

March 2, 2015

## **Yemen: A Land with a Rich Past and a Poor Present**

The country of Yemen is slowly dissolving in the midst of an ongoing civil war. The Houthi movement has aggressively secured territories in the north, including taking over the capital city of Sana, while al-Qaeda has widened its activities in the south.

At the end of January, Yemeni President Abd Rabbuh Mansur Hadi and his prime minister, Khaled Baha, were forced to step down after the presidential palace had been under insurgent Shiite Houthi fire for several days. Since then, the president has tried to resume his duties, but the leader of the Houthis has also claimed the presidency. Currently, there is no acting president, the parliament has been dissolved and it seems that military loyalties are fractured between tribal leaders. In this environment, it is unclear who is in control of the country.

Outside powers are watching these developments closely. Yemen's wealthy neighbor and U.S. ally, Saudi Arabia, would like to see the Houthi insurgency stopped as the group is widely viewed as a proxy for Iran. Saudi Arabia does not want to see Iran spread its sphere of influence.

At the same time, the U.S. has been a partner to Yemen in fighting al-Qaeda in the Arabian Peninsula, but the fall of its government has left the U.S. without a formal partner. A partnership of convenience with the Houthis seems like the most practical approach for the U.S.

However, this approach, in addition to the possibility of a U.S.-Iran nuclear deal, would make the Saudis nervous and unsure about the direction of American foreign policy in the region.

The single, unified country of Yemen is unlikely to survive in the current environment of fragmented political power. In fact, looking at Yemen's long-term history, existing as a unified country is an anomaly. It is likely that the country would return to its natural divided state, becoming a Sunni South Yemen and a Shiite North Yemen.

### **Brief History**

Historically, Yemen was a melting pot of people and faiths. The country's location at the tip of the Arabian Peninsula made it a well-situated, pivotal crossroad for trade and travel between the East and the West.

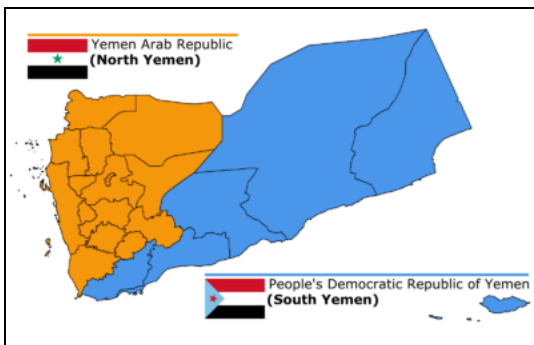


(Source: CIA World Factbook)

Like most of the region, the Yemeni area was ruled by various caliphates or kingdoms, and most of its people lived in tribes. Near-constant fighting occurred between the tribes, the caliphates and the Ottoman Empire. The Ottoman Empire controlled parts of northern Yemen, and in 1832, the British Empire captured a part of Yemen to serve as a strategic waypoint between Europe and its territories in India. To this day, Yemen remains an important strategic sea lane country, located at the mouth of the Red Sea through which ships have to pass in order to get to the Suez Canal. Additionally, most of the Persian Gulf oil exports to Europe have to pass through the region.

In 1904, the British and the Ottoman empires divided the area that is current-day Yemen into an Ottoman-controlled northern region and British-controlled southern region. When the Ottoman Empire fell after WWI, the north became an independent kingdom. However, civil war broke out after Arab nationalists toppled the kingdom in an attempt to establish a republic. Fighting has plagued the region ever since.

Britain ruled South Yemen until 1967, fighting an aggressive insurgency in the later years of its rule. Radical Marxists, with the help of the Soviet Union, established the People’s Democratic Republic of Yemen in the south soon after Britain left the region.



(Source: Wikipedia)

The region became a unified country for the first time when the south and north merged in 1990. The south had been heavily funded by the USSR, and when it fell, South Yemen lacked another sponsor. Additionally, the countries merged in order to jointly invest in oil exploration and production in the region around their shared border.

Since its inception, the unified Yemen has been plagued by near-constant civil strife, with poverty, corruption and a weak rule of law. The long-time president of North Yemen, Ali Abdullah Saleh, took over as the president of the unified country. However, he primarily played various factions against each other to centralize power, rather than build a strong republic.

The southerners have long-resented the northern-led government that has favored northerners for political posts and development projects. The rivalries between various tribes make governing the region even more complicated.

Inspired by the Arab Spring, the Yemeni people staged mass protests against corruption, poverty, unemployment and general economic conditions during the Yemeni Revolution in 2011. The protests also called for President Saleh to step down. Heavy fighting ensued, but Saleh refused a peace deal brokered by the Gulf Cooperation Council, instead offering not to run for president in the next elections. Only after one of the more politically powerful tribes expressed its support for the opposition party did Saleh step down. He was replaced by Vice President Abd Rabbuh Mansur Hadi to head a transitional government until formal elections could be held. Hadi won the presidential elections in 2012, although the election results as well as Saleh’s resignation were rejected by some tribes. Since his resignation, Saleh has been

accused of undermining the stability of the new government. As mentioned above, Hadi and his government stepped down at the end of January of this year.

### **Various Conflicts**

The conflicts in Yemen are widespread and multifold. The north/south division is centuries old, while the Houthi/government fighting has received increasing international attention recently. At its core, there are four main conflicts brewing in Yemen.

First, the historic north/south conflict is based on the differences between religion and view of government involvement. As described in the history above, the ideologies of the two regions are different. At the same time, most of Yemen's oil fields are located in the middle of the country and both sides want the controlling stake and are ready to fight for them.

Second, followers of the old regime's long-time president, Saleh, are actively undermining the new transitional government. The Houthis are in a union of convenience with the supporters of Saleh. Given that military loyalties still lie with Saleh, it has been speculated that Saleh has instructed the officers to aid, or at least not stop, the Houthi movement. Saleh would benefit from the Houthis eliminating the current government as it is speculated that he would like to see his son become president. He may succeed in this endeavor if the choice is between the Houthis from the north or al-Qaeda from the south; Saleh, or his son, may seem like the moderate option at that point.

Third, military loyalties do not lie with the central government, but with the leaders of the local tribes and sects. As mentioned before, these tribes also oftentimes support

Saleh rather than the new president, Hadi. This effectively leaves the government without the tools to fight insurgencies or implement its policies.

Fourth, the power vacuum since the Yemeni Revolution in 2011 has allowed other insurgencies to spread. Various tribes and provinces have allowed al-Qaeda to set up camps and training facilities as alternative security measures to guard against the Houthi offensive. These provinces have been left out of the formal political process, and thus feel that joining a terrorist group is the only way to fight the incumbent government. Additionally, Yemen is majority Sunni, so a tribe is more likely to support the Sunni al-Qaeda than the Shiite Houthis.

### **Who are the Houthis?**

The Houthi movement was founded by Hussein Badreddin al-Houthi, who was inspired by the Iranian revolution and politics of Hezbollah in Lebanon. The group's original slogan was, "God is great, death to America, death to Israel, damnation to the Jews, victory to Islam," but they have since modified it to be "Ansar Allah," the "Partisans" or "Champions of God."

The Houthi military/political movement developed from a Shiite religious doctrine, in a similar fashion to how the Taliban terrorist movement arose. Apparently, President Saleh set up a religious school in the northern Yemeni town of Saada. The school was supposed to teach Shiite ideology but also train fanatical fighters that would protect Yemeni territories from a possible Sunni-ideology based Saudi Arabian attack. In the 1990s, when the school was established, the border between the two countries was not finalized and both sides accused each other of border violations.

Al-Houthi became the school's Imam, hence the movement's name. Many students in the school became ideological militants, just as President Saleh had allegedly wanted. However, these militants were also opposed to the spread of Sunni influences from the south.

When Yemen and Saudi Arabia signed the border agreement in 2000, the Houthi group was no longer needed by the government. Inspired by radical ideology and funded by Iran, the Houthis became increasingly aggressive.

When President Saleh stepped down in 2011, the group used this opportunity to expand its territory. At the same time, the Houthis also took part in the formal political process by forming a party, in a move similar to Hezbollah in Lebanon in the 1990s.

Although the Houthis are part of the political process, they have hindered the pace of reforms. In one instance, when a government-proposed reform suggested that the group should give up territories that it has gained through force, the group allegedly kidnapped the chief of staff. We do note that the practice of kidnapping in order to gain a desired political outcome is also apparently common in the country.

In a never-ending vicious cycle, the Houthis are claiming that they offer a moderate alternative to al-Qaeda, but the fighting is contributing to the endemic instability, poverty, unemployment and political divisions. These factors themselves contribute to the spread of al-Qaeda and other insurgencies.

### **International Response**

The international response has been mixed (and unenthusiastic). The U.S. has

withdrawn its military and diplomatic staff from the country. Additionally, a majority of the Gulf States do not support the Houthi movement due to its close ties with Iran. If the Houthi movement continues, the Gulf States will likely move to support the south's secession. An independent Sunni-led south would allow for safe passage of oil through the Red Sea.

Yemen depends heavily on foreign aid, especially from Saudi Arabia. Apparently, the Saudis have stopped their funding since the Houthis have come to power. If the Houthis remain in power, the Saudis may decide to permanently withdraw their aid.

Another major source of income for Yemen is oil production. However, given the lack of new investment in the sector by the government and the dearth of foreign investment due to the uncertain political environment, oil is projected to run out by 2017 using current technology.

Yemen has been a partner to the U.S. in containing al-Qaeda in the Arabian Peninsula, even though the country shows the highest rates of "anti-Americanism" in the Arab world.

Saudi Arabia has also historically been a U.S. ally. However, the U.S.-Iran nuclear deal and normalization of relations between the two countries could mean major changes in U.S. policy in the Middle East. In Yemen, the most compelling partner in fighting al-Qaeda would be the Houthis, who are rumored to be funded by Iran.

The strategic goals of the U.S. and Saudi Arabia in Yemen are slightly mismatched. The U.S. views al-Qaeda as the primary threat, while Saudi Arabia would like to support the conservative Sunni tribes and prevent the Shi'ite violence from spreading

across the border. Given that Saudi Arabia is involved in a proxy war with Iran, it does not want Iranian influence to spread.

### **Ramifications**

The civil war between the Shiites in the north and Sunnis in the south, supported by outside powers, is likely to divide the country. The north will be aided by Iran, while the south will be supported by Saudi Arabia.

At the same time, the U.S. is unsure if it should get involved and, if so, whom to support. The main goal of the U.S. in Yemen is to fight the al-Qaeda insurgency. However, its allies in the region, especially Saudi Arabia, would rather support the Sunnis, who are fighting against the Shiites in a union of convenience with al-Qaeda. U.S. foreign policy has become friendlier

toward Iran recently, so it is possible that the U.S. will either not get involved or will support the Iranian-backed Shiite Houthis. This, in turn, would deteriorate U.S.-Saudi relations.

Unrest in the region should be bullish for oil prices, especially if the fighting in Yemen spills over to Saudi Arabia. Unrest in the kingdom itself could have wider implications, especially now that the new king has taken his seat.

We could also see piracy pick up in the Gulf of Aden and the Red Sea. We would not expect any major disruptions, but smaller disturbances are possible.

Kaisa Stucke  
March 2, 2015

*This report was prepared by Kaisa Stucke of Confluence Investment Management LLC and reflects the current opinion of the author. It is based upon sources and data believed to be accurate and reliable. Opinions and forward looking statements expressed are subject to change without notice. This information does not constitute a solicitation or an offer to buy or sell any security.*

### **Confluence Investment Management LLC**

---

Confluence Investment Management LLC is an independent, SEC Registered Investment Advisor located in St. Louis, Missouri. The firm provides professional portfolio management and advisory services to institutional and individual clients. Confluence's investment philosophy is based upon independent, fundamental research that integrates the firm's evaluation of market cycles, macroeconomics and geopolitical analysis with a value-driven, fundamental company-specific approach. The firm's portfolio management philosophy begins by assessing risk, and follows through by positioning client portfolios to achieve stated income and growth objectives. The Confluence team is comprised of experienced investment professionals who are dedicated to an exceptional level of client service and communication.