An Economic Snapshot of Palestine and the PRDP
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Basic Information:

Gross Domestic Product (GDP): Defined as the total market value of all final goods and services produced within the country in a given period of time (usually a calendar year).

- Real GDP in 2007: $3901 million
- GDP per capita in 2007: $1130
- GDP real growth rates have dropped by 8.38% since the peak of 1999.

Annual Population Growth Rate

- The annual population growth rate is 4%, one of the highest in the world.

Unemployment

- In 2007, just over 45% of Gaza's work force was unemployed while in the West Bank, unemployment stood at 25.5% of the workforce.

Poverty: The official and deep poverty lines for a six-person household (two adults and four children) in the West Bank and Gaza at $572 and $457 in monthly expenditures respectively for 2007.

- Palestinians living in official poverty in the West Bank: 19.1% in 2007.
- Palestinians living in official poverty in Gaza: 51.8% in 2007.
- Palestinians living in the West Bank in deep poverty: 9.7% in 2007
- Palestinians living in Gaza in deep poverty: 35% in 2007

Private Sector Investment (West Bank and Gaza combined)

- Private investment in 2006 stood at about $665 million.
- There is no data to suggest private sector investment rose in 2007.
- This is 11.3% below the 2005 level, and less than half of the 1999 level.

Public Sector Investment (Government capital expenditures)

- In 2007, public investment was USD 306 million, all of it financed by donors, and much lower than rates in the late 1990's.

Consumer Price Index: The overall Consumer Price Index (CPI) for the Palestinian Territory with its 2004 base year (2004=100) reached 124.19 in September 2008, and increased by 10.91% compared to September 2007. In the first nine months of 2008, the average increase of prices was 10.52% compared to the corresponding period of year 2007. The percent change in the CPI is a measure of inflation.

Miscellaneous

- Manufacturing equipment is on average 12 years old.
- Restrictions on Gaza have led to the suspension of 95% of Gaza's industrial operations.

The Paris Donor Conference

On December 17, 2007, ninety countries and organizations met at a conference in Paris to help raise and pledge funds to support the ailing Palestinian Authority over the next three years. Advised and supported by the World Bank and DFID, amongst others, Palestinian Prime Minister Salam Fayyad presented a plan of reform, the Palestinian Reform and Development Plan (PRDP), which the government is using to guide the Palestinian economy from 2008 till 2010.

Approximately 90 delegations attended the Conference, including key political players in the peace process. Arab and Middle Eastern countries, the G8, the 27 EU Member States, major emerging countries (India, China, etc.), the European Commission, international and regional financial institutions (IMF, World Bank, OPEC Fund, Arab Monetary Fund, Islamic Development Bank, etc.), and United Nations members all attended. Speaking at the Conference, President Abbas said he hoped to collect US$ 5.9 million. These funds would be used to establish and run development projects in Palestinian controlled areas over the coming three years, and in essence, to finance the PRDP. By the conclusion of the Conference, donor countries had generously pledged $7.7 billion in funds to support Palestinian institution-building and economic recovery. Of this amount, $3.4 billion was pledged for 2008. This amount included humanitarian assistance to help with the essentials of the daily lives of the Palestinian population, especially in Gaza. The tables below explain who gave how much.

Distribution of pledges for each donor group		
Group	**Amount***	**% of total**
Europe Countries (Including EU)	4093	53.10%
North America	839	10.90%
Arab Countries	1524	19.80%
Other Countries	411	5.30%
Int'l Organizations	843	10.90%
Total Pledges	**7710**	**100%**
*in Millions US$		

Individual Known Pledges	
Donor	**Amount****
UK	490*
European Union	650
US	555
France	300*
Germany	290*
Japan	150
South Korea	13*
Saudi Arabia	500
UAE	300
Norway	140*
*Over 3 years: 2008-2010 ** Millions US$	

What is the Palestinian Reform and Development Plan 2008-2010 (PRDP)?

The PRDP was developed to help reverse the injurious cycle the Palestinian economy finds itself in today. Further details of how we came to be in this cycle are included below. The PRDP aims to reduce and control Palestinian National Authority (PA) government expenditure in order to redirect funds to infrastructure and development projects, with a view to bolstering private sector growth and investment. The PA government does not want the economy to continue to depend on the government for support. Hence, the PRDP contains difficult but arguably necessary steps to turn our economic situation around. Unfortunately some of those steps will hurt in the short term.

Since the tragic events of 2000 and the beginning of the Second Intifada, the Palestinian economy has descended into a severe downward cycle. Israel imposed curfews and closures on Palestinian towns and villages, rendering the movement of goods and people very difficult if not impossible. As instability and violence in the Territories increased, private sector growth came to a standstill and began to shrink, forcing a rapidly growing labor force to look to the public sector for employment. The public sector, i.e. the Palestinian government, began directing funds towards the hiring of employees, as well as increasing government subsidies, which at the time was necessary to prevent an economic catastrophe from occurring. As such, many families came to rely on the Palestinian government for their livelihood. Consequently, there was little money remaining to invest in much needed public infrastructure and development projects. In fact, most such projects ceased. This situation continued unabated, and so we find ourselves in the condition we are in today: not enough private investment, very little investment in infrastructure, negative economic growth rates, high unemployment figures, and a people who are heavily reliant on the government for survival (an average of 5.3 people were dependent on a government employee in 2007). The Palestinian government in turn is now almost completely reliant on donor funding to survive, using those funds to pay salaries and cover daily operating costs.

Where does PA government expenditure go?

Wages for civil servants and security personnel alone make up almost half of total government expenditure. This number has increased by 57% since 2004. Civil service employees account for 53% of the wage bill while security services account for 47%. Within the civil service, education accounts for 47 %, followed by the health sector at 15 %.

Net lending (government subsidies) is another large expense funded by the government. In 2007, net lending comprised the following: 76% was electricity bills paid on behalf of Palestinian municipalities, 11% was water bills, 11% was PA Ministry of Health bills owed to Israeli hospitals, while 2% was payments for sewage and PA Ministry of Agriculture bills owed to Israel for services provided. In plain English, either because of inability to pay on behalf of the consumer or inability to collect on behalf of the municipality, the PA stepped in with the finances to guarantee that Palestinians would continue to receive basic services such as electricity and running water. In short, the PA started to pay the bills to meet the shortfall. It should be noted that Israel has ultimate control over the provision of utilities such as electricity, water, and telephone access. Israel supplies these utilities to Palestinian intermediaries; hence in essence, most of this net lending indirectly goes to the controlling source, Israel.

Pensions also comprise a large portion of government expenditure. In fact, the government pays about 75% of pensions out of its own budget for about 17,000 former employees at the current time. For example, a government worker can collect a pension (about 3/4 of his original salary) after 15 years of work at the age of 55. This will cost the government $165 million by the end of this year alone.

What steps will the PRDP take?*

The first goal of the PRDP is to reduce and control its heftiest expenses: the wage bill, net lending, and pension reform.

The Wage Bill: The government is planning to freeze real wage increases and limit the number of employees to those currently employed (150,000), with up to 3,000 new employees hired annually for the more crucial services. This may not seem too difficult, unless understood in the context of past hiring practices. Acting as an employer of last resort, Palestinian government employment increased from 114,940 to 150,290 between 2000 and 2007. As such, reforms are necessary to control the wage bill, with the PA hoping that these policies will reduce the bill from 27% of GDP in 2007 to 22% of GDP by 2010. They are also hoping to raise productivity and efficiency of those employees. Within the health and education sectors as well, growth in government spending have been fuelled by staffing increases. Hence, the government is looking to control staffing increases, while diverting funds to finance the purchasing of medical supplies, learning and teachings materials, research supplies etc.

Security Services: In order to formulate any policy affecting the security services, accurate information is needed about them. As a result, this year the government is undertaking a sweeping survey of the security services, gathering up to date information on numbers, ages, performances, disciplinary actions taken, duties etc. The government is also hoping to reduce the number of security service members by removing non-compliant officers and offering early retirement to those nearing the age of retirement.

Pension Reform: The government is currently reviewing its current pension schemes, looking into other methods of funding them as opposed to financing them from its own budget as it has done in the past. It will also review pension laws which provide some of the most generous public sector pensions in the world.

Net Lending: As previously mentioned, net lending represents more than 10% of GDP. Much of this is through subsidizing power utilities. A World Bank study found that many municipalities are not paying for utilities due to a lack of enforcement mechanisms and inability to collect payments from residents within the individual municipalities. As such, the government is initiating steps to counter these problems. It will reduce the net transfers caused by electricity arrears, which comprises most of the net lending. It will decrease the salaries of public sector staff. It is requiring that all individuals provide proof they have paid their utility bills before being able to request a municipal service. For those unable to pay due to economic hardship, the government is looking into a progressive charge rate based on income and consumption levels to protect low-income households. It will also consider giving cash payments directly to the poorest families to ensure basic utility services, instead of paying on behalf of the municipality. Installing prepaid and automatic meter reading/payment systems are also being considered. The government is working towards the formation of the Northern Electric Distribution Company in an effort to transfer electricity supply away from the municipalities. Currently, Israel is the main supplier of utilities; hence the government is aiming to negotiate deals with neighboring Egypt and Jordan to supply utilities.

What has been achieved so far?

Almost $1.4 billion in donor funding was transferred to the PA at the beginning of this year. Unfortunately, PM Fayyad said in a recent press conference that it is not enough to support the government in the last quarter of 2008. He also took the opportunity to criticize the Israeli government for not easing its restrictions on Gaza and the West Bank as it had pledged to do. Israeli settlements and their extended jurisdiction over Palestinian territory have resulted in confiscation of over 38% of West Bank land and most Palestinians are excluded from important agricultural areas in the Jordan Valley and other regions due to these practices. An increase in house demolitions continues in east Jerusalem and other parts of the West Bank, which rendered almost 400 Palestinians homeless in December 2007 - February 2008 period alone. Despite promises that checkpoints and barriers would be reduced, their numbers have actually increased. The Palestinian government, as well as the World Bank, IMF, and other organizations, have stressed that no amount of aid and reform will help the Palestinian economy as long as the occupation continues. Economic reform and development should go hand in hand with political change on the ground.

Despite these worsening circumstances in the Palestinian Territories, some changes have been achieved so far this year. A reduction of over 40,000 civil and security personnel was carried out by the end of March 2008 through the cancellation of illegal and unfulfilled contracts, along with a general freeze on salary increases. The PNA has requested greater municipal/local government accountability and responsibility and is supporting the establishment of additional electricity distribution companies which will collect fees for services. Municipalities are to adopt a Unified Chart of Accounts and register fixed assets. These actions have resulted in the increase of payment of utilities, which will decrease overall net lending arrears.

An emphasis has been placed on ensuring transparency, accountability, and rule of law. Improvements on public finance management systems that comply with international standards of integrity and transparency are continuing; the Basic Finance Law was amended and an Office of the General Accountant was established in the Ministry of Finance. This office is supported by a new electronic database, linking PNA expenditures to budgetary appropriations. All funding received has been earmarked for certain budgets, and cannot be diverted elsewhere. All expenditures must be accounted for to guarantee the utmost transparency possible. The PA hopes this will insulate expenditures and financial management from political interference. Naturally, progress updates will be provided to the donors.

In addition, the Cabinet adopted new legislation/policies in the fields of procurement, income taxes, pensions, and money laundering. President Abbas signed a new simplified income tax law, with a maximum marginal rate of 15% for individuals and companies in March 2008. The Customs and Excise Department and the Palestinian Ministry of Finance also launched a major campaign against the undervaluation of imports by traders. A large number of revaluations have been effected which will result in higher tax collection.

An emphasis has also been placed on security. The government has imposed a ban on armed militias in the West Bank. It has also addressed the issue of Palestinian fugitives by securing an Israeli commitment not to target or arrest them, although this is certainly not a blanket commitment for all activists, i.e., it is exclusively for Fatah members, and has not stopped Israel from arresting/killing those who supposedly have immunity. An initiative is underway to enforce law and order by deploying forces in major urban areas. The government has already deployed security forces in Nablus, Jenin, parts of Hebron and other major West Bank towns. Reconstruction of security headquarters is also underway. With these actions, the PNA is hoping to send the message that it is rebuilding, upgrading and reasserting its authority.

With the help and advice of US Security Coordinator Lieutenant General Keith Dayton and EUCOPPS (EU Police Coordinating Office for Palestinian Police Support), the security services are in the process of professionalizing, reforming and equipping themselves in order to carry out their functions in a reliable and effective manner. However, Israel has imposed limitations on how and where security forces can or cannot act, which limits the PNA's ability to bring security to the people and to fulfill its security commitments under the Road Map. Furthermore, recurrent Israeli military incursions severely erode the credibility of the security forces and the government's efforts to restore rule of law and protection of civilians.

Criticisms of the PRDP

There are many individuals within the Palestinian and international community who have criticized the PRDP and its methods. Many criticize the World Bank and IMF's involvement in the plan, claiming that these institutions prescribe the same medicine to every country in economic difficulty (no matter how different the circumstances): fiscal discipline and private sector growth. Both do generally encourage striving for a government budget surplus and minimizing government expenditures, while the IMF often makes the issuing of financial and technical assistance contingent on fiscal prudence. Unfortunately, many governments have been known to do this by cutting government budgets for important social projects and services. This is not to suggest that the PA will employ this method. However, by not taking into account the individual circumstances of a country, requiring a cut in government expenditure will have a harsh, immediate effect on the local population. It should be noted that cutting government expenditures will be even more difficult to do if inflation continues to rise, fed by global problems such as the food security crisis. The following areas are a main cause for alarm: <u>public sector workforce cuts, wage freezes, certificate of payments, and industrial zones.</u>

Mass layoffs are never viewed as a good thing in the short run. Thousands of Palestinians depend on public sector employment. As indicated earlier in this paper, an average of 5.3 people depends on the income of a government employee. The wage freezes that have already taken place have also caused concern, as inflation is hovering around 10%, meaning that real wages (nominal wages minus inflation) will decrease by as much. Another cause for concern is the requirement of certificates of payment, or proof that Palestinian citizens have paid their utility bills before being able to request services such as ID cards, car licenses, building permits etc. This will place those who are having trouble paying such bills in an even harder situation. In addition, the subsidization of electricity and water bills (i.e. allowing these services to continue despite the non-payment of bills) is a central means of survival for thousands of Palestinians living in rapidly worsening poverty. Therefore a reduction in subsidization is not going to be looked on favorably. PM Fayyad's government has pledged to do what it can to ease the effects of its reforms, but that is not enough for some critics. Basically, this situation is likely to get worse before it gets better.

The industrial zones are another area of skepticism. PM Fayyad has said that these zones will promote trade with regional partners, including Israel. Not much information is available about how they will be run, but according to some, including the Boycott, Divestment and Sanctions National Committee, the industrial zones are just another way of guaranteeing cheap goods for export produced by an underpaid Palestinian workforce. Located on the periphery of Palestinian towns, these industrial zones will be funded by local and foreign capital, with Israel effectively controlling who goes in and out. These cheap goods will then be exported to Israel, the Gulf States, and the US. There are also claims that the main trade union body in the West Bank and Gaza Strip, the Palestinian General Federation of Trade Unions (PGFTU), has not yet been given the right to represent workers in the industrial zones. Without a union to represent their rights, it will be difficult to guarantee good treatment, sufficient pay, representation in the event of unfair dismissal, and other rights that should be afforded to workers.

The criticisms continue, but suffice it to say, the main point here is that this pursuit of economic recovery and reform is largely pointless unless Israel ends the occupation in its entirety. All these reforms, conferences and projects all have serious political implications to consider. Many are proposing joint Israeli Palestinian cooperation. While this is a step in the right direction, "The proposed projects take as their starting point Israeli participation in decision-making, and Israeli control over their legal status... [they] are designed to meet the economic demands of the Israeli administration, not those of the Palestinian people." (The Boycott, Divestment and Sanctions National Committee)

Conclusion

Nobody, including international donors and the World Bank, are naïve enough to believe that the PRDP will succeed if there is not parallel movement on the political front, especially in Gaza. The World Bank has repeatedly stated that any tangible success will require the easing of movement and removal of restrictions. If any growth does occur, it will most likely come from the West Bank, widening the economic and political gap that already exists between Gazans and their fellow West Bankers, and increasing the anguish of Gazans. In addition, on the political front, any progress in PRDP measures and other development projects will not contribute to ending the Israeli occupation of the West Bank and Gaza Strip. While Israel may look on a degree of economic stability in the West Bank and Gaza as a positive development (assuming it is achieved despite their impediments), only they can decide to end this occupation.

In a best case scenario, the Palestinian government envisages a situation in which the PRDP is fully implemented, all pledged donor funds are secured, and private sector growth and trade is revived. This requires a recovery in Gaza as a result of a peaceful resolution to the Hamas-Fatah rivalry. It also requires the removal of internal movement restrictions, a system of open crossing points with Israel, and Israeli accommodation of imports and exports into the West Bank and

Gaza. However, even with all this progress, economic growth will still take time to reach positive numbers, just as unemployment levels will take time to stabilize and eventually fall.
On the other hand, the worst case scenario is a continuation of our current situation, with the added burden of a lack of donor funds, leading to the eventual collapse of the Palestinian government. There are few who would wish to witness the economic and political effects of such a scene.
Of course, in all scenarios, nobody anticipated the effects of the global financial crisis that is still ongoing. This crisis may affect our own economy, although indirectly, as we rely on funds from donor states that have been directly affected by the crisis. As Palestinian Planning Minister Samir Abdullah said in a press conference recently, “The global financial crisis will have a direct impact on the financial support from states affected by the financial crisis. This will lead to an imbalance in the government budget.”
Other analysts have written about the impact of the financial crisis on a possible peace deal between the Palestinians and Israel, as funding will be needed to finance different aspects of the negotiations. Even peace has a price, and that price is likely to lie at the feet of the international community. For example, most people acknowledge that a resolution of the issue of the right of return for Palestinian refugees will involve some sort of financial compensation which the Israeli government is unlikely to fund with or without assisatnce. Also, Israel might demand that an early-warning system be set up should it withdraw from the West Bank and the Golan Heights (in the event of a peace deal with Syria). Even if a peace deal is reached, the Palestinian Authority will still need financial support initially to continue building security services and the infrastructure necessary for a successful Palestinian state. Of course, before jumping the gun, Palestine and Israel need to reach the stage where a peace deal is possible first.

*Please note that the issues discussed in this paper do no represent the full and comprehensive spread of issues the PA hopes to tackle with the PRDP. This paper merely highlights the main steps, problems and criticism of the PRDP.

Sources:

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