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August 6, 1981

To: Members of the Executive Board

From: The Secretary

Subject. Yemen Arab Republic - Staff Report for the 1981 Article IV Consultation

Attached for consideration by the Executive Directors is the staff report for the 1981 Article IV consultation with the Yemen Arab Republic. A draft decision appears on page 12.

This subject has been tentatively scheduled for discussion on Wednesday, September 9, 1981.

Att: (1)

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Department Heads

INTERNATIONAL MONETARY FUND

YEMEN ARAB REPUBLIC

Staff Report for the 1981 Article IV Consultation

Prepared by the Staff Representatives for the
1981 Consultation with the Yemen Arab Republic

Approved by A.K. El Selehdar and Subimal Mookerjee

August 5, 1981

I. Introduction

The 1981 Article IV consultation discussions with the Yemen Arab Republic (Y.A.R.) were held in Sana'a during the period June 6-10, 1981. 1/ The Y.A.R. representatives were led by the Deputy Prime Minister for Financial and Economic Affairs, and included the Ministers of Finance, Development, Economy and Industry, Agriculture, Electricity and Water, the Governor of the Central Bank, and other senior officials. The staff mission comprised Messrs. A.K. El Selehdar (Head), G.T. Abed, M. Hosny, S. Ishii, B.K. Short (all of MED), and Mrs. A.L. Yates (Secretary - MED). The discussions were attended by the six experts assigned to the Y.A.R. under the technical assistance programs of the Fiscal Affairs and the Central Banking Departments. The mission also met with the Vice President of the Republic and with the Prime Minister.

II. Background

Since the early 1970s, the Y.A R. economy has undergone substantial structural changes, reflected in a rapid rise in incomes from relatively low levels, the construction of basic infrastructural facilities, the establishment of social and economic institutions, and the diversification of economic activity from a narrow agricultural base. During this period, the Y.A.R.'s domestic resources were augmented by sizable inflows of workers' remittances and by sustained external assistance from bilateral and multilateral sources. The availability of these additional resources made possible relatively high rates of growth of consumption and investment while, at the same time, allowing for a steady accumulation of considerable national savings in the form of external reserves.

1/ The Y.A.R. continues to avail itself of the transitional arrangements of Article XIV.

Real growth in the four years ended in 1979/80 (the first four years of the First Development Plan) 1/ averaged 6.3 per cent per annum, with higher growth rates recorded in the earlier part of this period. Although the growth of the dominant agricultural sector was sluggish, primarily because of the loss of farm labor but also because of unfavorable weather conditions, the construction, industry, and services sectors remained buoyant throughout most of the period. Gross fixed investment rose steadily from 17 per cent of real GDP in 1975/76 to 44 per cent in 1978/79 before declining marginally in the following year. Consumption expenditures also rose steadily and total spending exceeded GDP by a wide margin. Beginning in 1978/79, the pace of economic activity appears to have subsided as remittance inflows stabilized, contributing to a slowdown in the most immediately affected sectors of private construction, trade, and other services.

Government finances showed considerable strength throughout the early and mid-1970s as government revenues rose rapidly while institutional and supply bottlenecks, especially in the early period, helped restrain the growth of government spending. However, beginning in 1978/79 the growth of budgetary revenues slowed while expenditures continued to rise strongly. The slowdown in the growth of revenues reflected mainly a leveling off of import duties (which account for the bulk of budget receipts) as import growth decelerated and the share of unrecorded overland imports increased. As a result, the overall budget deficit widened sharply from an annual average of just over YRls 0 3 billion in the three years ended in 1977/78 to about YRls 2.3 billion in each of the following two years equivalent to 19 per cent of GDP in the latter year. Moreover, as nondefense-related external assistance did not increase much during the period, the government net cash position with the banking system swung from a surplus to a deficit for the first time in 1978/79. The bank financed deficit widened to 15 per cent of GDP in 1979/80.

Monetary developments in recent years have mirrored the effects of the shift in the relative contributions of the external sector and the Government to the growth of domestic liquidity. Until 1977/78 the primary impetus to liquidity expansion was the rapid increase of net foreign assets while the Government steadily improved its cash position with the banking system Beginning in 1978/79, the impact of external sector operations ceased to be highly expansionary and in 1979/80 it turned contractionary for the first time in many years At the same time, government borrowing from the banking system, which was moderate in 1978/79, has become highly expansionary since 1979/80. Private sector credit, which grew strongly in the mid-1970s, has slowed considerably since 1976/77 and has fluctuated around a moderately declining trend since then. The countervailing effects on money growth of the external and government sectors, coupled with the restrained impact of private sector operations in recent years, helped reduce the overall growth of money supply from an average of about 75 per cent per year in the three years ended in 1977/78 to an annual average of

1/ Fiscal years ended June 30; the First Plan was scheduled to end on June 30, 1981 but has been extended to the end of 1981.

about 15 per cent in the subsequent two and one-half years. The impact on domestic price movements of even the relatively high rates of growth of liquidity in the mid-1970s was moderate due to rapid monetization of the economy and the concomitant rise in cash balances held by the public, the domestic inflation rate steadily declined to 11 per cent in 1979/80. In view of the slowdown in economic activity and the easing of labor market pressures in the more recent period, the inflation rate appears to have declined even further since then.

Throughout the mid-1970s, the rapid growth of inward remittances and the steady increases in external aid receipts underlined a strengthening balance of payments position in the Y.A.R. In the three years ended in 1977/78 the annual current account surplus averaged over US$250 million (about 17 per cent of GDP) and the overall balance over US$360 million (about 25 per cent of GDP). However, as remittance inflows stabilized and official aid receipts grew only marginally, deficits were recorded on the current account beginning in 1978/79 and on the overall position beginning in 1979/80. The slowdown in the growth of remittances reflected the decline in emigration of Yemeni workers to the neighboring countries in part because of narrowed wage differentials. Imports on the other hand continued to grow strongly in light of the expanding demand for both development and consumption goods and services. The weakening trend in the balance of payments has continued since then and the overall balance of payments deficit widened in the second half of 1980 and in the first quarter of 1981 By the end of 1980, reserves had fallen to US$1.3 billion, equivalent to about nine months of imports, and continued to decline through the early months of 1981 The Y.A.R.'s public external debt remains relatively small and debt service payments represent less than 2 per cent of current external receipts.

The Y A R continues to follow liberal trade policies and does not maintain any restrictions on the making of payments and transfers for current or capital international transactions. Since February 1973 the Yemen rial has been pegged to the U.S. dollar at the rate of US$1 = YRls 4.50. In the year ended June 30, 1981, the import-weighted exchange rate for the rial appreciated by 8.7 per cent.

III. Report on the Discussions

The discussions focused on the causes of the recent deterioration in the fiscal and external payments positions and on the measures that would be needed to ensure that the momentum of the development effort would be maintained in a framework of financial stability.

1. Development policies

The focus of the First Five-Year Development Plan (1976/77-1980/81) was on the development of the physical and economic infrastructure and on the establishment of institutions to provide essential goods and services. Nearly one third of total investment allocations was directed to the distribution sectors and about one quarter to the development of housing, health, and educational services. The commodity producing sectors received just over one third of the total. Detailed data on actual Plan implementation are available only for the first four years of the Plan and these indicate that the overall implementation ratio, which was close to 100 per cent in the first two years, declined in subsequent years but that high implementation rates were achieved in such key sectors as construction, housing, and health services. The overall growth rate for the four-year period ended in 1979/80 fell short of the 8.0 per cent target. The authorities stated that the decline in the implementation rates reflected delays caused primarily by shortages of managerial and skilled manpower and by supply bottlenecks which affected the distribution of development inputs. Studies were already under way in preparation for the Second Plan, which is to begin in 1982, and these studies have already benefited from the experience of the First Plan. The authorities indicated that although emphasis would continue to be placed on the further development of infrastructural facilities, greater attention was being given to the accelerated development of human resources, the agricultural and industrial sectors, and the country's mineral resources.

The structural changes that have characterized recent economic developments in the Y.A R. have been reflected in relatively high rates of growth in the nontraditional sectors of mining, manufacturing, electricity and water, construction, and financial services. Although the growth of agricultural output was negative in the first two years of the Plan period, increased investments and improved production and distribution methods as well as more favorable weather conditions helped restore growth in agricultural output in the subsequent period. The authorities indicated that prospects for higher growth rates in agriculture were good as the impact of improved infrastructure, especially for the control and use of water resources, better terms of trade for agricultural products, and the easing of labor constraints begin to take effect. They added that other than providing farmers with low cost credit, improved seed varieties, and technical assistance, the Government did not interfere with the pricing of inputs or outputs in agriculture and that this policy would continue

As regards industry, the authorities expressed satisfaction with progress made in this sector whose share in real GDP rose steadily to 6 6 per cent in 1979/80 A noteworthy development in this regard has been the growth of private sector investment in industry, encouraged by Public Investment Law No 18 of 1975 which provided for exemptions from import duties on capital goods and, partially, on raw materials, for income tax holidays, and for complete freedom of repatriation of profits These policies have also stimulated direct foreign investment, especially from the neighboring surplus countries. Most industrial goods production was intended as import substitutes but industrial exports have begun to show encouraging signs of growth. The authorities added that industrial pricing policies would continue to be conducive to the efficient allocaation of resources. Industrial projects in the public sector (mainly basic industries) must pass careful economic evaluation to ensure viability and the policy of refraining from providing direct subsidies to industry would be maintained. In this connection energy prices have been adjusted in accordance with rising acquisition costs and the added financial burden has been largely passed through to the users. This policy was expected to continue. Concerning other sectors of the economy there were indications of some slowdown in economic activity in 1979/80 and in the subsequent period, especially in construction and financial and other private services. The authorities attributed this slowdown to the stagnation in private remittances, which had financed much of the private spending in these sectors, and to high interest rates which had depressed private sector loan demand. They projected an overall real growth rate of GDP of about 5 per cent for 1981.

Accompanying the slowdown in activity in the Y.A.R. has been a considerable easing of domestic inflationary pressures. In 1979/80 the rate of inflation as measured by the consumer price index declined by one half from the preceding year to 10.6 per cent, and as measured by the implicit GDP deflator by one third to 10.9 per cent. The authorities projected the increase in the domestic price level in 1981 at 3.0 per cent on the basis of movements in the consumer price index during the last quarter of 1980. The authorities attributed the expected rapid decline in the rate of domestic price inflation to the moderating impact of the strengthening of the U.S. dollar on the cost of imports, the elimination of supply bottlenecks, and weakened demand in general. The mission pointed out however that the larger government deficits in prospect and the apparent recent rise in emigration of workers could rekindle inflationary pressures and that developments in domestic prices continued to merit close watch.

2. Fiscal policies

A major development in the fiscal structure in the recent period has been the sharp deterioration in the government accounts. Although the staff noted the small improvement in government finances in 1979/80, they expressed their concern regarding the continued surge in government spending, which had more than doubled its ratio to GDP in the five years ended in 1979/80 (from 20 per cent to 42 per cent), especially in the face of slower growth of revenues in 1978/79 and 1979/80. As external financing had returned to its historic levels from a temporary peak in 1978/79, the bank financed deficit had also risen sharply. The mission emphasized that this deficit had been the primary factor in the growth of domestic liquidity which, in an open economy with a small production base as that of the Y.A.R., had contributed to the growth of demand for imports causing a rapid deterioration in the balance of payments. Although the domestic price impact of the large deficits had remained small, the weakened external position, as reflected in the rapid loss of reserves, was a source of concern.

The Yemeni representatives agreed with the overall assessment of the mission and explained that the disappointing fiscal performance in recent years was due, at least in part, to the difficult political situation in the region. They added that the slowdown in economic activity in some sectors of the economy and continued inadequacy of the institutional and administrative machinery for tax collection had depressed the growth rates of government revenues. Meanwhile, it had been difficult to curtail further the growth of government expenditures as these were needed to finance basic facilities and services, especially in the rural areas of the country. The authorities expected that in the future improved performance on both the revenue and expenditure sides would help reduce the overall budget deficit in relation to GDP, while an expected increase in external aid receipts, virtually all in the form of concessionary loans and grants, would help reduce the Government's reliance on the domestic banking system for financing the deficit

Concerning recent trends in budgetary revenues, the mission noted with satisfaction the recovery of both tax and nontax receipts in 1979/80 from the depressed rates of growth recorded in the preceding year. Nevertheless, the growth of import duties, the single most important source of government receipts, has slowed in recent years and has lagged behind the growth of imports The Yemeni authorities cited several factors that had contributed to the erosion of revenue growth from this source. In the first place, the two fiscal years 1978/79 and 1979/80 witnessed a marked increase in the volume of investment and food imports, which are largely exempt from import duties. Secondly, many rates in the tariff schedule were specific (e.g., on petroleum products) and therefore did not respond to rising import values Thirdly, the early dramatic gains in customs administration began to reach diminishing returns in subsequent years as the volume of imports expanded much faster than the administrative capacity of the tax collecting units Finally, despite recent improvements in administration at land border posts, unrecorded and underrecorded imports through these points continued to be substantial. The authorities stated that measures had been taken or were under way to establish more effective administrative control over imports entering through overland routes. Administrative staff has been increased, new border posts opened, and a temporary 7 per cent surcharge has been imposed on unlicensed overland imports They expected these measures to have a positive effect on revenues later in 1981

Revised budget estimates for 1981 indicated growth of 28 per cent in revenues and 30 per cent in expenditures over the estimated 1980 figures, and a 32 per cent increase in the overall deficit to YRls 3.5 billion, equivalent to about 28 per cent of estimated GDP. 1/ As external financing

1/ GDP for 1980 was projected from the 1979/80 data on the basis of a 5 per cent real rate of growth and a 7.5 per cent annual rate of increase in the implicit GDP deflator, the latter rate corresponding to the actual rate of increase in the consumer price index in the second half of 1980. (See report on Recent Economic Developments to be issued shortly.)

was expected to decline from the estimated 1980 level, the bank financed deficit was budgeted to rise by 74 per cent to YRls 2.2 billion, equivalent to nearly 17 per cent of projected GDP. The authorities informed the mission, however, that the final budgetary outcome for 1981 could turn out better than revised estimates as development expenditures might not reach budgeted levels and as the impact of certain revenue measures began to be felt later in the year. In any event, the authorities intended to review actual budgetary developments in the third quarter of the year and indicated that additional measures could be taken if necessary.

As regards the 1982 budget, the authorities informed the mission that a Higher Committee for the Budget, headed by the Prime Minister, had just been formed and that preliminary work on the framework and guidelines had begun They added that certain budgetary procedures had been simplified and that closer scrutiny of expenditure requests would be exercised With regard to investment expenditures, procedures for greater coordination with the Central Planning Organization were being instituted More importantly, the authorities emphasized that the overall size of the budget would be decided primarily in relation to available revenues from noninflationary sources.

3. Monetary policy

For several years through 1977/78 the growth of domestic liquidity was determined largely by the highly expansionary impact of the external sector During this period the Yemeni authorities' policy concerns were tempered, however, by the relatively mild impact of this growth on domestic price levels and by the realization that the large payments surpluses were temporary, caused mainly by the country's low, but rapidly expanding, capacity to absorb imports. In the more recent period the offsetting impacts of a highly expansionary government deficit and of a contractionary external sector led to a decline in monetary growth rates to only moderate levels--the annual growth rates of broad money were 16 per cent in 1979/80 and 8 per cent in the second half of 1980--and domestic inflation rates continued to subside However, underlying these apparently favorable trends were certain disquieting developments of a weakened balance of payments position and a widened government deficit. Moreover, there have been indications of a tendency toward financial disintermediation through the banking system, a reversal of earlier trends of rapid monetization and spread of the banking habit. One manifestation of this disintermediation was the sharp decline in the private sector's use of bank credit despite continued strength in the growth of private sector imports. The Y.A.R authorities were cognizant of the policy implications of these trends and assured the mission that they were keeping a close watch on the balance of payments and the government budget. As regards bank credit to the private sector they cited several factors that may have contributed to the recent slowdown. Among these were the growth of informal financing arrangements for imports through overland routes, a slowdown in private sector business activity following the boom in trade and construction in the mid-1970s, the impact of higher interest rates on the demand for private borrowing, and the recent tendency, on the part of commercial banks, to place funds abroad in preference to lending for domestic operations.

The Yemeni authorities have accepted the need to maintain a flexible interest rate policy in the current international financial environment and have made several adjustments in the interest rate structure since the beginning of 1980. The last such adjustment took effect on May 9, 1981 and entailed an increase of one percentage point on time and savings deposits, to a range of 11-14 per cent, and a two percentage point increase on loans to 17 per cent. No changes were made in the interest rates on loans from the specialized credit institutions. Concerning the new structure of interest rates the mission observed that the spread between the effective cost of deposits to the banks (taking into account the 20 per cent reserve requirement) and the maximum lending rate was still very narrow for certain time deposits and was in fact negative for such deposits of 9-12 months' maturity. The authorities stated, however, that the commercial banks' profitability remained good despite this discrepancy, and that the deposits and loans denominated in foreign currency were free from interest rate regulations. The reserve requirements on interbank deposits were removed in March of 1981 and those on foreign currency deposits were under consideration for possible elimination. In any event, the authorities were watching the situation closely and assured the mission that the necessary corrective steps would be taken if and when the need should arise. The authorities added that the recent increase in the structure of interest rates should help stem the outflow of short-term capital, which appeared to have accelerated early in 1981.

4. Balance of payments policies

The weakening of the balance of payments, which had emerged in 1978/79, appeared to have accelerated since then, with the current account deficit widening from about US$140 million in 1978/79 to US$330 million in the following year. In 1980 it rose further to US$520 million while for calendar 1981 the deficit was projected at US$760 million. The overall payments deficit, which emerged for the first time in many years in 1979/80, has also widened and is projected at over US$600 million in 1981. The factors underlying this deterioration in the Y A R.'s payments position include the stagnation in workers' remittances and the stability of other external receipts, primarily official transfers, in the face of continued growth of imports stimulated by high levels of government spending. In addition, some short-term capital outflows appear to have emerged in the more recent period in response to higher interest rates abroad but also in connection with the somewhat unsettled political situation in the region and the decline in domestic investment opportunities.

The mission observed that in a fundamental sense, the weakening of the balance of payments reflected the country's improved capacity for the absorption of imports, especially for development. It was noted that in the circumstances of the Y.A.R. the utilization of external financial assets to build up real productive capacity in the country and to improve the consumption levels of the population was understandable. However, the speed with which the external surplus had been reduced and turned into a widening deficit merited the attention of the authorities. External reserves, which peaked at US$1.6 billion in March 1979 (equivalent to 15 months of imports at the then existing import level) declined by US$330 million by the end of 1980. The authorities informed the mission that in the first five months of 1981 reserves declined further by US$334 million and on the basis of official projections, the loss for the year as a whole would be around US$600 million. By the end of 1981, reserves would be equivalent to about four months of the projected imports, a level that might not be comfortable for the Y.A.R. in view of the inherent vulnerability of the country's external receipts and its enormous requirements for external resources to finance the development effort.

The authorities informed the mission that they were watching the payments situation closely and indicated that the rapid loss of reserves, evident in the first months of 1981, was expected to slow in the second half of the year. There had been some delay in the receipt of foreign aid commitments for the foreign cost components of certain development projects but these were expected to be disbursed later in the year. In addition, departure rates of workers to neighboring countries, coupled with the rapid rise of wages in the host countries in the region, were expected to improve the outlook for remittances inflows. Finally, the increase in domestic interest rates has narrowed the gap with international rates, and this should have a favorable impact on the recently evident short-term capital outflows. The mission emphasized that the authorities' efforts to stem the deterioration in the balance of payments could be fundamentally strengthened by the pursuit of more restrained demand management policies, as the source of much of the continued strength of private import demand appeared to be the sustained injection of liquidity by the public sector into the income stream.

As far as exchange rate policies and arrangements were concerned, the Yemeni authorities said that the present peg to the dollar at a rate of US$1 = YRls 4.5 had served their needs adequately. In light of the recent effective appreciation of the rial the question of the exchange rate would continue to be under review. On the management of their official reserves, they said their principal concerns were maintenance of capital value and minimization of risk, with due consideration being given also to adequate yield and liquidity. Their policy was to avoid shifts in the composition of their existing portfolio in response to short-term changes in interest or exchange rates; diversification of portfolio investments was generally achieved through the placement of new funds which depended, inter alia, on an assessment of prospects for various currencies.

IV. Staff Appraisal

The performance of the economy of the Y.A.R. over the past several years has been quite satisfactory in a number of respects. The Yemeni authorities have succeeded in achieving relatively high rates of growth of GDP, in diversifying the economy from a limited agricultural base, in building up substantial physical infrastructure, and in establishing the necessary institutions to provide public and private services. Moreover, with prudent economic management and despite mounting consumption and investment requirements, the country was able to accumulate a substantial stock of national savings in the form of external reserves. The authorities have continued to pursue their growth and diversification strategy within the framework of medium-term development plans. The staff considers that the recent orientation of development policy toward consolidation of project implementation, under the First Development Plan, to be appropiate in the circumstances and notes the careful and realistic approach being taken by the Yemini authorities in the formulation of the Second Development Plan.

In the past couple of years, however, certain financial trends have emerged which are a cause for concern. These trends are reflected in the financial position of the public sector, where both the overall budget deficit and the Government recourse to bank borrowing have risen to worrisome levels. The resulting expansion of domestic liquidity has been a factor in sustaining the growth of imports, and, together with the stagnation of inward remittances, has weakened the balance of payments and has led to a rapid loss of external reserves Although the use of foreign exchange reserves to finance economic development is understandable in the circumstances of the Y A.R., the speed with which these reserves are being drained is disquieting.

The staff considers that these financial developments cannot continue without ultimately jeopardizing the country's ability to achieve the objectives of growth and diversification in an environment of domestic and external financial stability Firm but deliberate action is called for and, as the authorities have recognized, the needed reform measures must, in the first instance, seek to reduce the size of the budget deficit and, simultaneously, to set in motion policies and mechanisms for effective mobilization of domestic resources Fortunately, the country's foreign exchange reserves, despite their recent decline, still provide a reasonable cushion so that remedial measures do not have to be precipitous and a suitable financial reform program can be formulated with careful and deliberate planning in the immediate period ahead.

The staff notes that with reference to budget preparation in the coming period, the authorities intend to place primary emphasis on a realistic assessment of available resources and on the macroeconomic impact of the budget in defining expenditure targets for 1982. To achieve the objectives of improved fiscal performance and to help mobilize domestic resources for development, the staff believes that continued efforts would need to be made to rationalize the growth of expenditures and to raise revenue growth to more satisfactory levels. In this connection, the growth of receipts from import duties, the single most important source of budget receipts, has been disappointing in the past two years and administrative measures need to be taken to restore revenue collections from this source, in relation to imports, to earlier levels. In the area of direct taxation, greater effort is needed to increase tax collections from the private sector, perhaps by simplifying the rate structure and collection procedures. Finally, with regard to excises, the staff notes the positive revenue results of converting certain specific levies to ad valorem rates and recommends that the authorities consider extending this approach on a wider scale, to include for example petroleum products, where the revenue potential is considerably greater.

In order for the resource mobilization effort to be successful, the full participation of the banking system and other financial institutions needs to be enlisted. The authorities continue to pursue a flexible interest rate policy which, together with the selective changes in reserve requirements instituted recently or currently under consideration, is intended to help stem the outflow of short-term capital that has emerged in recent months. In addition, the authorities are keeping the present interest rate structure under review to ensure that it continues to provide commercial banks with adequate incentive to accept deposits of medium- and long-term maturity and to particpate more fully in the process of financial intermediation for development.

The staff believes that policy measures, along the lines indicated above, to reduce the public sector deficit and to mobilize domestic resources in general, will help contain the present deterioration in the external accounts and provide greater assurance that the development objectives of the Y A.R can be achieved in an environment of financial stability The staff notes that the authorities continue to hold to the firm view that the imposition of quantitative restrictions or other restraints on current payments or transfers would not resolve the underlying problems in the balance of payments and could jeopardize the benefits that have accrued to the Y.A R. economy from a liberal exchange and trade system

V. Proposed Decision

The following draft decision is proposed for adoption by the Executive Board:

1. The Fund takes this decision relating to the Yemen Arab Republic's exchange measures subject to Article VIII Sections 2 and 3, and in concluding the 1981 Article XIV consultation with the Yemen Arab Republic, in the light of the 1981 Article IV consultation with the Yemen Arab Republic conducted under Decision No. 5392-(77/63), adopted April 29, 1977 (Surveillance over Exchange Rate Policies).

2. The Fund notes with satisfaction that the Yemen Arab Republic continues to maintain an exchange system that is free of restrictions on payments and transfers for current international transactions.

Yemen Arab Republic: Relations with the Fund

Date of membership:	May 22, 1970.
Status:	Article XIV.
Quota.	The Y.A.R.'s present quota is SDR 19.5 million.
Fund holdings of Yemen rials:	As of June 30, 1981 Fund holdings of Yemen rials amounted to 44.5 per cent of quota.
SDR position:	As of June 30, 1981 the Y.A.R.'s holdings were SDR 12.5 million, equivalent to 209.3 per cent of its net cumulative allocations.
Trust Fund:	The Y.A.R. was on the list of eligible countries, but did not satisfy the requirements of need for Trust Fund assistance.
Direct distribution of profits from gold sales.	SDR 1.2 million.
Gold distribution:	8,557.999 fine ounces (four sales).
Exchange system:	The Yemen rial is pegged to the U.S. dollar which is the intervention currency. In connection with a reserve tranche purchase in December 1970, the Y.A.R. proposed, and the Fund accepted, a provisional rate of YRl 1 = US$0.20. The free market rate for the Yemen rial had fluctuated, but toward the end of 1971 the rate stabilized at YRls 5 = US$1.00. The Central Bank maintained this rate until February 25, 1973 when the Central Bank rate was changed to YRls 4.5 = US$1.00 which has since been maintained. The representative rate established under the Fund's Rule O-2 is US$1 = YRls 4.5625, the average of the Central Bank's buying and selling rates for the U.S. dollar.

Technical assistance.	Since 1970 the Fund has been providing considerable technical assistance through central banking and fiscal experts stationed in the Y.A.R. At present, the Central Bank of Yemen and the Ministry of Finance each has three experts assigned by the Fund. In addition, the Fund staff provided technical assistance related to tax policy in 1974, a proposed bond scheme in 1977, and (with the IBRD) domestic resource mobilization in 1981.
Last Article IV consultation	The Staff Report (SM/80/106) was discussed by the Executive Board on June 25, 1980. Discussions were held by the staff in Sana'a during March 23-31, 1980

The Executive Board's decision (Decision No 6538-(80/98)), adopted June 25, 1980 was as follows

1. The Fund takes this decision relating to the Yemen Arab Republic's exchange measures subject to Article VIII, Sections 2 and 3, and in concluding the 1980 Article XIV consultation with the Yemen Arab Republic, in the light of the 1980 Article IV consultation with the Yemen Arab Republic conducted under Decision No. 5392-(77/63), adopted April 29, 1977 (Surveillance over Exchange Rate Policies).

2 The Fund notes with satisfaction that the Yemen Arab Republic continues to maintain an exchange system that is free of restrictions on payments and transfers for current international transactions

Yemen Arab Republic: Basic Data

Area and population					
Area					195,000 square kilometers
Resident population (mid-1980)					7 million
Per capita GDP (1979/80)					YRls 1,700 ($380)

	1977/78 1/	1978/79 1/	1979/80 1/	Est. 1980 2/	Proj. 1981
	(In millions of Yemen rials)				
Production and prices					
GDP	8,220	10,166	11,919	...	...
GDP (in 1975/76 market prices)	5,615	5,978	6,318	...	...
Percentage growth of real GDP	(8.3)	(6.5)	(5.7)	(...)	(...)
Percentage change in Sana'a consumer price index	(16.7)	(21.8)	(10.6)	(...)	(...)
Public finance					
Revenues	1,988	2,175	2,763	3,051	3,911
Expenditure	2,417	4,465	5,024	5,719	7,444
Current	(1,250)	(1,847)	(2,531)	(2,855)	(3,228)
Capital	(1,167)	(2,618)	(2,492)	(2,864)	(4,217)
Deficit (-)	-429	-2,290	-2,261	-2,668	-3,533
External financing	691	1,904	976	1,584	1,330
Domestic bank financing	-51	381	1,808	1,263	2,203
Deficit as a percentage of GDP	(5.2)	(22.5)	(19.0)	(...)	(...)
Money and credit (change during period)					
Money	1,565	1,192	1,077	541	...
Domestic liquidity (money and quasi-money)	1,835	1,378	1,240	882	...
Net foreign assets	1,914	574	-127	-176	-2,765
Net claims on Government	-51	381	1,808	1,263	2,203
Claims on nongovernment sectors	81	645	630	649	...
Credit to public and mixed enterprises	(163)	(188)	(316)	(325)	(...)
Credit to private sector	(-82)	(456)	(315)	(324)	(...)
Percentage change in domestic liquidity	(42)	(22)	(16)	(11)	(...)
Ratios of					
GDP to money 3/	(1.84)	(1.76)	(1.73)	(...)	(...)
GDP to domestic liquidity 3/	(1.56)	(1.47)	(1.45)	(...)	(...)

1/ Year ended June 30.
2/ Estimated from the 1979/80 data and from preliminary figures for the six-month transitional period, July-December 1980.
3/ Denominators are averages of June, December, and June balances.

Yemen Arab Republic: Basic Data (concluded)

	1977/78 1/	1978/79 1/	1979/80 1/	Est. 1980 2/	Proj. 1981
	(In millions of U.S. dollars)				
ınce of payments					
:ports, f.o.b.	7	3	7	13	18
ıports, f.o.b.	-801	-1,250	-1,546	1,708	-1,845
Balance of trade	-794	-1,247	-1,539	1,695	-1,827
:rvices (net)	-69	-36	--	-56	-67
·ivate transfers (net)	1,039	833	1,099	1,084	1,022
fficial transfers (net)	101	312	112	148	111
Current account	276	-138	-329	-520	-760
apital account	76	116	158	259	184
rrors and omissions (net)	73	150	143	221	-39
Overall balance	425	128	-28	-39	-614
ercentages of					
Current account to GDP	(15.1)	(-6.1)	(-12.4)	(...)	(...)
Oil imports to total imports	(2.7)	(2.7)	(4.8)	(...)	(...)
al reserves (end of period)	1,348	1,551	1,430	1,284	..
n months of imports	(20)	(15)	(11)	(9)	(...)
bursed external debt outstanding (end of period)	439	543	592	712	...
ercentages of					
External debt to GDP	(24)	(24)	(22)	(...)	(...)
External debt service to GDP	(0.5)	(0.6)	(0.5)	(...)	(..)
External debt service to current account receipts	(0.6)	(0.9)	(0 7)	(...)	( )