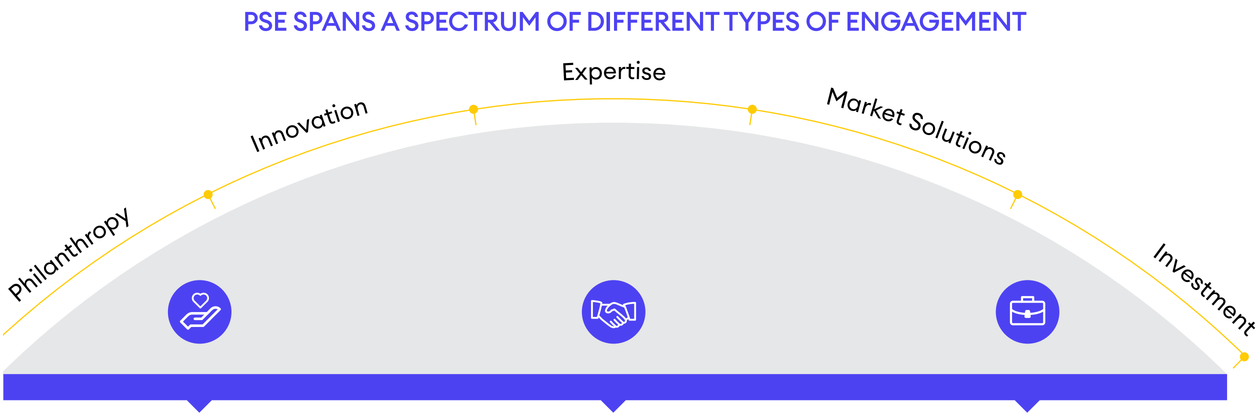
Indeed, defining PSE remains elusive. USAID, for example, states that PSE is 'a strategic approach to planning and programming through which USAID consults, strategises, aligns, collaborates, and implements with the private sector for greater scale, sustainability, and effectiveness of development or humanitarian outcomes.'[112] As one can see, such an open-ended definition does not distinguish between firms in the donor country (American firms in USAID's case) and local firms in recipient countries. USAID further defines a spectrum of different types of PSE engagements as shown in Figure 9.

110 Peter Davis, "Private Sector Development in Countries Progressing from Poverty," Final report to the UK Department for International Development, ECORYS, February 2016.
https://assets.publishing.service.gov.uk/media/57a0895a40f0b6497400002e/61510_Private-Sector-Development-in-Countries-Progressing-from-Poverty_040416.pdf

111 "Evaluation of the European Union's Support to Private Sector Dvelopment in Third Countries," Evaluation Unit of the Directorate General for Development and Cooperation, European Commission, 2013.
https://www.oecd.org/derec/ec/publicationsdocuments/privatesectorbusinessandindustry/1317_vol1_Main%20reports_EVAL_EU.pdf

112 USAID, "Private-Sector Engagement Policy," USAID.
https://www.usaid.gov/sites/default/files/2022-05/usaid_psepolicy_final.pdf

Figure 9 Types of PSE engagement



DONOR-LED

- USAID is the driver
- Activities and assistance leverage private-sector resources and expertise
- Might or might not be aligned with commercial interests or core business operations

CO-CREATION

- USAID is a co-creator
- Joint identification of challenges
- Joint design and programming that address shared interests, including through co-creation of market-based approaches

PRIVATE SECTOR-LED

- USAID is the facilitator
- Activities and assistance address private-sector constraints or risks
- Engagements build on for-profit and market-based approaches to challenges

Source: USAID Private-Sector Engagement Policy[113]

DCED further breaks down contemporary approaches to PSE into two areas: '1) Engaging (typically) large, international…companies as a key stakeholder or partner, around their core business or related activities; and 2) Engaging with private investors, funds and financial institutions, to leverage additional private finance or encourage its use towards…relevant projects'.[114] Again, there is little focus on local firms in recipient economies.

An example of the second area highlighted by DCED is the UN's Office for the Coordination of Humanitarian Affairs (OCHA) approach to PSE: 'Businesses are a major contributor to humanitarian action. Local and multinational companies can support humanitarian efforts by making a financial or in-kind contribution, providing a pro-bono service, supporting humanitarian appeals, engaging in advocacy and awareness of crises and promoting philanthropy among staff, clients and networks.'[115]

In summary, traditional PSE approaches by the donor community primarily seek out multinational firms that they can motivate to work in the developing world through various interventions. In that context it is worth noting that this has been an objective of U.S. foreign assistance policy since the end of World War II.[116] American officials have long believed that when multinationals invest in developing countries, they form linkages with local firms that builds up the capacity and skills of these domestic companies. This 'linkages strategy,'of course, was made famous by Albert Hirschman in his seminal writing on economic development.[117]

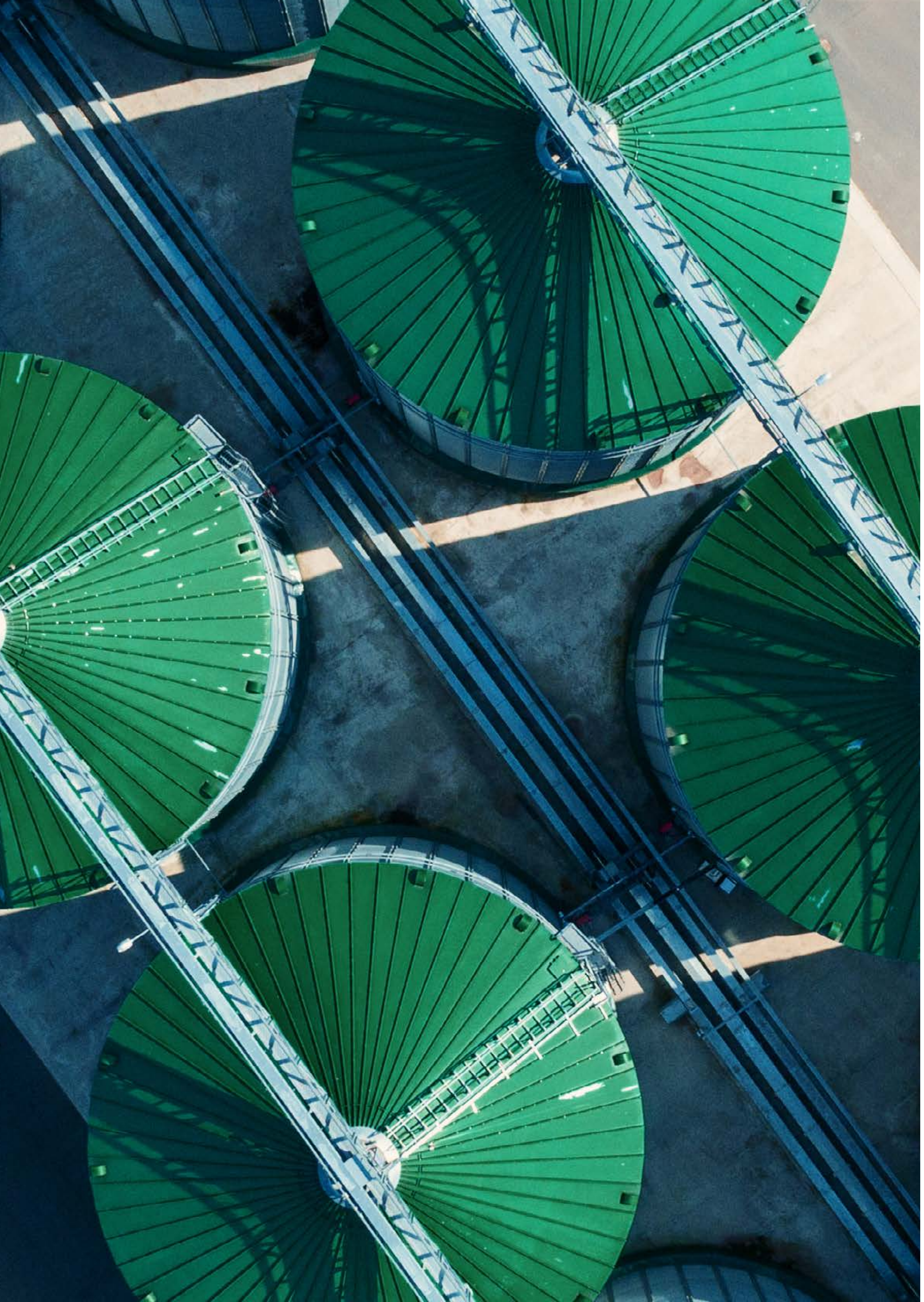
113 Ibid.

114 DCED website, "Private Sector Engagement," DCED. https://www.enterprise-development.org/implementing-psd/private-sector-engagement/

115 "How the private sector helps in emergencies," OCHA. https://www.unocha.org/es/themes/engagement-private-sector/how-private-sector-helps-emergencies

116 Ethan B. Kapstein, "Exporting Capitalism: Private Enterprise and U.S. Foreign Policy," Harvard University Press, 2022.

117 Albert O. Hirschman and Gerald Sirkin, "Investment Criteria and Capital Intensity Once Again," The Quarterly Journal of Economics, Volume 72, Issue 3, August 1958.



ANNEX 1: MAPPING OF DONOR-FUNDED PSD PROJECTS IN YEMEN[118]

118 Parts of the data provided in this mapping is quoted from the report "Economic Empowerment of Youth and Women in Yemen", co-authored by Rafat Al-Akhali and Marta Colburn for Proximity International and Particip GmbH, co-funded by the European Union and GIZ.

ANNEX 1: MAPPING OF DONOR-FUNDED PSD PROJECTS IN YEMEN

No.	Donor	Project Name	Sectoral Approach	Implementers/Sub-implementers	Intervention Level (Macro/ Meso/Micro)[119]	Size of Target Beneficiary[120]	Intervention Type
1.	Germany – BMZ	Promotion of the private sector and employment in Yemen	This EUR 10 million project (Jul 2019 – Jun 2024) aims to improve income and employability in selected value chains in the solar sector through: Support services (including advisory, business knowledge, and technical skills) to 1,500 micro and small enterprises (including women-led enterprises). Train 3,000 participants (including women) in financial literacy and access to financial services. Provide technical and vocational education and training (TVET) and business training to 900 young people. Provide technical and process support to microfinance institutions (MFIs) (including market studies, training, and coaching).	Deutsche Gesellschaft für Internationale Zusammenarbeit GmbH (GIZ)	Micro and Meso	Micro/Small/ Medium	Capacity building
2.	Germany – BMZ	Support to Microfinance Sector	The current portfolio is EUR 16.5 million. KfW has currently two investment grants and one technical assistance measure in implementation with the SFD SMED Unit project (2020–2023). It aims to provide refinancing and capacity support for microfinance institutions to ensure sustainable access to financial services for Yemeni MSMEs. It also supports capacity development in the microfinance sector. The planned results include: SFD has received funds to refinance MFIs (interest-free), and once MFIs repay they will use the funds again for the same purpose (revolving use of funds). 6 microfinance programmes have received capacity building and access to loans from the revolving fund.	Kreditanstalt für Wiederaufbau(KfW) Through the: Social Fund for Development (SFD) – Small and Medium-sized Enterprise Development (SMED)	Meso	Small/ Medium	Access to finance Capacity building
3.	EU	Promoting Economic Resilience in Yemen	This EUR 9.49 million project (2021–2023) aims to: Enable key central-level economic institutions to lead economic recovery and create the conditions for PSD. Promote resilience and PSD, focusing on job creation and employment of youth, women, and internally displaced persons (IDPs). Support donor coordination and policy coherence.	Organisation for Economic Cooperation and Development (OECD)	Macro	All	Technical assistance to improve the business environment
4.	EU	Support to Youth's Entrepreneurship and Financial Inclusion	This EUR 6.15 million action project (2018–2021) followed by a new EUR 10 million project (2023–2027) addresses economic empowerment needs in the following sectors: Entrepreneurship with youth (aged 18–35, 40% funding designated for women), with training provided by Reyadah. Access to microfinance to start/recover business and create jobs.	Silatech Foundation, a Qatari-based international development non-profit organisation that focuses on the economic empowerment of youth. Al-Amal Microfinance Bank (AMB), the first microfinance bank in Yemen and the MENA.	Micro	Micro	Access to finance
5.	EU & Netherlands	Rethinking Yemen's Economy	This Track II initiative brought together Yemeni experts from diverse backgrounds to analyse key economic challenges, propose solutions to address them, and engage with national and international stakeholders to promote these solutions (with a focus on policy and legal frameworks). Two funding cycles have been completed for this project (2017–2021) with a total budget of EUR 2.31 million and a third cycle started in 2022.	CARPO, a German-based research firm focusing on building partnerships with stakeholders in Europe and the Middle East working with: DeepRoot, a boutique consulting firm anchoring interventions in local contexts. Sana'a Center for Strategic Studies, an independent think-tank focusing on Yemen and the region.	Meso/ Macro	All	Private sector engagement Business environment
6.	Saudi Development & Reconstruction Program for Yemen (SDRPY)	Saba Project for the Economic Empowerment of Yemeni Women	This USD 212,940 project with a duration of 18 months targets women entrepreneurs in Marib providing them with vocational education and training, entrepreneurship training, and access to finance through grants.	Marib Girls Foundation	Micro	Micro	Capacity building Access to finance
7.	Saudi Development & Reconstruction Program for Yemen (SDRPY)	Mustaqbal Project	This USD 606,100 project with a duration of 24 months provides vocational education and training, entrepreneurship training, and access to formal and informal income earning opportunities for youth in Aden, Abyan, and Lahj.	Yemen Education for Employment	Micro	Micro	Capacity building Access to finance

120 Yemeni legal frameworks define micro as 1–3 workers, small as 4–9 workers, medium as 10–50 workers, and large as over 50 workers.

ANNEX 1: MAPPING OF DONOR-FUNDED PSD PROJECTS IN YEMEN

No.	Donor	Project Name	Sectoral Approach	Implementers/Sub-implementers	Intervention Level (Macro/ Meso/Micro)[119]	Size of Target Beneficiary[120]	Intervention Type
8.	USAID	Economic Recovery and Livelihoods Program (ERLP). Strengthening capacity of key economic institutions, facilitating flow of commercial and humanitarian goods and services through Yemen's borders and ports, supporting SMEs to improve fish and farm productivity and establish linkages to domestic and international markets. FCDO funded a tandem project entitled Economic Stablisation Project II (Sep 2020 to Mar 2022) in the amount of GBP 3,093,147. Pragma implemented an earlier USAID-funded project Yemen Economic Stabilisation and Support (YESS) Oct 2017 to Sep 2020.	This USD 27,408,907 project (2020–2023) aims to strengthen the capacity of key economic institutions, facilitate the flow of commercial and humanitarian assistance through Yemen's borders and ports, and support SMEs to improve fish and farm productivity and establish linkages to domestic and international markets. It supports economic empowerment activities in the following sectors: Improve economic performance through macro-fiscal reform, including rebuilding a strong CBY, establish a monetary control framework, develop an electronic payment system, strengthen foreign exchange management. Improve microeconomic conditions and livelihoods by raising household incomes, strengthening SMEs, and improving the performance of agricultural and fisheries sectors. Trade facilitation through modernising systems to increase flow of goods, applying international best practices, building collaboration between public/private sector actors with greater transparency, efficiency, risk-reduction, and dialogue. Work with government authorities and private sector to put in place best practices for increasing transparency and eliminating corrupt practices.	The Pragma Corporation, US-based for-profit organisation working in international development consulting	Micro / Meso / Macro	All	Business environment Capacity building Access to finance Value chain development
9.	EU, SIDA	Supporting Resilient Livelihoods and Food Security in Yemen Joint Programme – ERRY Phase III	**This EUR 45.1 million initiative (2019–2022) supports economic empowerment activities that target the most vulnerable community groups, including women, unemployed youth, *Muhammasheen*, IDPs, and stressed host communities in the following sectors:** Food/cash for assets. Revitalization of small-scale service delivery. Job and employment creation. Enhancement of productive assets and capacities. Building local capacity to contribute to community self-reliance. Strengthening cohesion among displaced, returnees, refugees, and host communities. Employability (training and apprentices) and entrepreneur skills and TVET.	United Nations Development Programme (UNDP) Food and Agriculture Organisation (FAO) World Food Programme (WFP) International Labour Organisation (ILO) Working with 24 implementing partners	Micro	Micro	Capacity building Access to finance
10.	EU	Enhancing Rural Resilience in Yemen Joint Programme (ERRY II)	This EUR 47.4 million initiative (2016–2019) had the overall objective to enhance the resilience and self-reliance of crisis-affected rural communities through support to rehabilitation of community infrastructure, livelihoods stabilisation and recovery, social cohesion and local governance and improved access to sustainable energy.	UNDP, FAO, ILO and WFP, with a range of international and local partners	Micro	Micro	Capacity building Access to finance
11.	EU	Strengthening Institutional and Economic Resilience in Yemen (SIERY)	This EUR 74.1 million project (2020–2023) provides economic empowerment activities with a specific focus on the poorest and most vulnerable focusing on the following sectors: Economic livelihoods through private sector support including business advisory services to MSMEs and MFIs. Local governance supporting resilience and recovery including interventions to promote community self-reliance and support to civil society. Service delivery including community infrastructure in education and health care. Key activities include: Analysing value chains in promising sectors, such as coffee, honey, horticulture, livestock, fisheries, and renewable energy. Strengthening a value chain approach by empowering producers, private sectors, and microfinance service providers for skill development, capital support, job creation, and employment. Supporting the recovery of market infrastructure, providing inputs, and improving access to support SMEs for collective growth for the expansion and scaling-up of businesses. Enabling and engaging microfinance service providers and network, private sector or business associations and regulators to support producers, private sectors, and local authorities to de-risk unstable market environment.	UNDP working with: PWP SMEPS Yemen Microfinance Network (YMN), a non-profit NGO established through a joint initiative by UNDP and the SFD in August 2010 as Yemen's national microfinance association	Micro/ Meso	Micro / Small/ Medium	Capacity building Access to finance Value chain development
12.	Japanese Government	Rebuilding Livelihoods and Capacities of Conflict-Affected Small-Scale Fisheries Households in Aden and Hadramaut (RELAC)	This USD 3 million project (Nov 2021 – Apr 2022) had the goal to strengthen the capacity of the targeted fishery communities whose livelihoods have been severely disrupted to adapt to the effects of both the ongoing conflict and the impact of the COVID-19 pandemic. Objectives: To improve households dependent on fisheries access to self-learning for productive assets for self-reliance in two communities of the targeted governorates, Aden and Hadramaut, through providing on the job training and fishing equipment to targeted beneficiaries in coastal communities. To improve women and youth income opportunities options through micro and small-scale enterprises in the targeted communities of Aden and Hadramaut through providing business skills trainings to 1,000 women and youth and micro-business grants to 500 HHs in the fisheries sector.	UNDP in partnership with Youth Leadership Development Foundation (YLDF)	Micro	Micro	Capacity building Access to finance
13.	Japanese Government	Women's Leadership, Empowerment, Access & Protection (LEAP)	This USD 1.5 million project (Aug 2020 – Mar 2021) was a local initiative under the UN Women global flagship programme providing livelihoods and protection services to women in six governorates. Programming included support for temporary shelters and skills training, cash-for-work, and livelihoods support.	UN Women Youth Leadership Development Foundation (YLDF) Sama Center also known as the Al-Usra Al-Sa'ada Association (Happy Family), based in Mukalla, Hadramaut.	Micro	Micro	Capacity building Access to finance

ANNEX 1: MAPPING OF DONOR-FUNDED PSD PROJECTS IN YEMEN

No.	Donor	Project Name	Sectoral Approach	Implementers/Sub-implementers	Intervention Level (Macro/ Meso/Micro)[119]	Size of Target Beneficiary[120]	Intervention Type
14.	Saudi Development & Reconstruction Program for Yemen (SDRPY)	Hirfa sewing and handicraft workshop	This USD 61,928 project (Jan 2021 – Jan 2022) targeted poor and marginalised women divorcees and widows in Socotra. The programme provided a workshop space (rented facility) and equipped it with sewing machines and handicraft tools and equipment. The project targeted 102 women.	Socotri Woman Association for Development	Micro	Micro	Capacity building Access to finance
15.	Saudi Development & Reconstruction Program for Yemen (SDRPY)	Supporting livelihoods of affected communities	This USD 4.44 million (Mar 2021 – Mar 2022) aims to support farmers, cattle rearers, and fishermen with capacity building and asset support to improve their livelihoods.	SMEPS	Micro	Micro	Capacity building Access to finance
16.	Islamic Development Bank, under the We-Fi Initiative	BRAVE Program (Business Resilience Assistance for Value-adding Enterprises)	This USD 8.8 million project (2018–2023) funded by the We-Fi initiative through the Islamic Development Bank (IsDB) aims to increase business growth opportunities for women entrepreneurs in Yemen by boosting investment and providing capacity-building training: Building the capacity and business resilience of women-owned SMEs in fragile and high-risk contexts. Providing business recovery and financial support to women entrepreneurs. Building the resilience of value chains in the country. Creation of the BRAVE IT platform to improve the interaction with entrepreneurs.	SMEPS channelling grants to beneficiaries through Kuraimi, Tadhamon International Islamic Bank and Saba Islamic Bank	Micro	Micro	Capacity building Access to finance
17.	Saudi Arabia	Deposit to CBY	A USD 2 billion deposit to the CBY allocated to cover the foreign currency needs for the import of basic commodities (2018–2022).	Central Bank of Yemen	Macro	Medium / Large	Access to foreign currency / Monetary stability
18.	IFC/FMO	Line of credit to HSA Group	The financing package includes a loan of up to USD 55 million from the IFC and a syndicated loan from FMO, the Dutch Entrepreneurial Development Bank, of up to USD 20 million. The financing package includes a first-loss guarantee of up to 50 percent from the International Development Association's Private Sector Window. The debt financing is provided to HSA Group for their operations in Yemen. The financing will be used as working capital for six food companies operating in the dairy, flour, and sugar sectors.	IFC/FMO/HSA Group	Micro	Large	Access to finance
19.	World Bank/ FCDO	Yemen Private Sector Cluster	The Yemen Private Sector Cluster [YPSC] was established and launched in January 28, 2019, with funding from the World Bank and later funding from FCDO. The cluster is composed of representatives of the major private sector entities including the chambers of commerce from all regions of the country and key business management associations. The YPSC aims to align and coordinate the efforts of the Yemeni private sector in the ongoing humanitarian, development, recovery and reconstruction efforts giving it a voice in economic decision making. It was designed as a platform linking the private sector to the government, national, international agencies and the UN to create strong strategic partnerships in emergency, peace building, and stabilisation efforts.	SMEPS	Macro	All	Private sector engagement Business environment

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