Economic Developments

At the Paris Conference in December 2007, the PA unveiled the Palestinian Reform and Development Plan (PRDP) which relied on growth of about 3.5% in the first year rising to about 5% in the third year of the plan. These growth projections were based upon the assumptions of a relaxation in economic restrictions on the Palestinian economy, and a resolution of the situation in Gaza. However, the economic restrictions have remained in place and the situation in Gaza has continued to deteriorate. As a result, the Palestinian Central Bureau of Statistics (PCBS) estimates that real GDP growth in 2007 was a mere 0.5%. Results from the first quarter suggest that growth in 2008 is slightly negative. IMF analysis notes a drop in GDP of -0.5% in 2007, and modest growth of 0.8% in 2008. This is likely due to a continued yet marginal drop in economic activity in Gaza, given its already-low base, matched with a modest rise in economic activity in the West Bank.

In addition to growth being low, the economy’s productive base continues to hollow out as evidenced by the changing GDP structure. In 1999, Agriculture and Industry accounted for nearly 25% of GDP, and Education, Health and Public Administration was less than 20%. In the first quarter of 2008, Agriculture and Industry combined were approximately 19% of GDP and Education, Health and Public Administration accounted for almost 25%. IMF estimates of GDP indicate that the PA’s cash wage bill alone is equivalent to over 27% of GDP. Furthermore, PCBS estimates that in 2007, manufacturing output was approximately 1.8% lower than in 2006 and 23% lower than in 1999. The lack of investment is also evidenced by the fact that the construction sector has seen little growth in the last four years and is less than 20% of its size in 1999. Recently, a few large housing construction projects have been announced in the West Bank, including a new planned community north of Ramallah, which will require over US $500 million in private investment. If these projects actually come to fruition they would be a large boost to the construction sector and the Palestinian economy as a whole.

As the economy stagnates and the population grows, per capita income continues to fall. The PCBS completed a new census at the end of 2007, which revealed a 2.6% average annual population growth for the last decade. With a growing population and a shrinking economy, real per capita GDP is now close to 30% below its height in 1999. From 1994 until 1999 the Palestinian economy was growing at about 6% per year. If this trend had continued, GDP per capita would be nearly 85% higher than it is currently.10

10 PCBS has not yet released revised population figures for years between 1997 and 2007. The graphs are based on the unrevised figures.
As the Palestinian economy declines it is steadily becoming more aid dependent. So far this year until end-August the PA has received $1.2 billion in recurrent budget support and may require almost $1.9 billion in recurrent budget support in 2008. Thus, with the IMF estimating nominal GDP at just over US $6.6 billion, external recurrent budget support will be the equivalent of at least 28% of GDP (and 32% of GDP including the projected development aid). By comparison, in 2007 the estimated recurrent and developmental budget support added up to 25% of GDP.

There are no separate figures for recent output in the West Bank and Gaza. Despite some anecdotal indications that the West Bank could be experiencing a increase in economic activity, there is no evidence that this increase is substantial. The Israeli Civil Administration reports that the number of trucks crossing between Israel and the West Bank in the first half of the year increased by more than 44% compared to the last half of 2007. In addition, tourist visits to Jericho and Bethlehem increased significantly in 2008. However, the figures on trucks also include traffic to Israeli settlements, and tourism represents only a small percentage of the Palestinian economy. In addition, the real value of domestic tax collections has fallen. Thus, whatever growth has been witnessed in the West Bank is unlikely to be substantial.

Unemployment in the West Bank rose from 17.7% in 2007 to 19% in the first quarter of 2008, while unemployment in Gaza has increased from 29.7% to 29.8%. These figures do not take into account underemployed workers who have turned to unpaid family labor or seasonal agriculture. The figures also do not include the many discouraged workers who have left the labor force.¹¹ The labor force participation rates are low and dropping. In the West Bank

¹¹ Unemployment figures do not include the large number of “workers absent from their usual work”. In the PCBS calculations, these workers are assumed to be temporarily away from jobs due to illness, work stoppage, natural disaster or for other reasons but still receiving normal pay. UNRWA estimates that nearly 45,000 Gazans have become “absentee” workers since the first half of 2007.
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It fell from 44% in 2007 to 42.3% in the first quarter of 2008, and from 38% to 37.5% in Gaza. Adding discouraged workers would increase the unemployment rate to 25.7% in the West Bank and 35.5% in Gaza.\(^{12}\)

**Figure 2:** Unemployment in the West Bank and Gaza

![Unemployment Graph](image)

Source: Palestinian Central Bureau of Statistics.

Palestinian unemployment is likely to increase if Israel proceeds with plans to levy taxes on Israelis hiring Palestinians. The Israeli authorities have announced an increase in the number of Palestinian workers granted work permits in Israel, including a recent statement referring to 5,000 new permits. However, the Israeli Government has introduced a new levy on Israeli recruiters of Palestinian workers in Israel. According to PA estimates, an average Palestinian worker earns about NIS 4,000/month. With this new levy—estimated at NIS 2,500-3,000 per worker per month—a Palestinian worker will now cost NIS 6,500-7,000 per month, thus reducing all their comparative advantage vis-à-vis the more expensive Israeli workers.

The crisis in Gaza has led to a drastic increase in poverty. The official poverty rate for 2007 was 51.8%, compared to 47.9% in 2006. In the West Bank poverty slightly declined, falling from 22% in 2006 to about 19.1% in 2007. The percentage of Gazans in Deep Poverty continued to rise, increasing from 33.2% in 2006 to 35% in 2007.\(^ {13}\) These rates reflect actual consumption. If remittances and food aid are excluded and poverty is based only on household income, the poverty rate in Gaza and the West Bank would soar to 79.4% and 45.7% respectively and the Deep Poverty rate would increase to 69.9% and 34.1%.\(^ {14}\) This illustrates the high levels of aid

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\(^{12}\) PCBC Labor Force Survey Q1 2008.

\(^{13}\) PCBS uses two measures of poverty: Deep Poverty (absolute) and Poverty. The Deep Poverty line reflects a budget for food, clothing and housing only. For a family of six, the deep poverty line in 2006 was NIS 1,837. The Poverty line adds other necessities including health care, education, transportation, personal care and housekeeping supplies; raising the line to NIS 2,300 for a family of 6. Thus, the percentage of households in Poverty includes those in Deep Poverty.

\(^{14}\) PCBS: Poverty and Living Conditions in the Palestinian Territory, 2007.
dependency in the West Bank and Gaza, particularly taking into account the fact that the majority public sector salaries are financed with foreign aid.

Poverty and the global rise in food prices have taken a heavy toll on Palestinian living conditions, as has the dramatic rise in catastrophic health payments by households. The consumer price index for food has increased by 28% in Gaza and 21.4% in the West Bank from June 2007 to June 2008. Despite the large inflows of aid, a recent WFP survey found that food insecurity continues to rise, and is estimated to have increased from 34% in 2006 to 38% in 2007. Food insecurity is even more pronounced in Gaza, reaching 56% of households. Approximately 66% of income earned in Gaza is spent on food, with 56% of income is spent on food in the West Bank. The analysis also reveals that Palestinians are eating less; 75% of Palestinians have reduced the quantity of food they buy and 89% have reduced the quality. The lack of protein and vitamins has increased the prevalence of anemia and other nutrient deficiencies and is likely to have long term health consequences on children. Furthermore, from 2006-2007, the percentage of Palestinian households spending 10% or more of their total household expenditures on health increased from 5.5% to around 12.1% – a more than two-fold increase in the prevalence of catastrophic health payments in one year. A similar rate of increase in excessive health spending is witnessed using discretionary household expenditure during the same time period.

The social impacts of the current crisis are no less significant. Continuing conflict is perpetuating an internal cycle of violence, fragmenting social cohesion and affecting psychosocial well-being. A 2006 survey concluded that nearly three quarters of the Palestinian population suffers from severe depression as a result of the current situation. Women, who historically play a key role in providing income for their households, are being increasingly relegated to the informal market as a result the restrictions on access and movement. Their participation in the labor market, at 15.7 percent, is amongst the lowest in the world. Also, since September 2000, youth have been caught literally and figuratively in the crossfire of the conflict. Nearly 75% of the total injured during the second Intifadah were between 10 to 29 years old. As of June 2008, 62% of those killed in the Israeli-Palestinian conflict are youth between 15 to 29 years of age.

20 PCBS, “Youth in Palestinian Territory, Statistical Indicators” 12 August, 2008
The Gaza Strip

The closure policy on Gaza since the Hamas takeover of Strip on June 14th, 2007 continues to erode the Strip’s industrial backbone. Over 54% of employment in Gaza was private sector-driven prior to the closure.\(^1\) Gazan manufacturers imported 95% of their inputs. About 76% of their furniture products, 90% of their garments and 20% of their food products used to be exported to Israel, and some to the West Bank. The Palestinian Federation of Industries (PFI) estimates that 98% of Gaza’s industrial operations are now inactive. According to PFI, of Gaza’s 3,900 industries, 23 are operating; 6 produce wheatflower, one produces clothing, and the remainder provide food processing. Nearly 40,000 farmers in the agricultural sector and more than 70,000 workers in other sectors (34,000 in the industrial sector) lost their jobs. As a result of the moribund economy, Gazan banking sector activity is estimated to have dropped from 40% of total Palestinian banking, to about 7%.\(^2\) Their ability to function is also compromised by the restrictions on the entry of currency into Gaza.\(^3\) Discussions with various representatives of the banking sector point to an emerging market for the supply of currency and industrial inputs as a result of the Israeli closures and the prevailing lawlessness in Gaza, leading to a redistribution of wealth from the formal private sector towards black market operators.

Closure of Gaza is also resulting in the collapse of the municipal sector. Municipalities, providing key services such as water, sewage, solid waste etc. are facing a deep financial crisis. The impoverishment of the population and the near absence of private sector activities imply that municipalities are unable to collect fees for service provision and are unable to pay staff salaries. The ability of municipalities to provide basic services is also severely constrained by their inability to import spare parts and supplies for the provision of basic services such as water and sanitation.

While the IT sector has circumvented movement and access restrictions to some extent, it is still too nascent to alter the course of the Gazan economy. Gaza’s emerging IT sector engages in hardware, services and software development/outsourcing. Firms specializing in software development and outsourcing have been particularly effective, with Gazan firms seeking to tackle new US, European and Arab markets. There are 1,000 new graduates in IT every year, of which 600 are in Gaza.\(^4\) However, the nascent IT sector’s impact on the Gazan economy is minimal, and the sector remains constrained by the current closures (for training, marketing, business relationships, participating in trade fairs), thus stopping them from achieving economies

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\(^1\) Private Sector Coordination Council (PSCC), Effect on Private Sector in Gaza, July 12, 2007.
\(^2\) Estimates provided by Cairo Amman Bank in Gaza.
\(^3\) In August, and after months of requests by the Palestine Monetary Authority and the international community, the Israeli authorities allowed for the entry of NIS 68 million into Gaza, and the recycling of approximately NIS 20 million in old currency. This allowed the PA to pay public sector salaries in Gaza, albeit on a staggered basis.
\(^4\) Engineering design is another sector with the same fundamentals.
of scale. Moreover, several donors who regard this as a promising sector continue to focus on firms in the West Bank.

On 19 June, at 6 am, the ‘Tahdi’ah’ (i.e., calm) between Israel and Hamas came into effect. Despite the agreed calm, several incidents took place subsequently in which Palestinian factions launched rockets into Israel, and Israel reacted to each of these by closing the crossings. Nevertheless the ceasefire is still holding, and there has been an increase in the flow of goods through the crossings. In a briefing to the World Bank, the Israeli Ministry of Foreign Affairs notes that, since the calm: (a) goods entering Gaza have increased from 60-70 trucks per day to 90/day, with the Sufa Crossing at full capacity; (b) fuel for the power plant has increased from 2.2 million liters/week to 2.9 million liters/week; (c) Diesel has increased from 800,000 liters/week to 1.2 million/week; and (d) greater quantities of other types of fuel, including cooking fuel, have been allowed into Gaza.

Table 1: Comparison of Flow of Goods in/out of Gaza since the Tahdi’ah

<table>
<thead>
<tr>
<th></th>
<th>Before June 2007</th>
<th>June 2007- June 2008</th>
<th>After Tahdi’ah (June 22 on)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Average Monthly Imports, All Terminals (Trucks)</td>
<td>9400</td>
<td>1930</td>
<td>4715</td>
</tr>
<tr>
<td>Average Monthly Exports, All Terminals (Trucks)</td>
<td>1440</td>
<td>0</td>
<td>0(^{26})</td>
</tr>
<tr>
<td>Average Monthly Aggregate Imports(Trucks)</td>
<td>4500</td>
<td>0</td>
<td>2122</td>
</tr>
<tr>
<td>Average Monthly Cement Imports (Trucks)</td>
<td>1000</td>
<td>0</td>
<td>123</td>
</tr>
<tr>
<td>Average Monthly Metal Imports (Trucks)</td>
<td>80</td>
<td>0</td>
<td>1</td>
</tr>
<tr>
<td>Average Monthly Cooking Gas Imports (’000 Kg)</td>
<td>5000</td>
<td>4525</td>
<td>4118</td>
</tr>
<tr>
<td>Average Monthly Diesel Supply (’000 liters)</td>
<td>8500</td>
<td>4138</td>
<td>4788</td>
</tr>
<tr>
<td>Average Monthly Benzene Supply (’000 liters)</td>
<td>1500</td>
<td>1463</td>
<td>0.541</td>
</tr>
</tbody>
</table>

Source: Paltrade, August 2008.

Despite the truce, and the marginal reduction in closures on Gaza, little progress has been made so far improving living conditions of the population there. First, the increase in fuel and humanitarian imports remains far below needs. According to the UN, fuel imports increased by ¼ in June compared to May (from 11.4 million liters in May to 14.1 million liters

\(^{26}\) No exports were allowed out of Gaza since February 2008. Since June 2007, only 132 truckloads, mainly strawberries, potatoes, and flowers had passed through Kerem Shalom. Paltrade.
in June, including industrial diesel for the Gaza power plant. However, this was 54% of Gaza’s monthly needs (about 26 million liters). The amount of cooking gas entering Gaza in June (3 million liters) increased by only 0.5% compared to May, and constitutes about 40% of monthly needs. The Coastal Municipal Water Utility (CMWU) is receiving approximately 40% of its fuel requirements.\textsuperscript{27} In their July 24th Report, the UK House of Commons International Development Committee noted that “…The humanitarian situation in Gaza has been acute. Food, fuel and water have been in short supply and the public health system has been under severe pressure…”\textsuperscript{28}

**Consequences of the shortage of fuel and other humanitarian items continue to be apparent.** These include the curtailed production of electricity by the Gaza Power Plant, the major restrictions of water supply, the continued use of vegetable oil to run vehicles, the accumulation of 600 tones of garbage a day on the streets, and the daily dumping of 70-80 million liters of raw or partially treated sewage into the Mediterranean Sea. The linkages between this situation and the emergence of 40 cases of bacterial meningitis in Gazan hospitals are apparent.\textsuperscript{29}

**The existing minimal social services such as health and education are further disrupted by on-going tensions.** About 50% of health workers have been on strike since August 30th, 2008. Most Gaza hospitals are only providing emergency services, with about 40% of health workers reporting to work. In the education sector, about 60% of teachers are said to be reporting to work in Gaza and student attendance ranges between 50% and 80%. A one day universal strike was called on September 8th, 2008 for all university staff.\textsuperscript{30}

**Due to the closure policies and recent actions by the authorities within Gaza to intervene, various donor projects targeting an improvement in basic services to Gaza’s population are unable to be completed, or even start.** Gaza’s water and sewage system continues to be in urgent need of rehabilitation. In the long term, the Gaza Strip requires three modern sewage treatment plants to ensure that all waste water is properly treated. The Israeli authorities have recently allowed in a number of spare parts into Gaza and increased the fuel supply, and have continued to facilitate the completion of the North Gaza Emergency Sewage Treatment Plant. However, at the time of this report, the project remains incomplete due to the inability to bring all goods in. The Israeli authorities note that efforts are made to facilitate the entry of all goods through one crossing, as the Kerem Shalom Crossing was closed after an attack by militants in Gaza. The Kerem Shalom Crossing has reopened on August 19th and is regarded as being able to increase the flow of goods. Moreover, the June takeover of one of the buildings of the Palestinian Water Authority (PWA) by Hamas-affiliated personnel is also regarded as an

\textsuperscript{27} The UN Humanitarian Monitority for the Occupied Palestinian Territory, June 2008.


\textsuperscript{29} According to Physicians for Human Rights, forty cases of bacterial meningitis were found in Mohammad Al-Doura Hospital in Gaza, which according to them is due to the water and sanitation problem.

impediment to project implementation in Gaza, as are the closures of critical NGOs there by Hamas affiliates. With regard to actions taken within Gaza that have impacted donor assistance, the Israeli authorities have noted the continued refusal of Hamas to accept the conditions posed by the international community, and the need for this report to reflect “…the responsibility borne by the Hamas regime in Gaza, for the low living standards in the area under its control, and in the fact that Hamas probably is responsible for the allotment of the products entering Gaza, controlling their distribution.”

The reversal of Gaza’s humanitarian crisis extends beyond the entry of goods, and must include the access of the population to the West Bank for all purposes, and to Israel and elsewhere for health, education and other social services. Recent analysis by Physicians for Human Rights shows a combination of increased referrals out of Gaza- due in no small part to the closure of Rafah Crossing with Egypt and the lack of medical spare parts in Gaza- along with a reduction in Israeli permits to exit to and through Israel. There has been a sharp increase in the proportion of patients denied exit permits: from 10% in the first half of 2007 to 35% in the first half of 2008. Access to education and training opportunities outside of Gaza is equally limited. According to the Israeli NGO Gisha, as of January 2008, 480 of the 1,100 students and family members that requested to leave Gaza were granted exit. Recently, the Ministry of Defense informed the UN of a decision to provide an additional 100 exit permits for Gazans wishing to study abroad. Currently, the estimated requirement is for 600 exit permits.

In addition to humanitarian relief, there is an urgent need to revive Gaza’s private sector. The current increase in the quantities and categories of items entering Gaza is a necessary step, but is insufficient. Karni, the main commercial crossing between Gaza and Israel, remains closed, except for a conveyor belt transporting cement, grain and fodder. The Kerem Shalom crossing was closed between April 19th and August 19th as a direct result of an attack from Gaza on the crossing, and as of the time of the report was allowing only 5 truckloads.

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31 Israeli Ministry of Justice comments on this report, September 8th, 2008
32 Physicians for Human Rights-Israel, Access to Health Care Report, July 2008. More recent reports place the rejection rate as closer to 44%.
33 Excerpt of letter from Foreign Minister Tzipi Livni to Member of Knesset, July 7, 2008: «The policy of not permitting exit abroad for students from Gaza is part of the Security Cabinet decision from 19.09.07 which defined Gaza as a hostile entity and placed restrictions on the borders for passage of goods and movement of people from the Strip and to it except for humanitarian cases. As of today, there is no change in this policy. At the same time, after consideration of particular cases, a few exceptions were approved, following, among other things, requests made by international actors. The Ministry of Foreign Affairs is in touch with the relevant authorities in the security system in order to analyze the policy in this matter and its implementation according to the circumstances of each case, among other things by responding positively to requests from friendly countries and this in parallel with the work of military authorities in the security system to clarify its position on this subject.» Gisha, Students Still Trapped in Gaza, July 16, 2008.
34 The events surrounding the US Fulbright Scholarship cancelations for seven students on May 29th, and reinstatement of some, due to lack of exit permits are well-documented.
36 In August-September 2007 and again in December 2007-January 2008, Israel arranged shuttle bus services allowing Gazans to travel via the Erez crossing directly to the Nitzana and Kerem Shalom border crossing. Only around 480 students successfully exited Gaza via the shuttles during the 07-08 academic year. Since January 13, 2008, Israel has not allowed any students out via the shuttles.
per day. The daily averages of truckloads through Sufa and Karni have increased, but remain well-below the daily average of 450 truckloads in January 2007. Lastly, the Rafah Crossing with Egypt, regarded as a potential trade route for the Palestinian economy, has been closed even for passengers since the Hamas elections in early 2006.

Not only are the quantities of inputs entering Gaza insufficient to resuscitate the private sector, the categories and combinations of items allowed to enter are not conducive to most industrial operations. While the expansion of categories to include some inputs (cement, gravel, steel bars, pipes, spare parts, wood, etc.) is a very welcome step and has triggered a partial return of the construction sector, over 90% of imports remain humanitarian items. Furthermore, the partial entry of one input has rendered some of the other inputs useless for production. For instance, substantially more gravel was allowed to come into Gaza, but relatively less cement, steel bars, plaster, wood, etc. As a result, the process by which inputs are being allowed in is rendering a large proportion unusable in the production process. Thus, the increase in crossing utilization, and daily operations, is necessary to avoid a scenario where more ‘categories’ are allowed in, but with reduced quantities for each category.

Most critical for Gaza’s private sector is the ability to export to and through Israel, which is still not permitted. Thus, to the extent there is production under the current circumstances, it is geared towards the local market which itself is struggling to withstand the collapse of its private sector. For Gaza’s economy to revive, it needs to be able to import a large quantity of industrial and agricultural inputs, and export its products and agricultural produce. On July 23rd, the Government of the Netherlands announced that Israel had allowed the import of Dutch seeds for Palestinian flower growers. This represents an opportunity for crops to be grown and exported by the winter season – provided that the closure of Gaza is relaxed.

On June 26th, the Private Sector Development and Trade Sector Working Group of donors asked the Palestinian Private Sector Coordinating Council (PSCC) to survey the Gaza private sector and to provide their immediate needs in order to sustain themselves. The PSCC’s note focused on: the release of 1,790 containers currently held at Israeli ports and storages since June 2007; financial aid to help the private sector cover demurrage costs; increase in imports to 800 trucks per day and removing restrictions on the types of goods to allow for exports; increase in fuel imports to meet local demand; ease movement of businesspeople, and

37 Paltrade.
38 Paltrade, and UN Gaza Strip Inter-Agency Humanitarian Fact Sheet, June 2008. According to Paltrade, in normal times Gaza needs 850 truckloads of imports daily to sustain its economy.
39 The Palestinian Federation of Industries also notes a need for inputs and items to cover the local demand for 120,000 dozens of school notebooks and the same number of writing pens and pencils. Also needed are 110 containers of raw materials to produce school clothing.
40 According to Paltrade, the post-calm increase of humanitarian items from 11 to 30 has not been matched with a commensurate increase in import truckloads into Gaza, nor the usage of the crossings to full-capacity. As a result, imports of certain categories of items have actually decreased.
students, out of Gaza; inflows of currency to maintain banking operations; facilitation of all donor projects providing basic services, particularly water and sanitation; and extension of the fishing zone to at least 12 nautical miles. As of the time of this report, none of these requirements have been met.