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REPUBLIC OF YEMEN

Joint Staff Assessment of the Poverty Reduction Strategy Paper

Prepared by the Staffs of the International Development Association
and the International Monetary Fund

Approved by Jean-Louis Sarbib and Gobind Nankani (IDA)
and George T. Abed and G. Russell Kincaid (IMF)

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I. OVERVIEW

1. **The Poverty Reduction Strategy Paper (PRSP) of the Government of Yemen builds on the interim strategy (I-PRSP) presented to the Boards of the IDA and the Fund in February 2001 and presents the government's strategy for poverty reduction in Yemen for the period 2003–05.** The preparation of the strategy involved extensive consultations among government agencies and with civil society, stakeholders, including the poor. It also benefited from broad donor support during its preparation. The PRSP's main strengths are (i) an active participatory and consultative process; (ii) a macroeconomic framework geared towards maintaining stability as a condition for economic growth and poverty reduction; (iii) a thorough diagnosis of poverty and its multi-dimensional nature; (iv) recognition of a wide gender gap, weak governance structures, lack of security and poor delivery of public services and their impact on poverty; and (v) the identification of challenges and program areas critical for poverty reduction.

2. **While the PRSP presents a comprehensive and coherent strategy for poverty reduction in Yemen, additional work is needed in several key areas,** notably to (i) strengthen identification, costing, and monitoring of programs for poverty reduction; (ii) improve prioritization of government actions and budgetary allocations; (iii) improve transparency and build a capable and accountable public administration that efficiently delivers public services and deals with business environment and security issues which are crucial to higher and sustained GDP growth and effective poverty reduction; (iv) build the institutional capacity to implement, monitor, and evaluate the PRSP and strengthen coordination among the various agencies involved in the social safety net; (v) better address environmental sustainability issues, especially water; (vi) develop better information on population dynamics and subsequently a multi-pronged population management program; and (vii) integrate more effectively gender issues in the implementation of the strategy.

3. **Implementation of the strategy is subject to a number of risks related to possible external shocks as well as weaknesses in capacity and commitment.** The economy will remain vulnerable to oil price volatility and to droughts. In order to protect the poverty reduction objectives from the fiscal implications of such shocks, specific contingency measures need to be developed. Weaknesses in governance, implementation capacity, and an insufficient base of support for reform may also threaten the attainment of the PRSP targets. Strengthened national capacity and strong political leadership will be needed to limit these risks.

II. THE PARTICIPATORY PROCESS

4. **The PRSP preparation has been characterized by strong government ownership and broad consultation.** The National Committee for the Preparation of the PRSP comprised 21 members, chaired by the vice-minister of the ministry of planning and development, and has included officials from six central ministries (planning and development, finance, labor and social affairs, health and population, tourism and environment, and education); representatives of the Central Statistical Organization (CSO), National Committee for Human Rights, National Women Committee, universities and specialized institutes, an NGO, strategy and planning consultants, and a representative of civil society. As described in some detail in Chapter 1, preparation of the PRSP included extensive consultations with large sections of Yemeni civil society, members of the parliament, media, NGOs, and others, and perhaps most importantly, the poor. A number of workshops (thematic and regional) and consultative meetings were held around the country, beginning in early 2000 for the interim strategy and extending up to the finalization of the strategy. An early survey of the voices of the poor was conducted in 2000, followed in 2002 by field visits and participation of the poor in 20 districts with the highest incidence of poverty.

5. **The PRSP document also builds on a number of government development plans and is being widely disseminated.** To fill knowledge gaps in specific areas, the PRSP team also commissioned the preparation of special reports and background papers by consultants and experts.¹ The PRSP draws from the Poverty Reduction and Job Creation Program and the I-PRSP as well as the Second Five-Year Plan (SFYP: 2001–05) and the Strategic Vision for the year 2025, which were approved by parliament/Shura Councils in January 2002. The government prepared the PRSP in Arabic to ensure wider dissemination of the document

¹Topics were decided by the PRSP team and were advertised in the local media. The background papers covered the following issues: (i) analysis of poverty and its causes; (ii) causes of poverty and basic priorities at the governorate level; (iii) the role of the agricultural sector and cooperatives in poverty reduction; (iv) the role of the fisheries sector and cooperatives in poverty reduction; (v) challenges of the labor market in Yemen; (vi) evaluation of the effectiveness of the social safety net; (vii) role of civil society organizations in poverty reduction; (viii) impact of cuts in subsidies on consumers and farmers; (ix) the education sector and strategies for its upgrade for poverty reduction; (x) the health sector and reform strategies for poverty reduction; (xi) women and poverty; (xii) the private sector and its role in poverty reduction; (xiii) globalization and international trade and their impact on poverty; and (xiv) voices of the poor.

after its final approval. The PRSP document (in both Arabic and English) has been posted on government official web sites (e.g., <http://www.mpd-yemen.org>). At the government's request, a number of development partners (including the World Bank and the IMF) provided input to the development of the strategy (e.g., poverty analysis, sources of economic growth, macroeconomic framework and projections, medium term expenditure framework, and other areas).

6. **Meetings were held in May and June 2002 with representatives of donor agencies and international NGOs**, in which the draft PRSP document was disseminated. Participants welcomed the PRSP and appreciated the analysis and the identification of challenges. Their main concerns included lack of priority public actions in the areas of corruption, security, weak enforcement of laws, as well as weaknesses in the proposed monitoring and evaluation set-up. Further meetings are scheduled in the summer of 2002 to discuss implementation of the strategy and the role of the international community therein. In addition to the PRSP, the government plans to share with the international community its first Millennium Development Goals (MDG) Report at the occasion of the donors' Consultative Group (CG) meeting scheduled for October 2002.

III. POVERTY DIAGNOSIS

7. **Three surveys were conducted in the 1990s: the 1992 and 1998 Household Budget Surveys (HBSs) and the 1999 National Poverty Survey (NPS)**. The 1992 dataset is incomplete and has many weaknesses. The 1998 HBS was implemented over four rounds covering the entire calendar year, capturing differences in household expenditures due to seasonality effects, with a sample size of about 14,000 households. The 1999 NPS had a much larger sample, designed primarily to inform on access to services and other aspects of nonincome living standards at the district level. The 1999 NPS, however, is not suitable for measuring income poverty because household expenditures were recorded for only one month. Therefore, it was not possible to provide a trend analysis of poverty in Yemen. The 1998 HBS was used to establish the baseline of measuring income poverty in Yemen.

8. **The PRSP provides a sound and comprehensive poverty diagnosis despite existing data and methodological constraints**. The determinants of poverty are well identified based on the 1998 HBS with additional information from the 1999 NPS. The poverty estimates in the PRSP show that poverty is widespread with 18 percent and 42 percent of Yemenis under the food-poverty and the low-poverty lines respectively in 1998. Many households are also vulnerable to shocks, with a large proportion living just above the poverty line. The poverty diagnosis also made a good assessment of the current constraints (e.g., in agriculture), weaknesses in programs (e.g., on safety nets), and the key concerns of the poor.

9. **The PRSP provides a comprehensive picture of the status and trends in basic needs and core social development indicators**. Children and women and the rural population without access to education and health services are the most deprived. Data are disaggregated in many instances by gender, by governorate and by habitat (rural/urban).

Despite the absence of comparable poverty indicators covering the 1990s, the analysis makes a good attempt at assessing the impact of past policies, trends in economic growth and the impact of adverse shocks in the early 1990s. The analysis also addresses the distributional impact of government programs and inefficiencies in public spending and service delivery.

10. **The PRSP shows that poverty in Yemen is predominantly a rural phenomenon** (83 percent of the poor and 87 percent of those under the food poverty line live in rural areas). Poverty is especially concentrated in four governorates. Large family size, high dependency ratios, location in rural areas, and lack of education were identified in the analysis as being correlated with poverty in Yemen. Poverty analysis undertaken by Bank staff confirm the PRSP's conclusions that current public expenditures in social sectors (education and health) are mildly pro-poor, but current service provision does not address the magnitude of the rural/urban and gender gaps.

IV. THE POVERTY REDUCTION STRATEGY

11. **The PRSP presents a coherent and outcome-oriented medium- and long-term framework for poverty reduction in Yemen, which is generally sound, although effective implementation of the strategy will require clearer definitions of programs and priorities and a reinforcement of implementation capacity.** The poverty reduction strategy is based on four major pillars: (i) achieving a high and sustained rate of economic growth; (ii) enhancing human resources development; (iii) improving basic infrastructure and access to basic services; and (iv) enforcing and strengthening social safety nets. Good governance, broader participation, environmental sustainability, and effective inclusion of gender are identified as cross-cutting themes in the strategy. The PRSP recognizes the importance of broad-based pro-poor economic growth as the most important pillar for poverty reduction in Yemen. The staffs agree that these areas of focus adequately address the root causes of poverty in the country, and they consider the policy action plan and the programs and projects set forth in the strategy to be broadly consistent with the objectives of the PRSP. Nonetheless, staffs consider that implementation of the strategy will hinge on further work in several areas, including an agenda for governance reform, the setting of priorities, clearer linkages between programs and desired outcomes, the development of contingency measures in the event of adverse shocks, improvements in monitoring, budgeting, and implementation capacity, and enhanced attention to environment, gender, and population issues. The authorities are encouraged to address these issues in the annual progress report on implementation of the PRSP.

A. Targets, Indicators, and Monitoring

12. **The goals, targets, and intermediate indicators presented in the PRSP are selective, well identified and consistent with the MDGs. They are, however, ambitious, and their attainment will require improvements in the institutional and implementation capacity of public service delivery agencies.** The indicators of progress are established with annual and medium-term targets, as set out in Chapter 5. The main goals of the PRSP include: (i) reducing incidence of poverty by about 13 percent between 2003 and 2005 to

reach 35.9 percent, mainly through achieving an average annual GDP growth of 4.7 percent during the period; and (ii) raising coverage of social services (65 percent for health coverage, 69.3 percent enrollment in basic education, coverage of 600,000 families under the Social Welfare Fund, 40.3 percent electricity coverage, and others). If these are reached, Yemen will be on course to achieve some of the MDGs. However, according to the PRSP targets, Yemen will not be able to meet the MDGs that focus on elimination of the gender gap in basic and secondary education by 2005.

13. **The indicators and targets of the PRSP are consistent with the assessment of poverty and the disparities in the access to social and basic services.** Attention to reducing the gender gap is provided in terms of targets for education and maternal (and child health) indicators. But the gaps remain extraordinarily large (for example, maternal mortality rates are targeted to decline only modestly from 351 to 305). Absence of targets and programs with respect to improving adult literacy is also notable.

14. **Current monitoring and evaluation systems are inadequate, and the PRSP recognizes this obstacle and proposes a set of institutional and policy changes for better monitoring and evaluation.** The authorities are planning to undertake the third round of the household budget survey in 2003, which will provide an important input to the annual PRSP review, monitoring and evaluation, and the preparation of the next PRSP. In addition, the government, with the assistance of the UNDP, established a Poverty Information and Monitoring System (PIMS). The PIMS will use the 2003 HBS as well as other rapid surveys and techniques to facilitate the monitoring of poverty trends in Yemen as well as provision of services at disaggregated levels. The PRSP proposes to strengthen the capacities of the CSO to undertake surveys and to collect basic data, and the PIMS unit to coordinate efforts on poverty monitoring. Coordination among the funds providing social services and assistance is also weak, and a consolidated database for beneficiaries does not exist. These issues will require attention.

15. **The proposed monitoring and evaluation systems represent significant improvement to existing mechanisms.** Staffs, however, believe that the government needs to give a higher priority to strengthening these capacities and seek coordinated support from development partners to help build sustainable capacities in this area. In particular, to allow a more comprehensive analysis of poverty. The forthcoming 2003 HBS will need to be upgraded by improved information on access to public services and safety net programs. Also, it will need to allow comparability with the 1998 HBS in order to measure trends in poverty and program progress. Improvements in statistical capacity and in the capacity to analyze and use the information will be needed, including development of local research institute capacities. Statistical improvements will also be necessary in other areas, especially on the coverage of education and health services. Improvements to the monitoring and evaluation system should make use of the participatory methods and not limit the process to government agencies.

B. Macroeconomic Framework

16. **The macroeconomic framework is realistic and provides an appropriate guide to policies over the medium term.** The framework makes due recognition of the projected decline in oil revenues over the medium term and targets an appropriate fiscal policy response to ensure the long-term viability of the fiscal and external accounts. The PRSP contains a commitment to maintaining fiscal deficits below 4 percent of GDP and to keeping inflation below 10 percent.

17. **The PRSP rightly points to the acceleration of growth as key to reaching the poverty reduction targets.** Growth in the non-oil sector is targeted to increase gradually from a recent average of 5 percent to 7 percent by 2005, roughly in line with the targets of the I-PRSP. The growth objectives remain relatively ambitious but are, in the staffs' view, achievable provided: (i) the government addresses the governance and security problems, which hamper private sector activity generally; (ii) the PRSP strategy is fully implemented; and (iii) the country does not face major external or internal shocks as was the case in the early 1990s (e.g., civil unrest, drought, etc.). A stronger program to address governance issues is particularly important for private sector development, with emphasis on land rights, judicial processes, security and reduction of violence, transparency in government, and improvements in the overall business environment, public administration, and regulatory processes.

18. **The PRSP has much better analysis of the sources of growth, compared to the presentation in the I-PRSP, although the targets are ambitious.** The key sources of growth are identified as agriculture and fisheries, manufacturing, tourism, construction, trade, and re-export. The contributions of these sectors to overall growth appear generally achievable, but will involve major improvements in the policy and regulatory barriers to private activity. The more ambitious annual growth targets for fisheries (7.8 percent) and tourism (9.9 percent) reflect the very narrow base of these two sectors in the economy and, consequently, their potential for rapid growth.

19. **The proposed fiscal policy framework adequately balances the needs for overall fiscal adjustment and for an improved expenditure structure towards pro-poor and pro-growth programs.** The non-oil fiscal deficit is projected to decline from about 25 percent of GDP in 2002 to about 20 percent in 2005, while development spending is set to increase from 6.2 percent of GDP in 2002 to 7.8 percent in 2005. Achievement of these ambitious objectives will require strong political commitment to reform. In the absence of major new oil discoveries, the long-term viability of the fiscal and external accounts requires that adjustment be pursued at roughly the same pace well beyond 2005. In this context, lapses in fiscal adjustment would pose a risk to long-term sustainability. Underlying the improvement in the non-oil fiscal balance through 2005 are a projected increase in non-oil revenues, a phasing-out of subsidies on fuel, and retrenchment in military spending from the peak level reached in 2002. The policies and measures needed to achieve these objectives, although touched upon in the PRSP, will need to be more fully articulated. In particular, the authorities will need to (i) spell out a detailed tax reform plan on the basis of the review of

the tax system proposed to take place in 2002; (ii) commit to a specific timetable for closing the gap between domestic and international fuel prices; (iii) develop a rationalization plan for reducing military expenditures; and (iv) clarify the role of local governments in the development strategy and define upfront their claim on budgetary resources.

20. **The macroeconomic and fiscal frameworks will need to be updated and adapted in response to changes in macroeconomic conditions.** The PRSP does not present scenarios or provide for specific contingency plans in the event of adverse shocks (e.g., lower oil prices) or lower-than-expected growth. While the comfortable level of reserves can accommodate the impact of a temporary decline in oil prices (relative to the assumed path), a sustained reduction in oil revenues or lower-than-projected growth will put the fiscal targets at risk and will require additional adjustment. Alternative expenditure scenarios and clearer contingencies would help to deal with these risks, if they materialize. By the same token, a strategy for responding to higher oil prices or new oil discoveries needs to be outlined to ensure that medium-term adjustment targets are not undermined and that the additional resources are not directed to unproductive spending.

C. Policies for Implementing the Strategy

21. **Sectoral policies and the priority programs and projects set out in the PRSP appear broadly appropriate.** These include pursuit of economic reforms, raising productivity in the agricultural sector, conserving water usage and raising efficiency of irrigation, effective utilization of fishery resources while ensuring sustainability of the stock, promotion of tourism, control of rapid population growth, raising health coverage, raising enrollment levels in basic education and reducing the wide gender gap in enrollment rates, raising coverage of basic services and access to infrastructure, and expansion of the social security system and the social safety net. A list of policies was proposed for the achievement of the above targets as well as a list of priority programs and projects in each of the above areas. In general, the proposed policies and programs benefit from a review of past policies and interventions in various sectors.

22. **However, in some areas that have been identified as problems in the poverty diagnosis, the policy action plan remains weak.** Three main areas of insufficient attention are (i) improvements in governance, related to the financial management and probity in public expenditures, delivery of public services, and the business environment facing the private sector (e.g., transparency of public policies, land rights, judicial processes, security and reduction of violence, and regulatory framework); (ii) environmental sustainability of the strategy, especially given acute water shortages; and (iii) gender issues, especially in access to rural education and health services.

23. **While the PRSP contains a list of proposed policies and a set of programs and projects, no strict prioritization of public actions is provided, and it is not clear which policies or programs will have the most important effect on poverty reduction in Yemen.** In general, it is unclear how the policies relate to the lists of projects that are presented in the document. Staffs believe that the lack of clear prioritization of public action

is one of the major weaknesses of the PRSP. In the absence of such prioritization, resources may be stretched too thinly across many projects, undermining the overall efficiency of the strategy. Also, the focus on poverty reduction will be lost in the case of a shortfall in available resources. Furthermore, the document does not give adequate attention to the likely poverty and social impact of proposed programs and projects. In this context, there will be a need to develop measures to compensate for the effects of the planned phasing-out of fuel subsidies on poor and vulnerable households. The authorities proposed continuation of a differentiated structure of public utility rates (electricity, water, and sanitation) goes in this direction. Also, while the PRSP recognizes weaknesses in the social safety net, it still envisages continuation in multiple programs, with new initiatives, without due attention to rationalization of, and better coordination among, the programs.

24. **Lack of prioritization and weak linkage of programs to PRSP objectives reflect limited country capacity to cost programs and policies, and to budget and monitor expenditures on a functional (rather than economic) basis.** It also reflects the wide range of views expressed by domestic constituencies and donors through the participatory process. Staffs believe that further work and institutional capacity building in the above areas should be given a high priority by the authorities and development partners.

D. Public Expenditure Program and Financing

25. **The medium-term expenditure program contained in the PRSP is broadly consistent with the poverty reduction priorities of the strategy and represents a major improvement in the medium-term orientation of policies.** Despite its various shortcomings, the PRSP offers a first realistic approach to expenditure planning, grounded in an explicit macro-framework. The expenditure framework will, nonetheless, need to be refined and prioritized across subcategories to enhance the linkage with PRSP objectives. In particular, the proposed health sector program allocation appears to remain very low. A significant part of expenditures are executed through extra-budgetary funds and nonfinancial public enterprises, on which little information is currently available. Thus, effective implementation of the PRSP will require efforts to broaden the coverage of the budget. Similarly, the tracking of PRSP implementation will require the identification of all budgeted pro-poor expenditure in a base year for comparison purposes.

26. **For each of the four pillars of the strategy, the PRSP presents a complete list of programs and projects, the estimated costs of which are fully reflected in the expenditure program.** More effective budgeting and monitoring at the functional level, as well as enhancements in implementation and costing capacity will be required to strengthen the link between expenditure programs and desired outcomes. There will be a need to create a mechanism to ensure a link between priorities and the budgetary process, for instance through the issuance of specific guidelines to all agencies and governorates.

27. **The PRSP provides little information on the role of fiscal decentralization in the implementation of the PRSP.** Starting in 2002, the devolution of responsibility for new development spending as well as education and health expenditures to local authorities places

subnational governments at the center of the poverty reduction strategy. Accordingly, the authorities will need to clarify (i) how PRSP priorities will be reflected in the expenditure programs that are formulated by local governments; (ii) what share of resources will be transferred to local authorities to meet the overall spending priorities; (iii) how the strategy will ensure adequate redistribution of resources towards the poorer governorates; and (iv) how local government budgets will be managed to ensure adherence to the overall budget objectives set by the macroeconomic framework.

28. **The financing plan of the expenditure program appears realistic.** Although the PRSP lacks full balance-of-payments projections, the external financing assumptions of the PRSP are shown in the first table of Annex 2 (Priority Programs and Projects). Accordingly, the PRSP is built around realistic projections of total gross foreign financing, averaging about 4 percent of GDP per year for the period 2003–05. The magnitude of donor financing in support of the PRSP is still subject to some uncertainty (pending the CG meeting in October 2002). Staffs consider that additional donor assistance in the form of grants would allow for a correspondingly higher level of development and social spending. At the same time, the authorities should develop appropriate contingency measures to ensure that shortfalls in external assistance do not lead to corresponding retrenchment in pro-poor spending.

29. **The authorities' proposal for the establishment of a PRSP fund to channel resources to the implementation of the strategy will need to be clarified.** Staffs recognize the limitations on channeling donor resources in the form of direct budgetary support. Nonetheless, programs funded by the budget and by donors should be more clearly integrated and monitored under a single framework. A notional PRSP fund, as in Uganda, could help strengthen this tracking mechanism. Staffs recommend against the establishment of additional extra-budgetary funds, outside of the budget process.

E. The Risks to the Strategy

30. **The PRSP recognizes that implementation of the PRSP is subject to substantial risks and cites three exogenous risk factors:** (i) vulnerability of the agricultural sector, and most of the poor in the sector, to drought and floods; (ii) vulnerability to fluctuations in oil prices; and (iii) increased reliance on volatile trends in external aid. As noted above, the PRSP, however, does not indicate what the policy responses would be in the case of adverse shocks and how poverty-related spending would be protected.

31. **Staffs believe that the achievement of the PRSP poverty targets is also subject to risks that are not identified in the PRSP, including (i) political and security risks** including civil unrest or domestic security threats, which would deter the flow of private (domestic and foreign) investment into Yemen and paralyze the tourism industry; **(ii) weak implementation capacity**, which would undermine the effectiveness of programs and point to the need to mobilize technical assistance from development partners; and **(iii) weak political commitment to the more difficult reforms that are needed to sustain fiscal adjustment and address governance issues** in a timely and consistent manner so as to

improve the efficient delivery of public services to the poor and provide an adequate business environment for private sector development.

V. CONCLUSIONS

32. **The Yemen PRSP provides a good framework for the country's efforts towards sustainable poverty reduction.** The strategy is a country-owned document and was prepared in a participatory manner through consultation with government line ministries, NGOs, civil society, elected officials, and donors. The strategy is coherent and has well defined and realistic poverty reduction targets, grounded in an ambitious but realistic and coherent macroeconomic framework aimed at maintaining internal and external stability. There are significant risks facing the implementation of the strategy, some of which are beyond government control. The successful implementation of the PRSP also requires filling several knowledge gaps, building the requisite capacity to implement and monitor the strategy, a more detailed action plan to address governance problems, and a strong commitment to reform generally.

33. The staffs of the World Bank and the IMF consider that the PRSP presents a credible poverty reduction strategy and provides a sound basis for Bank and Fund concessional assistance. The staffs recommend that the respective Executive Directors of the World Bank and the IMF reach the same conclusion.