Studies and Economic
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Policy Paper

The Parallel Market and the Yemeni Banking Sector:

A Struggle of Roles Amid Monetary Fragmentation and Multiple Exchange Rates

December 2025

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The Parallel Market and the Yemeni Banking Sector: A Struggle of Roles Amid Monetary Fragmentation and Multiple Exchange Rates

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Introduction:

Over the past decade, Yemen's banking and economic sectors have undergone two critical phases that marked deep turning points in their trajectory and had significant repercussions for the country's financial and economic future.

The first phase began with the outbreak of the armed conflict and the Houthi group's takeover of the capital, Sana'a, in late 2014, followed by the intervention of the Saudi-led Military Coalition. It continued until December 2019, when the Houthi group banned the circulation of new banknotes printed by the Central Bank of Yemen (CBY) under the IRG of Yemen in Aden, an act that ushered in the second phase.

Throughout these two phases, the economy experienced profound shifts that clearly affected financial and banking performance. However, the second phase proved to be the more critical and impactful one, as it produced a severe monetary division reflected in the existence of two exchange rates for the Yemeni Riyal, with a gap exceeding fivefold. This disparity negatively affected all economic, commercial, and financial sectors.

In both phases, the parallel (informal) market emerged as the biggest beneficiary. During the first phase, it exploited the banking sector's shock and the Yemen Central Bank's efforts to stabilize exchange rates amid a liquidity crisis. In the second phase, the monetary split and the dual decision-making between the CBY headquarters in Aden (after its relocation) and its branch in Sana'a created a fertile environment that enabled the parallel market to expand its activities and perform functions comparable to those of the formal banking sector, particularly in external transactions.

This policy paper focuses on analyzing this key component of the parallel market, namely, money exchange companies and establishments that operate without licenses or fail to comply with the legal and procedural regulations governing banking activity in Yemen, in addition to individuals or entities engaging in speculative currency trading.

Definition of the Parallel Market:

The parallel economy or shadow economy refers to all economic activities that are not officially registered, whether legitimate or illegitimate, and that operate outside the tax system.

In the Middle East and Asia, the shadow economy accounts for approximately 25–35% of GDP, compared with 14–16% in developed economies[1]. In some Arab countries, the rates are even higher: Egypt 40%, Morocco 30%, Jordan 20%, Syria 40%, Saudi Arabia 19.95%, Iraq 80%, and Algeria 30%[2].

Although there are no precise statistics for Yemen, it is expected that the share is quite large. Tax and customs evasion, along with the widespread non-registration of commercial activities, are much higher than in other Arab countries, mainly due to Yemen's poor performance on international transparency and integrity indicators.

The parallel currency market in Yemen is part of this informal economy and includes unlicensed or non-compliant money exchange companies, as well as currency speculators and war profiteers. It represents one of the most pressing economic challenges in a country heavily dependent on imports.

The Central Bank of Yemen (CBY) and the Financial Intelligence Unit (FIU) are responsible for overseeing the integrity of financial institutions. Although the 2008 assessment by the Financial Action Task Force (FATF) revealed deficiencies in Yemen's anti-money laundering and counter-terrorism financing measures, the country made subsequent progress. After relocating to Aden, CBY in Aden sought international advisory expertise to strengthen financial oversight mechanisms.

1- Medina, Leandro, and Friedrich Schneider. Shadow Economies Around the World: What Did We Learn Over the Last 20 Years?,International Monetary Fund, January 24.2018. https://www.imf.org/en/Publications/WP/Issues/2018/01/25/Shadow-Economies-Around-the-World-What-Did-We-Learn-Over-the-Last-20-Years-45583?utm_source=chtgpt.com

2- "The Black Market and Its Impact on the State." Democratic Arab Center, December 2022. https://democraticac.de/?p=86749

Background and Context:

The Houthi group's takeover of Sana'a and the outbreak of armed conflict in March 2015 led to a sharp deterioration across Yemen's macroeconomic indicators. According to a World Bank Group report (Spring 2016), Yemen's GDP contracted by 28% in 2015, inflation reached around 30%, and the fiscal deficit widened to 11.4% of GDP. Meanwhile, foreign reserves fell to below USD 2 billion, an amount covering only about two months of imports[3].

Amid this economic collapse, the Yemen Central Bank continued to manage monetary policy based on an undeclared understanding between the warring parties and with implicit support from certain international financial institutions. It kept paying salaries of public sector employees, both civilian and military, including the Ministry of Defense, and covered part of operational expenditures using available resources.

However, these resources gradually declined as a portion of public revenues began to leak outside the CBY's control. To finance the growing fiscal deficit, the CBY resorted to printing new banknotes amounting to 400 billion Yemeni Rials[4] and relied on approximately USD 4.7 billion in available foreign reserves to back those issuances. It used a currency substitution mechanism through direct intervention in the money exchange market selling foreign currency to meet importers' needs[5].

These policies, combined with other contributing factors, resulted in a notable increase in the volume of both local and foreign currencies circulating outside the formal banking system, while CBY's liquidity became severely depleted. This situation culminated in a serious liquidity crisis by mid-2016, undermining depositors' confidence in the banking sector.

The liquidity crunch created a fertile environment for the expansion of the parallel market, which began to perform functions similar to those of commercial banks and to extend its influence within the financial and banking sector. This was clearly reflected in the sharp rise in the number of money exchange outlets and companies, from 517 in 2011 to 565 in 2012, then 600 in 2014, and finally a dramatic increase to 1,350 by 2018, nearly 800 of which operated without official licenses from the Central Bank of Yemen[6].

3- "Financial Sector Diagnostic Report – Yemen." World Bank Group, December 2024. https://documents1.worldbank.org/curated/en/099102324070011985/pdf/P177631-d18a7ee4-3fcf-4393-9665-77f98b3e43a7.pdf

4- Economic and Social Developments Bulletin in Yemen: "Where Is the Yemeni Economy Heading?" Issue No. 30.

5- "Yemen Economic Monitoring Brief." World Bank, Fall 2018.

6- "The Parallel Market and the Role of the Central Bank in Regulating It." Public Policy Paper, Studies and Economic Media Center (SEMC), 2018.

Yemen Banking Sector's Two Critical Phases

Since that time, Yemen's banking sector has gone through two pivotal phases:

- **Phase One (2015–2019):**

This phase was marked by a severe liquidity crisis, the relocation of the Central Bank of Yemen (CBY) from Sana'a to Aden, the printing of new banknotes, and the closure of Yemeni banks' U.S. dollar accounts with correspondent banks. During this period, the parallel market strengthened its role and became the main source of import financing.

- **Phase Two (since December 2019 until now):**

It began when the Houthi group banned the circulation of banknotes printed by the CBY in Aden. This created a broader opportunity for the parallel market to expand and dominate the financial scene by exploiting monetary policy duality. Consequently, two exchange rates emerged, leading to a deep monetary and financial split and an unprecedented collapse in the value of Yemen's local currency.

Phase One: Expansion of Cash Outside Banks and the Rise of the Parallel Market

The moments when monetary authorities believe they can cover market shortages and maintain exchange rate stability are the ideal window of opportunity for the parallel market. In Yemen, this parallel market closely monitored the CBY's injection of foreign currency during 2015–2016, aiming to capture a large share of it, knowing that continued CBY intervention was unsustainable under wartime conditions, that the foreign currency supply was limited and non-renewable, and that its depletion would gradually lead to depreciation of the local currency.

Between 2015 and 2016, CBY intervened by selling foreign currency directly to support the exchange rate. In 2016 alone, it sold approximately USD 1.2 billion, at an average of USD 200 million per month, through what was known as the "substitution mechanism". This mechanism aimed to ensure the availability of essential commodities, such as wheat, milk, sugar, and medicines, by providing traders with foreign currency against official import documentation at the CBY exchange rate. However, the mechanism lacked strict oversight due to the ongoing conflict and weak control over land and seaport customs outlets.

The volume of currency in circulation outside the banking system grew sharply. CBY data indicates that this volume increased by YER 222 billion in 2015, reaching YER 298 billion in the first quarter of 2016[7], representing a 753% and 1,046% increase, respectively, compared to YER 26 billion in 2014. By 2016, cash outside banks had reached YER 1.34 trillion[8]. These factors, combined with the consequences of war, created fertile ground for the emergence of the parallel currency market as a major player in economic activity.

As the International Monetary Fund (IMF) explains, such a situation arises "when the states central banks are unable to meet demand at the official exchange rate," prompting the rise of a parallel market as an alternative[9].

7 - احمد الطيار، لجنة الخبراء الأكاديميين تشخ الوضع الاقتصادي والمالي، صحيفة الثورة العدد 18968، 25 أكتوبر 2016.

8- Central Bank of Yemen – Annual Report, December 2020.

9- International Monetary Fund (IMF). Official and Parallel Exchange Rates. IMF Special Series on COVID-19. Washington, DC: International Monetary Fund, 2020.

https://www.imf.org/-/media/Files/Publications/covid19-special-notes/en-special-series-on-covid-19-official-and-parallel-exchange-rates.ashx

Expansion of the Parallel Market at the Expense of the Formal Banking Sector

The liquidity crisis that struck the banking sector severely undermined the business community's confidence in commercial banks, leading to increased cash withdrawals and a flow of liquidity toward the parallel market. This occurred amid a shortage of foreign exchange resources and a decline in commercial banks' external balances, as a significant portion of external remittances, to Yemen, began flowing through informal channels.

Banks faced a double dilemma, meeting importers' foreign payment obligations abroad or accommodating massive cash withdrawals domestically, while CBY restricted withdrawals from their accounts due to the liquidity shortage.

In addition, the banking sector encountered further challenges after their U.S. dollar accounts were closed by correspondent banks following U.S. Treasury Department directives, which limited their ability to settle import payments in US dollars. Consequently, they were forced to rely on the euro, despite its higher transaction costs.

After CBY relocated its headquarters to Aden in September 2016, it began printing new banknotes to finance public spending and pay salaries. This move expanded the money supply, which reached YER 3.6 trillion[10].

Data also shows a remarkable growth in money exchange activity during that period. By 2023, the number of licensed individual money exchange outlets in Aden reached 332, in addition to 96 money exchange companies and 86 money transfer agents. Meanwhile, the number of licensed money exchange companies in Sana'a exceeded 170.

Between 2014 and 2023, this sector experienced substantial growth: the number of exchange companies in Sana'a increased from 179 to 415, and in Aden from 34 to 91, reflecting the expanding dominance of the parallel financial system in Yemen's fragile economy[11].

10- Central Bank of Yemen – Annual Report, December 2020.

11- World Bank Group. Financial Sector Diagnostic Report – Yemen. December 2024.

https://documents1.worldbank.org/curated/en/099102324070011985/pdf/P177631-d18a7ee4-3fcf-4393-9665-77f98b3e43a7.pdf

Roles of the Parallel Market

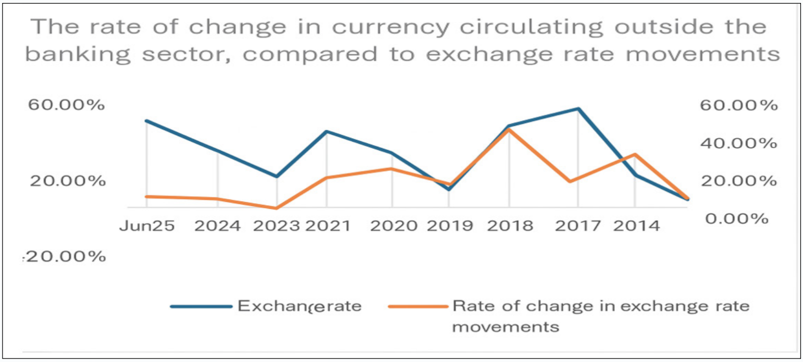
The parallel market has witnessed a significant expansion of its activities, exceeding the functions permitted under Law No. (19) of 1995[12], particularly Articles 21, 22, and 23, which prohibit exchange companies from performing banking functions such as commercial financial transfers, opening accounts, conducting credit and debit operations, or executing large-scale currency transactions.

Despite these legal restrictions, the parallel market has surpassed them and taken on multiple roles, summarized as follows:

1- Speculation and Currency Trading Outside the Formal Banking System

The volume of cash circulating outside the formal banking system doubled, reaching approximately YER 3.2 trillion by the end of December 2024[13], with most of it concentrated in exchange companies and outlets.

A World Bank report estimated the total assets of exchange companies at YER 1.4–2 trillion, while these money exchange companies



12- Law on Foreign Exchange Activities, Republican Decree No. (19) of 1995, Office of the Public Prosecutor, https://agoyemen.net/lib_details.php?id=18

13- Monetary and Financial Developments Bulletin, Central Bank of Yemen, December 2024.

hold 52% of all currency circulating in the banking sector[14]. Furthermore, the 2016 Expert Committee Report indicated that approximately YER 1.3 trillion (equivalent to USD 5.2 billion) was circulating outside domestic banks, an amount equal to 40% of Yemen's annual import bill[15].

2- Capturing Expatriate Remittances and Accumulating External Balances

The parallel market exploited the restrictions imposed in Saudi Arabia on remittances from expatriates and investors, particularly limitations on transferring large amounts directly.

As a result, the market provided informal channels for transferring funds, depriving the formal banking sector of these important financial inflows.

According to an ACAPS report (October 2021), expatriate remittances are a major source of foreign currency supply in Yemen. However, a large portion of these funds do not pass through banks and is instead handled by money exchange companies or informal money transfer networks[16].

3- Informal Trade and the Financing of Import Operations

By capturing a large share of remittances from expatriates, particularly in Saudi Riyals and U.S. dollars, the parallel market has been able to build up foreign balances that it uses to finance imports through covert networks and social-media-based channels, entirely outside any formal oversight or accounting records. These operations typically proceed through two main steps:

1. First Step:

An expatriate transfers an amount (for example, one million Saudi riyals) to a representative of a Yemeni exchange company in Saudi Arabia, on the condition that the company in Yemen pays the equiv-

14- Financial Sector Diagnostic Report for Yemen, World Bank Group, December 2024, https://documents1.worldbank.org/curated/en/099102324070011985/pdf/P177631-d18a7ee4-3fcf-4393-9665-77f98b3e43a7.pdf?utm_source=chatgpt.com

15- Ahmed Al-Tayyar, "The Committee of Experts Diagnoses the Country's Financial and Economic Situation," Al-Thawra Newspaper, previously cited reference.

16- ACAPS – The Impact of Remittances on Yemen's Economy, October 2021, https://www.acaps.org/fileadmin/Data_Product/Main_media/20211015_acaps_yemen_analysis_hub_impact_of_remittances_on_yemens_economy.pdf?utm_source=chatgpt.com alent amount to a beneficiary designated by the expatriate. Through this mechanism, the exchange company acquires an external foreign-currency balance.

2. Second Step:

The company uses this foreign balance to finance commercial operations, such as transferring USD 300,000 to China, against a local deposit in Yemeni Rials. The transfer is executed through a third party (e.g., a trader in Saudi Arabia or an external account).

The exchanger profits from exchange-rate margins and commissions, selling to the trader at a higher rate (3.85 SAR per USD) while purchasing US dollars at the official rate of CBY in Yemen (3.75 SAR per USD). The payment is then deposited into the supplier's or import agent's account in China, after which the goods are shipped to Yemen or via intermediary ports such as Dubai or Jeddah.

This mechanism is used daily for hundreds of transactions involving tens of millions of US dollars, enabling the parallel market to dominate the flow of external transfers and trade financing while accumulating liquidity and balances both inside and outside the country.

Interviews with employees of several exchange companies confirmed that electronic banking services in neighboring countries have facilitated these operations, allowing money exchangers to make direct transfers using front or proxy accounts belonging to traders in those countries.

Mechanism of Money Transfer Through the Parallel Market

1. An expatriate abroad wants to send a remittance to Yemen.

2. He contacts an agent/intermediary of the Yemeni exchange company abroad.

3. The agent receives the amount and coordinates with the exchange company in Yemen.

4. The exchange company in Yemen delivers the amount to the beneficiary at the parallel-market exchange rate.

5. The exchange company's agent deposits the amount into a commercial account belonging to a trader in the expatriate's country of residence.

6. The exchange company sends the invoice and details to the intermediary and receives confirmation of the transfer to the foreign supplier on behalf of the Yemeni trader.

As a result, the Yemen's formal banking sector incurred substantial losses, while cash circulation outside the banking system expanded significantly. This has constrained the effectiveness of monetary policy in managing liquidity and influencing overall macroeconomic stability. What is particularly striking is how countries such as China, India, and the United Arab Emirates accept exporting their products to Yemen through invoices and transfers issued in the name of non-Yemeni companies, despite the fact that these states possess advanced legislative, regulatory, and supervisory frameworks for combating money laundering and counter-terrorism financing.

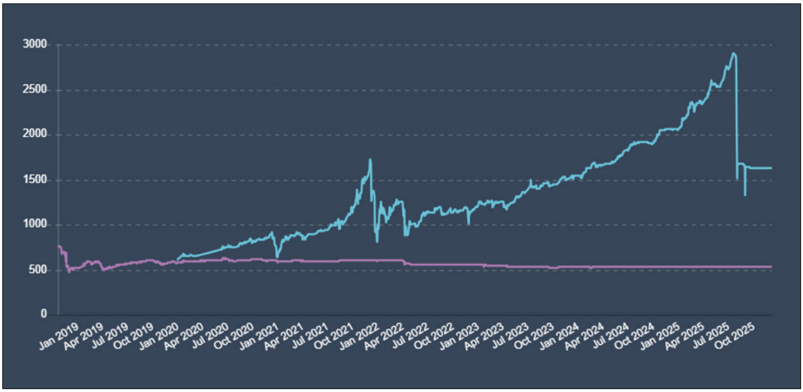
Second Phase: Monetary Fragmentation as a Fertile Environment for the Parallel Market

On December 19, 2019, the Central Bank in Sana'a, under Houthis control, issued a decision prohibiting the circulation or possession of newly printed banknotes issued by the Aden-CBY. The Sana'a-CBY justified this decision by claiming that the new banknotes caused severe harm to the national economy, and it required citizens to exchange them within thirty days for electronic currency or old-printed banknotes.

This decision constituted a shock to Yemen's monetary system and triggered consequences that continue to deepen over time. The most significant impacts include:[17]

1. Speculation and Liquidity Transfers

The parallel market contributed to aggravating the monetary imbalance through currency speculation, smuggling of funds, and transferring local and foreign liquidity between governorates. It capitalized on the exchange-rate gaps created by the dual monetary authorities in Sana'a and Aden, undermining the effectiveness of fiscal and monetary policies.



Yemen economic tracking initiative , https://yemen.yeti.acaps.org/xr-commodities/

Average exchange rate in Aden

Average exchange rate in Sana'a

17- https://saba.ye/ar/news3082111.htm

2. Creation of Dual Exchange Rates and the Use of Foreign Currency as an Intermediary

The decision led to the widespread use of the US dollar and the Saudi Riyal as intermediary currencies for daily transactions between northern and southern governorates, due to the wide value gap between the old and new printed banknotes of the Yemeni Rial (YER).

Although financial transfers between the two sides continued, the flow of funds leaned in favor of Sana'a, which has historically been the center of commercial activity, in addition to the Yemen government-held areas' reliance on agricultural and food products originating from Houthi-controlled areas.

This situation placed heavy pressure on the demand for foreign currencies and resulted in the creation of two exchange rates for the Yemeni Rial, with the gap widening to nearly sixfold.

3. Trade Between the Two Sides Resembling Trade Between Two Countries

The Houthi authorities treated the areas under their control as if they were an independent state, such that purchasing goods from these areas became similar to importing from abroad. Key goods sold to government-held regions include:

- Imported goods arriving through Hodeida Seaport and re-distributed to government areas
- Products from food, pharmaceutical, and beverage factories within Houthi-controlled zones
- Agricultural products such as fruits, vegetables, and qat
- Telecommunications and internet services, which generate substantial revenue and are paid for in newly printed banknotes before being converted into foreign currency

This large volume of trade conducted using the US dollar and the Saudi Riyal created a vibrant and permanent market for the parallel exchange system.

4. Money Laundering and Terrorism Financing

The parallel market created an enabling environment for money laundering and illicit financing during the war. Its methods have included:

- Transferring funds domestically and internationally without documentation or justification
- Moving funds of unknown origin through seemingly legitimate channels
- Opening accounts for war profiteers and individuals involved in corruption
- Purchasing assets and real estate using unidentified sources of money
- Fake import operations and smuggling funds abroad
- Cryptocurrency trading to obscure the origin of funds
- Draining foreign currency by receiving remittances outside formal financial channels

5. Establishment of Unregulated Transfer Networks

Unsupervised individual remittance and exchange networks emerged, operating entirely outside the formal regulatory framework and running flexible, concealed financial systems that disrupt monetary policy. These networks are concentrated largely in Sana'a, where they attract large volumes of Yemeni and foreign currencies and create parallel pricing between cash and electronic balances.

According to a World Bank report, 71% of communities rely on informal exchange outlets, while 64% use the Hawala system as their primary method for transferring money rather than banks.[18]

Media reports have also highlighted billions of Yemeni Rials and millions in foreign currencies stuck within these networks as unclaimed remittances. One network alone reportedly holds more than 60,000 uncollected transfers, including nearly 2 billion Yemeni Rials and over 6 million Saudi riyals.[19]

18. World Bank Group. Financial Sector Diagnostic Report for Yemen. December 2024.
https://documents1.worldbank.org/curated/en/099102324070011985/pdf/P177631-d18a7ee4-3fcf-4393-9665-77f98b3e43a7.pdf

19. Al Jazeera. "Forgotten Transfers Worth Billions of Rials." Shabakat Program, February 2023.
https://www.aljazeera.net/

Roles of the Central Bank of Yemen and the Parallel Market

Since relocating the headquarters of the Central Bank of Yemen to Aden under Republican Decree No. 119 of 2016, the Aden-CBY has adopted a series of policies and measures aimed at addressing the monetary and financial crisis and limiting the expansion of the parallel market, which has been exacerbated by political and economic fragmentation. The most notable of these policies can be summarized as follows:

• Cash Liquidity Management

Immediately after its relocation, the Aden-CBY resorted to printing and issuing new banknotes to cover liquidity shortfalls and finance public sector salaries. According to the Aden-CBY reports, the volume of currency issued reached YER 1.7 trillion from September 2016 to December 2019, rising to YER 3.6 trillion by December 2024.[20]

In December 2021, following a change in its Board of Directors[21], Aden-CBY decided to halt deficit financing through currency issuance and to cover expenditures through limited exports of oil derivatives in coordination with the IRG of Yemen.

• Foreign Currency Auctions

The Aden-CBY introduced an electronic auction mechanism via the Refinitiv platform, utilizing its reserves from foreign aid and grants, alongside cash deposits from allay countries (notably Saudi Arabia) and Special Drawing Rights from the IMF. By the end of 2024, the value of bids purchased by commercial banks reached approximately

20. Central Bank of Yemen. Monetary and Financial Developments Bulletin. December 2024. https://cby-ye.com/files/67bebcccb000e.pdf
21. Saba News Agency. "Presidential Decree No. 14 of 2021 on Forming a New Board of Directors for the Central Bank of Yemen." December 2021. https://www.sabanew.net/viewstory/81751

USD 2 billion out of USD 3 billion offered, representing 69.7%, to cover essential needs such as food and medicine.[22]

During the first half of 2025, the value of executed auctions amounted to USD 209.8 million from total bids of USD 460 million.[23]

• Regulation of Money Exchange Companies

The Aden-CBY worked to regulate the sector by issuing updated regulations and manuals, raising capital requirements as follows: YER 1 billion for partnership exchange companies, YER 500 million for individual money exchange outlets, and YER 100 million for remittance agents.[24] It also intensified inspections and field oversight, launched training programs to support regulatory compliance, and issued repeated circulars to control exchange activities and mitigate associated risks.

• Establishment of a Unified Remittance Network

Under Decree No. 18 of 2020, the Aden-CBY established the Unified Remittance Network (UNMONEY)[25], which was officially activated in February 2024 with an initial capital of YER 5 billion. In June 2024, Decree No. 23 halted the operations of other bank and exchange company networks, limiting all domestic remittances to the unified network to curb financial speculation and strengthen oversight. The Aden-CBY encouraged banks relocated to Aden to contribute to the network, increasing its capital to YER 12 billion[26], granting them a central role in its management and development as a primary payment platform.

22. Central Bank of Yemen. Monetary and Financial Developments Bulletin. June 2024. https://english.cby-ye.com/files/66fcee194c1df.pdf
23. Central Bank of Yemen. "Foreign Currency Auction Results." June 2025. https://cby-ye.com/auctions?page=3
24. Central Bank of Yemen. "Decision No. 58 of 2022 on Regulating Money Exchange Activities." August 2022. https://cby-ye.com/files/62ed43decda74.pdf
25. Central Bank of Yemen. "Decision No. 18 of 2020." https://cby-ye.com/news/58
26. Central Bank of Yemen. "Official Statement." July 2025. https://cby-ye.com/news/826

• Raising Capital of Banks and Microfinance Institutions

As part of its efforts to enhance financial inclusion, the Aden-CBY granted new licenses to microfinance banks and gradually raised their capital from YER 5 billion under Decree 11-2-2022 to YER 15 billion under Decree 3/2023, requiring them to pay 50% annually over two years.[27] It also prohibited combining exchange activities with microfinance operations, although in practice the overlap continued. In this context, the Aden-CBY issued Decree No. 8/2022, raising the minimum capital of operating banks in Yemen to YER 45 billion[28], and Decree No. 9/2022, increasing the legal reserve ratio of annual profits to 25%.

Pressure on Banks to Relocate Their Headquarters or Operational Centers

The Aden-CBY issued Decision No. (17) of 2024, stipulating that all commercial banks, Islamic banks, and microfinance banks operating in Yemen must relocate their headquarters from Sana'a to, Aden. The decision granted a 60-day deadline for banks to comply and transfer their headquarters/operational centers. Any institution failing to relocate within the specified period would be subject to "legal measures" under the Anti–Money Laundering and Counter-Terrorism Financing Law.[29]

However, the decision was not implemented immediately. Banks were subjected to significant pressure from the Sana'a branch of the Central Bank, which is under the control of the Houthis, leading to confusion among banks and affecting their relationships with foreign correspondent banks. These correspondent banks follow the directives of Aden-CBY, which requested proof of relocation from financial institutions wishing to continue operating their international transactions.

27. Central Bank of Yemen. "Decision No. 3 of 2023 on Increasing Minimum Capital Requirements for Microfinance Banks." December 2023.
https://cby-ye.com/files/659aa2ee5852b.pdf
28. Central Bank of Yemen. "Decision No. 8 of 2022 on Increasing Minimum Capital Requirements for Commercial Banks." March 2022.
https://cby-ye.com/files/623ad7ce6d172.pdf
29- https://cby-ye.com/news/658?utm_source=chatgpt.com

Impacts of the Parallel Market

The parallel market in Yemen is a manifestation of the ongoing war, the collapse of state institutions, lack of transparency, and political division. It is a key factor behind the current economic and livelihood deterioration. If left unchecked, it is likely to exacerbate the crisis. Its main effects include:

- The parallel currency market causes severe exchange rate fluctuations and weakens the Yemeni Rial against foreign currencies.
- The gap between exchange rates in Aden and Sana'a threatens the banking system.
- Difficulty in managing foreign currency reserves.
- Currency smuggling abroad, leading to a severe shortage of foreign cash within the country.
- Rising import costs due to exchange rate deterioration, contributing to sharp inflation, which exceeded 30% in 2024.
- Prices of essential goods such as food, fuel, and medicine increase significantly because traders rely on the parallel market to access foreign currency.
- Households' ability to meet basic needs declines, poverty rises, and inflation continues to surge.

Existing Policies

The Houthi group has economically isolated its areas of control and reduced commodity exchanges from IRG of Yemen's areas by imposing additional customs fees. It relies on efficiently collecting revenues and various levies to finance its operations, suspended salary payments (the largest component of public spending), and circulated only old banknotes. It also controlled most incoming foreign currency remittances to fund imports, while imposing strict oversight over the parallel market and fixing the exchange rate. This approach stabilized exchange rates on the surface but caused a contraction in economic activity.

Meanwhile, the IRG of Yemen continued its commodity exchange with Houthi-controlled areas without imposing any measures to reduce demand, relying instead on limited public revenues that were collected with low efficiency. It resumed re-exporting petroleum derivatives before the 2022 Houthi attacks on the export facilities, while continuing to pay salaries as the largest component of public expenditure. The government financed its deficit through new monetary issuance, revenues from petroleum derivative exports, and by using a significant portion of incoming remittances as a monetary cover to facilitate import operations. It also maintained a floating exchange rate with weak oversight of the parallel market.

This situation contributed to the deterioration of the exchange rate, rising inflation, and the expansion of parallel market activity. Recently, the IRG of Yemen implemented new measures and policies aimed at stopping the depreciation of the local currency, regulating the exchange market, and attempting to address structural economic distortions through the adoption of a comprehensive economic reform plan.

Policies Implemented in 2025

The year 2025 witnessed the implementation of a wide package of monetary and regulatory measures by the Central Bank of Yemen (CBY) in Aden under the IRG of Yemen, as part of efforts to contain the depreciation of the local currency, enhance the management of the monetary base, and reorganize the exchange market, after the exchange rate of the Yemeni Rial had reached 3,000 YER per USD. These measures focused on the following areas:

• Tightening Oversight of Liquidity Movements and Regulating Exchange Operations

The Aden-CBY adopted strict supervisory measures over liquidity flows and conversions between foreign currencies and the Yemeni Rial. This included activating tools for both direct and indirect oversight of the financial systems operated by money exchange companies. These measures aimed to curb speculation and improve transparency in financial operations across the banking and exchange sectors.

• Restructuring the Exchange Sector lthrough License Revocations

Aden-CBY issued several decisions revoking the licenses of a number of exchange companies and establishments that violated regulations governing financial activities, particularly those found to be engaged in currency speculation or in breaching operational ceilings and professional standards set by the Aden-CBY. This contributed to reducing the number of non-compliant actors in the market and reinforcing regulatory discipline[30].

• Relocation of the Banking Sector

Following the 2024 decision requiring banks to relocate to Aden, the U.S. Department of the Treasury imposed sanctions in January 2025 on two Yemeni banks, in addition to several exchange companies and commercial firms. At the same time, the Houthi group was of-

30- https://cby-ye.com/news/854

ficially added to the U.S. list of terrorist-supporting organizations.

These developments led all major banks and leading exchange companies to leave Sana'a and transfer their headquarters to the Yemen's interim capital, Aden, making the Yemeni banking sector fully operational from Aden, according to the Governor of Aden-CBY.

• Benefiting from International Technical Assistance

The Aden-CBY strengthened its institutional capacity by benefiting from technical support and consultations provided by international financial institutions, including the World Bank and the International Monetary Fund, along with donor countries engaged in Yemen's economic file. This support included training administrative staff and revising regulatory and procedural manuals such as compliance guides and anti-money laundering and counter-terrorism financing (AML/CFT) standards.

• Enhancing Foreign Currency Management through Relocating Banking Operations to Aden

Relocating the main operational and administrative centers of banks to Aden enabled the CBY to manage foreign currency inflows more effectively, particularly remittances coming from abroad. This measure ensured stronger central supervision and reduced distortions arising from the previous dual monetary authority.

• The Economic Reform Plan

In October 2025[31], the Yemen's Presidential Leadership Council (PLC) issued Decision No. 11 of 2025, approving an economic reform plan aimed at restoring financial and monetary stability and improving overall economic performance through a coordinated set of policies.

The plan focuses on strengthening government revenues, rationalizing public expenditure, stabilizing the exchange rate, and developing the banking sector.

It also seeks to improve the business environment, combat corruption, and diversify income sources by supporting productive sectors

31- https://ydn.news/?p=101603

such as agriculture, industry, and energy. The plan includes measures to unify state revenues, reform customs and tax systems, enhance the efficiency of public services, and empower the private sector to contribute to economic growth.

Problem Description

The monetary, financial, and institutional division, along with fragmented public revenues among parties, has weakened the economy, created space for the parallel market, deepened inflation, and caused local currency collapse. The situation has been worsened by the systematic use of available resources to harm the opposing party without regard to societal or public interests.

The parallel market in Yemen poses a clear threat to Yemen's national economic stability, controlling a significant portion of economic and financial activity through trade, imports, and currency circulation via informal channels. Its expansion has caused distortions in the economic structure and directly affected macroeconomic indicators, including trade balance stability, foreign currency flows, and local currency value under speculation.

Despite the noticeable improvement in exchange-rate stability resulting from the measures taken, foremost among them the establishment of the National Committee for Regulating Imports, which introduced a clear mechanism for buying and selling foreign currency and organizing the flow of imports through various customs entry points, along with the adoption of an economic reform plan, the resurgence of parallel-market activity continues to pose a threat to both the monetary and economic systems.

This threat becomes even greater in the event of any intervention by the Houthi group or in the case of political or military unrest in areas controlled by the internationally recognized government. Therefore, it is essential to examine appropriate options and alternatives for dealing with these risks, in addition to formulating effective and sustainable recommendations to mitigate their negative impacts in the future.

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31 - الموقع الالكتروني ليمن ديلي، موقع اخباري يمني، https://ydn.news/?p=101603

Options and Solutions

Option 1:

Foreign Exchange Trading Platform (FX Trading Platform)

Following the relocation of local banks to the Yemen's temporary capital, Aden, the Aden-CBY gained more options to implement new monetary policies capable of influencing the financial system once the banking system is fully operational. One of these options is the creation of a centralized foreign exchange trading platform, either by establishing a new platform or upgrading the existing Refinitiv platform for public US dollar auctions.

Platform Concept:

The platform would facilitate the buying and selling of foreign currencies through a closed electronic system including local banks, major exchange companies, the Aden-CBY, importers, exporters, and traders. The platform would be supported by Aden CBY and supervised technically by reputable global firms selected by Aden-CBY.

Objectives of the Platform:

1. Reduce reliance on the parallel market and narrow the gap between actual supply and demand.
2. Consolidate bids and offers among banks, major exchange companies, importers, and exporters.
3. Enable partial and flexible exchange rate liberalization.
4. Utilize foreign aid and remittances, integrating them into supply and demand.
5. Increase transparency by setting a reference rate based on the daily average of bids.

Platform Functions:

- Buying and selling foreign currency to/from banks, exchange companies, importers, and exporters.
- Receiving remittances from abroad, automatically converting them into local currency, and linking them to a local electronic payment system that could be established by the Unified Remittance Network.
- Allocating foreign currency to priority sectors (medicine, food, oil derivatives, etc.).
- Potential integration with other payment systems, such as the Unified Remittance Network.

Key Success Factors:

- Adoption of a managed float or semi-fixed exchange rate based on realistic assessments of supply, demand, and market needs.
- Adequate foreign reserves for Aden-CBY intervention during the platform's initial phase.
- Transparency and accountability through an oversight committee and periodic reporting.
- Issuing a platform regulation, including anti-money laundering and counter-terrorism financing rules.
- Secure and transparent electronic system, supported by trained personnel specialized in risk management.
- Structural reforms to address weak export volumes and low public revenue, reducing reliance on inflationary financing sources.
- Automated, secure settlement system among banks, exchange companies, and the Central Bank.

Stakeholder Roles:

Stakeholder	Main Role
Expatriates	Sending foreign currency remittances from abroad
Correspondent Banks (Foreign (Accounts	Receiving remittances and recording them in accounts under the platform or Aden-CBY
Central Platform	Recording balances in virtual accounts for banks and exchange companies; managing buy/sell orders
Local Banks	Entering buy/sell orders, using balances to meet client needs
Transfer Companies / Digital Wallets	Receiving expatriate remittances and crediting them within the platform for beneficiaries
Importers & Traders	Purchasing foreign currency through the platform to pay for imports
Central Bank of Yemen	Supervising the platform, controlling liquidity, ensuring external balances match records
Parallel Market	Gradually shrinks as the platform expands and transparency improves

Additional Measures to Enhance Effectiveness:

- Strict oversight of speculators, with limited trading margins for compliant banks and exchange companies.
- Direct linkage with compliant exchange companies and monitoring large positions.
- Elimination of dual ownership or circumvention between exchange companies and microfinance banks.
- Surprise inspections and graduated fines for violators.
- Increasing public revenue and reducing expenditures.
- Reducing budget deficits.
- Integrating customs and port authorities in import monitoring.
- Disbursing salaries and other government payments through bank wallets to ensure fair distribution.
- Establishing an electronic portal for public revenue collection.

Option 2:

Unified Foreign Exchange Management Account

This option involves linking the Yemeni Rial to the US dollar and Saudi Riyal and managing a central portfolio of these currencies across local banks, exchange companies, and official entities to fund importers based on local market priorities. All incoming remittances would be routed through a unified Central Bank account, allowing the bank to monitor inflows and coordinate their management with local banks using a clear mechanism.

Components of the Unified Account:

1. Cash flows via banks and exchange companies.
2. Humanitarian aid from UN and non-UN organizations.
3. Foreign government grants and aid.
4. Export revenues and contributions from friendly countries to the government.

Operational Mechanism:

Unified accounts are established at the Aden-CBY with local banks receiving foreign remittances, either via their own wallets or foreign companies, to record them in this account under direct supervision. The Aden-CBY authorizes banks to convert remittances to Yemeni Rial at a designated rate and use foreign balances to cover importers' obligations according to a mechanism defined by the Aden-CBY.

Objectives:

- Strengthen foreign reserves and reduce the trade deficit.
- Support exchange rate stability and limit speculation outside the formal sector.
- Control supply and demand for foreign currency and avoid artificial demand.
- Support monetary and economic policies with accurate data on cash flows.
- Control inflation by managing exchange rate effects on imported goods.
- Reduce the parallel market and informal trading.

Success Factors:

- Government, security, and judicial support to control the parallel market.
- Setting a balanced exchange rate based on accurate supply and demand data.
- Monitoring imports and ports to ensure goods enter local markets.
- Integrated fiscal policies with monetary policies to maximize revenues, reduce expenditures, and curb corruption through electronic wallets.
- Reducing budget deficits, improving revenue collection (especially customs), and stopping inflationary financing.
- Reducing cash circulation, promoting electronic payments, and decreasing currency outside banks.

Experiences from Other Countries:

Country	Experience	Black Market	Outcome
India	Transparent FX-Retail platform	Nearly eliminated	Successful
Philippines	Linking remittances to digital platforms	Weak	Successful
Malaysia	Banking platform post-1997 crisis	Weak	Successful
Brazil	Official system mandatory	Limited	Moderate
Argentina	Official auctions	Strong	Failed
Mexico	Auctions + smart interventions	Nearly eliminated	Successful
Pakistan	PRI	Weak	Successful
Ethiopia	Ethiopian Electronic Forex Trading System	Very strong	Failed
Nigeria	Nigerian Autonomous Foreign Exchange Market (NAFEM)	Strong	Failed
South Sudan	Central Bank FX Window	Medium-Strong	Moderate
Egypt	Previous Central Bank auctions	Medium	Moderate
Zimbabwe	Multi-exchange rates system	Very strong	Failed
South Africa	SAMOS + Johannesburg Stock Exchange	Nearly eliminated	Successful
Indonesia	BIRS	Limited	Successful
	Indonesia		

successful experiences were coupled with regulatory measures and structural economic reforms, particularly enhancing transparency, combating corruption, and addressing tax evasion.

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The Studies and Economic Media Center (SEMC) is a leading Yemeni civil society organization dedicated to promoting economic awareness, transparency, and good governance. It actively encourages citizen participation in decision-making processes and advocates for the development of a professional and responsible media landscape in Yemen.

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