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PROSPECTS FOR AND PROBLEMS OF THE PALESTINIAN ECONOMY IN THE WEST BANK AND GAZA STRIP

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The state of affairs in the Palestinian Territories, in the West Bank and Gaza Strip, and its effects upon the economic development in these territories has been a source of considerable concern, especially following the Israeli-Palestinian Accord of September 1993. It seems significant, at this time, to shed light on and to explore the potential for development of the Palestinian economy in these territories. In light of the already deteriorating economic and social situations in these territories, and considering the restrictive measures against the smooth operation of the Palestinian economy due to the Israeli occupation, which further complicated and aggravated the situation, this study will examine the existing economic and social situation in the Palestinian economy, investigate the potential for its development and propose alternative options, strategies and policies for its revival and growth.

1. INTRODUCTION

By the year 1993, the situation in the Occupied Palestinian Territories (OPTs) entered a new phase with the Oslo Accords on Palestinian self-rule on the West Bank and Gaza Strip, and the signature of the Israeli-Palestinian Peace Agreement- the Declaration of Principles (DOP) in September 1993. In accordance with the (DOP), the Palestinians assumed control of the Gaza Strip and the Jericho Area of the West Bank on 17 May 1994, and under the terms of the Israeli-Palestinian Interim Agreement, in November and December 1995, Israeli armed forces withdrew from the West Bank towns. In all of these territories, the Palestinian Jurisdiction is now being exercised by the Palestinian National Authority (PNA) through the Palestinian Legislative Council elected in January 1996. It has been agreed that the PNA will manage the civil and economic affairs in the Palestinian self rule areas of the West Bank and Gaza Strip, and that the Israeli occupation will be maintained in the Jewish settlements in these areas, military installations and East Jerusalem until the conclusion of the final phase of the Agreement's talks which has been scheduled for May 1999 to define the final status of the Palestinian question.

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Realising the intricate relation between the economic development and the political situation, this paper attempts to work within the context defined by the political reality of the OPTs in the West Bank and Gaza Strip, and to focus on issues relating purely to the economic development process in these territories. The paper attempts to arrive at a better understanding of the economic development processes taking place in these territories. It aims at presenting an assessment of the economic development prerequisites and needs for sustainable development in the future. To this end, the paper, first, reviews the economic situation in these territories and its evolution over the past 30 years, that is since the start of the Israeli occupation in 1967, and assesses the environment in which the economies of these territories are operating. Then, the paper examines several structural policy reforms for the future affecting the structure of economic development in these territories.

The economy of the OPTs is mainly service-oriented with agriculture accounting for about 30% of GDP, industry about 8%, construction about 12% and services accounting for the remaining 50%. Private sector activity dominates the economy of the OPTs, accounting for about 85% of GDP. The main feature of the OPTs economy is its heavy dependence on the Israeli economy. Until the recent border closures with Israel by the Israeli authorities, more than one third of the OPTs labour force was working in Israel (mostly on a daily compensation basis). The earnings of the Palestinian workers in Israel accounted for more than one quarter of the OPTs GNP. Moreover, almost 90% of the OPTs trade is also with Israel. Remittances from Palestinians working abroad, other than those in Israel, have been another important component of the OPTs disposable income.

Despite the contradictions in the data on the total land area of the OPTs among the different statistical sources, the UN has estimated it at 6257 sq km, of which the West Bank covers an area of 5879 sq km and Gaza Strip covers 378 sq km. By 1993, land under Israeli occupation control had reached 3070 sq km or about 49% of the total area of the OPTs. Out of the total land area, an estimated 2267 sq km was under cultivation in 1966, a year before the Israeli occupation. By 1993, this area has declined to about 1665 sq km, or by 27% of its level before the occupation. Much of this is attributed to the occupation authorities' gradual expropriation of land area and bringing it under their direct control.

The population of the OPTs has grown despite continuous migration over the past 30 years of occupation (at a high annual rate of at least 4%). According to the only population census which has been conducted in the

OPTs by the Israeli military administration in September 1967, the Palestinian population was recorded at 966,700. Out of this, 585,900 was in the West Bank and 380,000 was in Gaza Strip. According to the Palestinian Central Bureau of Statistics, the population of the OPTs as at 31 December 1995 was estimated at 2,267,000, of which, the population of the West Bank including East Jerusalem numbered 1,333,000 and that of Gaza Strip was 934,000. Some 46% of the total Palestinian population in the OPTs were under 15 years of age. While almost 40% of the West Bank's population are refugees, over 65% of Gaza Strip's population are refugees living in eight overcrowded and impoverished refugee camps. The population density in Gaza Strip in 1995 was 2470 persons per sq km, the highest in the world and almost 10 times that of the West Bank of 266 persons per sq km. In addition, it is estimated that currently about 3.5 million Palestinians live outside the OPTs. Some have maintained residency rights in the OPTs and are, in principle, free to return, while the return of the majority of them will be subject to the results of the negotiations between Israel and the Palestinians. Moreover, it is estimated that there are about 135,000 Israeli settlers residing in some 150 settlements that have been built in the OPTs over the years of occupation.

As many structural problems and strategic choices affecting the West Bank and Gaza Strip are quite similar, much of the discussion in this paper treats the two territories together in order to avoid repetition and unnecessary detail. However, there are notable differences that must be kept in mind. In addition to the differences in total land area and population densities and the number of refugees in the two territories, there is also a notable difference in the economic performance of the two territories. For example, the GNP per capita in Gaza Strip amounted to $1310 in 1994, compared with $2175 in the West Bank; investment per capita in Gaza Strip is less than half of that in the West Bank; the physical infrastructure is much worse; the water demand/supply balance is much more precarious in Gaza than in the West Bank; and the dependence on the Israeli market for employment is significantly higher for Gaza than it is for the West Bank.

In addition to the present introductory section, the paper comprises five other sections. Section two provides a brief evaluation of the patterns of economic growth and development in the OPTs since 1967 until the year 1993 by examining the actual trends and underlying determinants of observed economic performance, policies and relations in different periods of time. Section three examines the Israeli occupation economic policies and restrictive measures applied in the OPTs during the years of occupation and their consequent adverse effects on the economic development there. Section four sheds light on the post-peace period (the current situation) in the OPTs. Section five investigates the prospects for placing the Palestinian economy on a path of sustained and independent economic development through examining the priorities of the macroeconomic and the structural policy changes for the future. Finally, section six presents the findings and conclusions of the study.

2. PATTERNS OF ECONOMIC DEVELOPMENT SINCE 1967

2.1. The Past Pattern of Growth

In the period directly following the 1967 war the economies of the OPTs in the West Bank and Gaza Strip developed rapidly up to the end of the 1970s. There has been a substantial rise in income over and above that represented by the recovery of the economies from the severe disruption of the 1967 war. In this period, the rapid growth in the economies of the OPTs continued even when economic growth in Israel and on the world scale began to slow down in the mid-1970s, following the first oil crisis. This was due, at that time, to the increasing employment of Palestinians from the OPTs in the Gulf states. As oil prices increased, so did the remittances of Palestinian workers and transfers from oil-rich Arab countries.

However, the growth in income that occurred in the period between 1968 and 1980 was mainly due to the rapid integration of the economies of the OPTs into the Israeli economy. This integration manifested itself mainly in two important and parallel relationships between the two economies:

First**,** in the early years of the occupation, there was a large scale inflow of unskilled and semi-skilled labour force from among the unemployed of the OPTs into the Israeli economy. At the peak of this movement in 1988 the Palestinian labourers working in Israel numbered about 109400 and were estimated to be over 37.8% of the OPTs' labour force (see Appendix-1a and Appendix-2, figure 2). Earnings of Palestinian workers in Israel rose from negligible levels in 1968 to almost one third of GNP in 1984 (Appendix-1b). These earnings, in turn, generated a high rate of savings and stimulated the domestic economic activity, especially the construction sector.

Second**,** a major trading relationship between the OPTs and Israel has developed parallel to the flow of labour from the territories into Israel and has grown along with the income generated by these new employment opportunities. This trade has operated behind a common high tariff system imposed by the Israeli authorities that has served to limit imports into the

OPTs from outside Israel. Thus, more than 85% of the OPTs' imports came from Israel and more than 65% of their exports went to Israel. While exports to Jordan from the OPTs, permitted by the Israeli "Open Bridges" policy, have only 30% of the total, imports from Jordan have been negligible. Trade with other countries has been negligible, too (ratios are calculated using data in Appendix-1c and Appendix-1d, see also Appendix-2, figure 4 and 5).

These advances mirrored the substantial improvements in income levels and in living conditions in the OPTs during the period 1968-80. The standard of living of the population had measurably improved not only over the pre-1967 level but also over what that level might have been if the income trends of the pre-1967 had continued (Arkadie, B. V., 1977). In this period the growth of income (GNP) in the OPTs was estimated at almost 20% in current prices, and the average annual increase in real per capita GDP and GNP was estimated at 15% and 18%, respectively, also at current prices (calculated using data in Appendix-1b). Since unskilled labour played a central role in the growth, the poor shared in this growth, and as a result, in all likelihood, there was a significant reduction in poverty in this period. Household conditions also improved substantially, with a several-fold rise in the possession of consumer durables and significant increases in access to municipal water and electricity connections. School enrolments also rose during this time (The World Bank, 1993).

2.2. Shocks and Responses

With the end of the regional boom in the early 1980s, the growth in the economy of the OPTs continued, although at a lesser rate, until the onset of the popular Palestinian uprising (*intifada*) in late 1987. The economic situation in the OPTs was weakened, in general, due to the recession which spread in the region during the early 1980s. However, the situation was aggravated by the Israeli economic restrictive measures and policies practised against the Palestinians in the OPTs, as we shall see later in section three. Moreover, due to the close economic links established with Israel, the high inflation rate in Israel in the first half of the 1980s had a negative effect on the economies of the OPTs, where the prices have risen by more than 300% (See Appendix-1e). The Israeli economic policy had inevitably obliged the Palestinians in the OPTs to consume Israeli goods, use the Israeli currency and exchange or convert the remittances which they receive from abroad to the inflation-ridden Israeli shekel.

During that period, agriculture income declined by almost 5%, and export growth stagnated. The OPTs experienced a deficit in foreign trade which reached $504 million in 1986 and accounted for one-third of the GDP. Furthermore, a marked reduction in temporary migration in search of employment outside the OPTs and Israeli labour markets, a return of well-educated Palestinians from abroad, and a continuing high and temporarily growing rate of natural increase were demographic factors that contributed to increasing an unfulfilled need for housing, health care, education and general public services. For Palestinians in the OPTs, the recession meant a drop in per capita income in real terms, a considerable reduction of job opportunities abroad, and a marked deterioration of their living conditions. In the period between 1980 and 1986, GNP per capita increased by only 2.5% and GDP per capita increased by 3%.

The situation was exacerbated after 1987 with the *Intifada*, which caused disruptions in economic relations with Israel. The periodic closures of the OPTs by the Israeli authorities and the Palestinian strikes adversely affected employment and trading activity. Exports fell sharply after 1987 and never fully recovered. In 1988, merchandise exports were estimated at $209 million, compared with $387 million in 1986. The impact of these adverse shocks was further amplified by a tightening up of the regulatory Israeli policies on the movement of goods and people, prolonged delays in the granting of business licenses and permits and strict tax administration measures. As a result, the per capita income levels hardly increased during the 1980s, a major turnaround from the exceptionally rapid growth of the 1970s.

The lower growth rates that occurred in the period between 1987 and 1991 were mainly due to the high growth reported in the OPTs agriculture sector following the *Intifada*, which was stimulated by Palestinian resistance to consuming imported Israeli products and the return of a significant number of Palestinian workers working in the Israeli agriculture sector to work in their lands due to the repetitive closures of the border with Israel during this period. Per capita non-agriculture GDP declined by 12% between 1987 and 1991 (The World Bank, 1993). During the first three years of the *intifada*, the pervasive, simultaneous and repeated use of collective punishment by the occupation power was extremely damaging to the social and economic sectors in the OPTs. In the period 1987-89, although the data is weak here, the standard of living was estimated to have decreased by approximately 50%, consumer spending by 40% and economic activity by 30% (ILO, 1989).

By the year 1991, the economy of the OPTs in the West Bank and Gaza Strip was in a state of crisis. Following the Gulf war in January 1991, there was a substantial reduction in Palestinian employment in most Gulf states led to a significant decline in remittances from abroad. This has been matched with the effectively partial closures of the border with Israel during the Gulf war in the same year. As a consequence, the Palestinian employment as well as trade with Israel fell drastically causing large income losses. Moreover, the reduced purchasing power of the Israeli currency (shekel), which is used as legal tender in the OPTs, adversely affected domestic economic activities. In 1992 there was a substantial rebound of economic activity, fuelled partly by expectations of peace, and partly due to the relaxation of some of the regulatory Israeli constraints. However, a sharp downturn occurred in 1993 mainly as a result of the closure of the OPTs economy by the Israeli authorities in March 1993.

3. IMPACT OF ISRAELI OCCUPATION POLICIES: STRUCTURAL IMBALANCES AND DISTORTIONS

The power of regulating and controlling economic and other activity in the OPTs has been assumed by the Israeli occupation authorities since 1967 through a military government, which has been partially transformed in 1981 into a “Civil Administration”. This authority rules by issuing periodic military orders and decrees, guided by overall or specific policy decisions and orientations emanating from the Israeli central government. By the year 1984, for example, out of 1950 military orders issued in the West Bank and Gaza strip, some 935 (almost half) were directly concerned with economic matters like taxation and customs, banking, money and insurance, agriculture, industry, land and water, labour and other areas (Benvenisti M., 1984). Although some of these orders were adapted or amended versions of Jordanian or Egyptian laws in force before 1967, most of them represented new regulations reflecting Israeli policy concerns.

However, the Israeli occupation economic policies in the OPTs have been aimed at destroying the economy and at arresting any economic development there. In general, Israeli economic policy in the OPTs has been officially stated in 1986 by Y. Rabin, Israeli Minister of Defence at the time, as follows: “There will be no development [in the OPTs] initiated by the Israeli Government, and no permits will be given for expanding agriculture or industry which compete with the State of Israel” (*The Economist*, January 1986, p.3).

In this context, Roy, S. (1995) pointed out three policy methods employed by Israel and applied in the OPTs to secure its economic interests and to block the Palestinian national economic development in the West Bank and Gaza Strip: expropriation and dispossession of Palestinian land and water, coupled with limiting public finance for development; forcing the Palestinians to be dependent on Israel for employment, leading to income without domestic economic development; and a de-institutionalisation policy limiting and/or debilitating Palestinian institutions which could facilitate economic development.

Thus, the economic policies and measures applied by the Israeli authorities in the OPTs can be seen to be based upon three major premises: maintaining the minimum of order in the economic affairs of the OPTs; ensuring that the regulations of economic activity in the territories correspond to the general pattern of relevant policy and legislation in Israel; and most importantly, ensuring that economic activity in the territories does not conflict with or harm Israeli economic interests. As a result, the Palestinians in the OPTs were left with only three options: to take employment inside Israel; to migrate; or to do with a steady decline in their standard of living and give up any hope of development.

3.1. The Impact of Israeli Occupation Policies

Of relevance here is how the Israeli occupation economic policies and measures ultimately make themselves felt in their application and what effects they have upon economic development in the OPTs. In general, the economic sectors of the OPTs have been undermined by Israeli economic policies as follows:

3.1.1. Agriculture Sector

With respect to agriculture, the Israeli policy was proceeding along a number of axes involving the expropriation of land, increasing restrictions on the types and quantities of crops to be grown and exported to the Israeli markets, and control of water resources. The use of land by the Israeli occupation authorities for military purposes, roads, settlements, and other Israeli purposes has adversely affected the agriculture sector in the OPTs. As a result of the expropriation of approximately 60% of the West Bank land and over 40% of the Gaza Strip, the total land area under cultivation in the OPTs has declined by 27% of its level before the Israeli occupation in 1967 (UNCTAD, 1989). Consequently, the contribution of agriculture in terms of output and employment has begun to decline since the start of the 1980s. Another traditional economic activity, fishing in Gaza Strip, has declined during the years of the Israeli occupation due to the military restrictions on specific fishing areas. The Gazan fishermen are limited to a fishing area within 19 miles of the shoreline, an area that is one-quarter of the pre-1967 size (Roy S., 1986).

Since 1967, the OPTs' water resources have been under full Israeli control. By means of military orders and regulations the Israeli Government has been exercising complete legislative, administrative and judicial authority over the OPTs' water resources. During the years of occupation, the Israeli authorities continued to deplete, divert and restrict the use of water resources in the OPTs for the benefit of Israel and its settlements there. Control over the use of Palestinian water resources was exercised, for example, by restricting the number and depth of wells, limiting planting and irrigation and enforcing discriminatory pricing policies. In agriculture, Palestinians were permitted to use only the amount of water allocated for that purpose in 1967. The restrictions on water use in the OPTs ensured the underground flow of water to Israel, supplying between 35 to 40% of its annual water consumption. The Israeli settlements in the OPTs, their per capita water consumption being a multiple of the amount of water allocated to the Palestinians, further contributed to the depletion of the water resources in the OPTs. As a consequence, the health, environment, agriculture and economy of the OPTs were increasingly adversely affected.

3.1.2. Industry

Industry, which contributes an average of about 8% of GDP in the West Bank and Gaza Strip, has suffered especially from the lack of finance, since it is not self-generating in the way that agriculture is, requiring much more in terms of investment, raw materials, technology and labour skills. Subcontracting arrangements have increasingly involved small-scale industries, transformed them into ancillary industries catering to the needs of Israeli industries through subcontracting arrangements. While initiation of new factories has been restricted by the Israeli occupation authorities since 1967 for political and economic reasons, Israeli policy towards industry in the OPTs is such that the special needs of a weak and unprotected indigenous sector with limited markets dominated by a strong Israeli industrial sector are not catered for. Israeli industrial trade policy has worked to ensure that over 90% of the industrial imports of the OPTs originate in Israel. Palestinian industrial exports account for just 2% of Israeli industrial imports. The OPTs have been kept dependent on Israel for both industrial imports and markets, with about 80% of industrial exports going to Israel (Benvenisti M., 1986). In brief, while the Palestinian industrial sector is unable to withstand Israeli competition, it has at the end to compete with Israeli enterprises located in the settlements which enjoy far reaching incentives and subsidies.

3.1.3. Foreign Trade

Over the years of occupation, Israel has developed a policy with regard to trade with the OPTs which resulted in a number of measures having a negative impact on their trading position. The major consideration influencing Israel's policy regarding trade with the OPTs is that Israeli exports should be able to flow freely into the West Bank and Gaza Strip while exports to Israel from these territories should be tightly controlled to safeguard the interests of Israeli producers. For example, Israeli trade restrictions have ensured that the costs of agricultural inputs have increased while the value of crops have fallen. While Israel has at times provided the OPTs' markets for as much as a third of their agricultural production, it restricts its purchases from the OPTs to those crops which can be processed in Israel for sale abroad or which are labour intensive and more cheaply produced in the OPTs. Because Palestinian production is increasingly diverted towards crops which Israel wants and not those which compete with Israeli production, it is subject to prices determined by Israeli purchasers. The non-tariff trade barriers, both in Israeli and Arab markets, dictated political, economic and technical constraints, have restricted the flow of Palestinian products in those directions, and facilitated dumping of Israeli products on the OPTs' market. Due to such policies and other factors, economic and trade relations between the OPTs and neighbouring countries were uneven. In addition, economic and trade interaction within and between the West Bank and Gaza Strip was very limited.

3.1.4. Money and Banking and Public Finance

All indigenous financial institutions of the West Bank and Gaza Strip ceased to function following the territories' occupation by Israel in 1967. Branches of Arab and non-Arab banks and other financial institutions were closed down by the Israeli military authorities and replaced by some Israeli banks and institutions. The military authorities have been entrusted with power over banking and monetary operations, including the licensing of banks and foreign exchange dealings, administrating bank assets and liabilities, closing and/or liquidating banks and establishing the level of credit, interest rates and liquidity. During the years of occupation, the Israeli authorities have issued more than 100 military orders governing banking and monetary activities in the West Bank and Gaza Strip. As a consequence, the financial system has remained both economically and politically fragmented, inadequate in terms of resources, and technically incapable of meeting the growing financial needs of the OPTs.

Concerning public finance, while it is claimed that fiscal laws and regulations prevailing in the West Bank and Gaza Strip prior to their occupation are still in force, a wide range of Israeli military orders and proclamations have created a different situation. The tax system alone has been the subject of more than 177 military orders, all aimed at increasing the Israeli Government revenues in order to meet expenditures by the occupation authorities. In this regard, it is worth mentioning that Government finance statistics on the OPTs were inadequately reported by the Israeli official statistic sources, i.e., the Israeli Central Bureau of Statistics (ICBS). A shortcoming in the data was particularly apparent regarding the public finances, and as no data were published on deficit financing, the extent to which Government expenditures were financed through local and other sources of revenues was unclear.

According to M. Bevenisti's 1986 report, the Palestinians living in the OPTs paid an "occupation tax" to the occupying Israeli authorities after 19 years that was estimated at a conservative figure of $700 million (for West Bank alone) or two and a half times the total Israeli authorities' capital formation in the entire occupation period. This fact refutes Israeli claims that the low level of public expenditure and investment in the OPTs derived from budgetary limitations. If net fiscal transfers of the Palestinians (mostly taxes) had been invested in the territories, rather than added to the Israeli public expenditure, it would have been possible to improve local services significantly, and in particular, to develop local economic infrastructure in the OPTs. As a result of all that, a colonial pattern of public finance has emerged, whereby revenues and expenditures were more or less balanced. In general, the public finance sector in the OPTs has served only a marginal role, if any, in the economic development process as a whole.

As a result of all the above and despite the growth in income that occurred in the OPTs during the years of occupation, there has been no significant economic development in the sense of structural changes in the economy. Due to the restricted Israeli economic policies, the lack of efficient domestic banking and financial system and, consequently, the absence of the necessary domestic investment needs of the productive base, the capacity for long-run industrial and agricultural growth in the territories has not been altered during the occupation years. The traditional economic sectors have gradually given way to areas within the other sectors, which have gradually enjoyed higher rates of productivity and emerged as areas closely linked to the Israeli economy. Examples are constructions and services.

In brief, the nature of the Israeli occupation policies in the OPTs has been to deny any Palestinian indigenous central planning for either agriculture or industry, and to restrict autonomous decision-making with regard to the economic development process as a whole. The development in these and other sectors indicates an increasing alignment of the economic interests of Israel rather than the creation of a viable national economy. The lack of appropriate Palestinian institutions to safeguard the interest of the domestic economy through various policy instruments has further compounded the problems of indigenous economic development and has led to the increasing subservience of the OPTs economy to the Israeli economy.

3.2. Structural Imbalances and Distortions

Taking all the above into account, the economic performance of the OPTs over the past 30 years can be characterised as rapid growth, but with serious imbalances. Specifically, while the current per capita income levels in the OPTs were more than threefold the level that prevailed in the early years of the occupation, this growth has been highly uneven over time and has been accompanied by the emergence of major distortions in labour markets, in sectoral production, in the structure of trade and in the balance between public and private consumption.

In this connection, it is note worthy to mention that on the basis of official statistics (ICBS), the OPTs had a GNP per capita of $1671 in 1991. This GNP was higher than that of Tunisia ($1500), and very near to that of Turkey ($1780) and substantially ahead of Jordan ($1050), Morocco ($1030) and Egypt ($610). However, this overstated the relative economic development position of the OPTs, possibly by a substantial margin, for two reasons. First, the official estimates of the population may be underestimated due to the fact that a population census has not been carried out in the OPTs for 30 years since the first one has been carried out by the Israeli authorities in 1967. Second, and more important in quantitative terms, is the fact that comparisons at the official exchange rates often fail to reflect the relative incomes in terms of real purchasing power because of differences in the prices of goods and services across countries.

However, the International Comparisons Project (ICP) attempts to adjust for this by directly comparing the prices of goods in different countries. In terms of international purchasing power (using prices in the United States as a base), the GNP per capita for Morocco is estimated at $3300; for Tunisia it is $4700; for Turkey $4800; and for Egypt $3600. There is no direct data for Jordan, though on the basis of adjustments made in other countries, its GNP per capita would also be expected to be increased by three to four times (The World Bank, 1993). The OPTs, for which there is also no direct data, will be affected by the high degree of openness to Israeli prices; the ICP estimates for Israel's GNP per capita in international purchasing power terms is only 10 per cent more than the figure at official exchange rates. Accordingly, the adjustment for the OPTs income levels will be substantially less than those in Jordan, Morocco and Tunisia and not above them as the estimates at official exchange rates indicate.

The structural imbalances and distortions of the OPTs economy are manifested in several areas. The most important are: (a) heavy dependence on outside sources of employment for the OPTs labour force; (b) low degree of industrialisation; (c) a trade structure heavily dominated by trading links with Israel and with a large trade deficit; and (d) inadequacies in the provision of public infrastructure and services. In the following, we shall briefly examine the structural imbalances and distortions in these areas.

3.2.1. Labour Markets

Despite the continuous emigration over the years of occupation (at an average rate of 1% per annum), the Palestinian labour force in the OPTs has more than doubled. In contrast, the domestic employment opportunities have grown by less than 25% (The World Bank, 1993). Instead, Palestinian employment grew mostly into two areas: Unskilled work in Israel and higher-skill services throughout the world, particularly in the Gulf countries. The number of Palestinians working in Israel rose to 75000 in 1980 and to 115000 by 1992; these workers accounted for almost 38% of the OPTs labour force in 1988 (Appendix-1a). This employment was wholly in unskilled and semi-skilled work; most of the workers being employed in the construction sector; and wages were around the Israeli minimum wage. Direct contribution to GNP from wage income from abroad, mainly in Israel, rose from negligible levels at the start of the occupation to about $375 million in 1980 and to about $816 million by 1992 (Appendix-1b). The pattern of employment of Palestinians in the Gulf states was quite different. The highest demand in these countries was for skilled Palestinian labour; and the wages earned there were substantially higher than those in the OPTs. It is estimated that about 40000 Palestinians from the OPTs were working in the Gulf countries during the 1973-1982 period (The World Bank, 1993). Although reliable data are lacking, remittances from Palestinian workers in Gulf countries, and elsewhere, have also constituted an important source of income.

It is, then, clear that the external labour markets have played an important role in the economic development and growth of the OPTs over the past 30 years. However, the future prospects for these labour markets do not look promising, which will adversely affect the economic development of the OPTs in the future. On the one hand, the Gulf countries' demand for Palestinian labour has dried up in the wake of the Gulf war. On the other hand, the continuing access to the Israeli labour market has been substantially affected by the deteriorating security situation and the increasing restrictions on the movement of people since the onset of the *Intifada* in 1987.

3.2.2. Production Structure

Due to the heavy dependence on outside employment there was a lack of dynamism in domestic economic activities in the OPTs, particularly in industry and services. For example, with 8 per cent of the GDP, the share of industrial production in OPTs is much below that in other economies with similar income levels. The economy remains predominantly based on small, underdeveloped and sole proprietorship enterprises in both the production and services sectors. The normal consolidation and rationalisation of the industrial sector has not occurred. The combination of the small size of the enterprises, the underdeveloped state of the financial and banking system and marketing services and the lack of infrastructure constrained producers, decreased competition and severely impeded the efficiency of factor utilisation. Businesses support services and institutions, both public and private, have yet to develop to a stage where they can offer the needs of the private sector.

Investment by the private sector in productive assets remained extremely low. While total gross fixed capital formation (GFCF) averaged 27% of GDP during the period 1968 to 1991, construction (mainly in housing) accounted for more than 80% of GFCF in the same period (The World Bank, 1993). The low level of investment in industry reflected a combination of factors, including political uncertainty, tenuous property rights, entry barriers, a restrictive regulatory and taxation environment and the lack of a supportive financial system. Therefore, private sector investments were limited to individual savings and internal cash generation. However, following the relaxation of some of the regulatory and administrative impediments in the early 1990s, there have been some signs of increased investment activity and improved business environment fuelled in 1993 by the expectations of peace. Finally, the growth potential of the agricultural sector has remained constrained by stagnating or shrinking land and water resources and by the asymmetric trade relation with Israel which limited the OPTs agricultural exports to Israel.

3.2.3. Trade Patterns

A major redirection of trade towards Israel and the emergence of a large trade deficit were the main two features of the pattern of trade in the OPTs during the past 30 years. While Israel has become practically the sole trading partner of the OPTs, the share of Jordan in total OPTs' trade declined drastically over this period. Exports to Jordan as a share of total OPTs' exports declined from 44% in 1968 to 15% in 1992. Although Jordan does not impose any customs duties on goods imported from the OPTs, exports to Jordan were constrained by regulatory and security restrictions imposed by Israel, as well as by requirements regarding proof of origin and seasonal quotas on agricultural products imposed by Jordan, especially since the mid-1980s. Furthermore, as a result of the security restrictions imposed by Israel, the OPTs can import virtually nothing from Jordan. The Arab boycott of Israel, as it relates to the OPTs, as well as various impediments to trade with the rest of the world, have also acted to distort the overall pattern of trade in the OPTs. These trade patterns were accompanied by a sizeable and chronic trade deficit, mainly with Israel while the OPTs enjoyed a trade surplus with Jordan (Appendix-1d). Although the trade deficit has been largely offset by incomes of Palestinian workers in Israel, the resulting dependence on a single market makes the OPTs economy vulnerable to shocks, especially because labour flows are subject to political developments in the region.

3.2.4. Public Infrastructure and Services

Despite the impressive gains in private incomes and consumption, the provision of public services and physical infrastructure in the OPTs is highly inadequate. Although the coverage of public services, particularly in the major urban areas, is fairly high, the quality of these services is very low and inadequate. Examples include the following:

1. Due to the limited access to water resources and inadequate investment, the average urban water supply was only 60 litres per capita per day in the early 1990s as compared to 115 for Tunisia, 137 for Jordan and 230 for Egypt (The World Bank, 1993). Water actually consumed was even much less due to deficient distribution systems with high losses in most municipalities.

2. Due to the supply constraints and network deficiencies, current electricity consumption is also very low compared to neighbouring countries like Jordan and Egypt. In 1991, some 138 Palestinian villages had no electricity supply or only a part-time supply. Regulatory constraints on network expansion and on supplies from the Israeli system have forced many industrial users to resort to expensive supplies sources. Because of these problems, all electric utilities in the OPTs are now in an urgent need for major rehabilitation and upgrading.

3. While the length of road network per capita is typical of a country with similar per capita GDP, the physical condition of the roads serving the Palestinian people has deteriorated to the point where, without immediate rehabilitation, past investment may be completely lost (The World Bank, 1993).

4. Education facilities are also in poor condition. Many school buildings require major repairs. Libraries and laboratories are generally inadequate. Universities are too small to be able to provide the facilities required for advanced studies, particularly in physical sciences. The frequent school

closings through the years of *Intifada* have led to a breakdown in discipline and a deterioration in student achievement. The health infrastructure is less in need for repair. However, the OPTs do not obtain the health impact that should be expected from the large expenditure in the health sector.

The inadequacies in the provision of public services have to be seen in the light of the public finances that prevailed in the OPTs as we have seen above in this section. Expenditures in the OPTS by the Israeli occupation through the Civil Administration and the municipalities have been confined to the revenues collected by them. Public sector capital expenditure in the OPTs amounted to about 3.5% of GDP over the 1970-90 period, which is significantly below the average of developing countries and neighbouring countries like, for example, Jordan with government capital expenditure amounting to about 9% of GDP.

4. POST-PEACE ECONOMIC SITUATION

By the year 1993, the situation in the OPTs entered a new phase. After 27 years of occupation, Palestinians are finally getting the chance to determine their own economic destiny. In accordance with the Oslo Accord of “Palestinian Interim Self-Government Authority” and the Declaration of Principle (DOP) signed in September 1993 by Israel and the Palestinians, the Palestinians assumed control of the Gaza Strip and the Jericho Area of the West Bank on 17 May 1994, and in November and December 1995, Israeli armed forces withdrew from the West Bank towns. In all of these territories, the Palestinian Jurisdiction is now exercised by the Palestinian National Authority (PNA) through the Palestinian Legislative Council elected in January 1996. In the four years since the DOP was signed, the PNA formally began to function after the Israeli military occupation had redeployed from the OPTs. The PNA assumed to govern and manage every aspect of life including the economic affairs in the Palestinian self-rule areas of the West Bank and Gaza Strip until the conclusion of the final status talks of the Palestinian-Israeli Peace Agreement which has been scheduled for May 1999.

4.1. The Economic Aspect of the Israeli-Palestinian Peace Agreement

The DOP of September 1993 announced the start of a political process that has begun to change the economic relationships between the OPTs and Israel. With the establishment of the PNA, a series of further agreements between the two sides defined more precisely the gradual assumption of responsibility by the PNA in the West Bank and Gaza Strip. In the area of economic activities and relations between the Palestinian territories and Israel, an agreement was reached in April 1994 on the "***Protocol on Economic Relations between the Government of the State of Israel and the Palestine Liberation Organisation, representing the Palestinian People***" (henceforth referred to as the Protocol or Paris Protocol), and signed by the two sides on 29 April 1994 in Paris. This 60-page document establishes the contractual agreement which will define and govern the economic activities and relations between the two sides during the interim period, specified as five years starting from 4 May 1994. Another agreement between the PNA and Jordan, the neighbouring country with which the OPTs have the strongest economic ties after Israel in the region, was also signed in Amman on 26 January 1995. Finally, following the Israeli-Jordanian peace treaty in 1994, a trade agreement between these two countries was signed in October 1995.

The 1994 Paris Protocol on Economic Relations defines and governs the economic relations and, in part, the economic policies of the PNA with Israel in the following areas of economic activity (see The United Nations A/49/80, S/1994/277, 20 June 1994):

1. Import Policy: Israel and the PNA will have an import policy basically similar in all respects regarding imports and customs. Nonetheless, the PNA will be able to import mutually agreed goods at customs rates differing from those prevailing in Israel, following jointly agreed import procedures. Moreover, it will be able to import goods from Arab countries, in agreed, limited quantities. Agreements will be made for the two customs authorities jointly to operate the border crossing between the two entities.

2. Labour: Work in Israel is essential for the Palestinians to expand their employment opportunities; the guiding principle in this area is to enable mutual movement of labour. The rights of Palestinian workers employed in Israel will be preserved according to arrangements existing in Israel, a social security system being established in the meantime by the PNA.

3. Monetary Policy: The PNA will establish a monetary authority whose main functions will be the regulation and supervision of the banks operating in the Palestinian areas, the determination within certain limits of the liquidity ratios on deposits, the management of foreign exchange reserves and the supervision of foreign exchange transactions. The two sides will continue to discuss the various alternatives for a Palestinian currency. Until then, the New Israeli shekel (NIS) will continue to constitute a legal means of payment in the

West Bank and Gaza Strip side by side with other currencies. To encourage trade, they will mutually allow the opening of bank branches.

4. Direct & Indirect Taxation: The Palestinian Tax Authority will conduct its own direct tax policy, including income tax on individuals and corporations, property taxes and municipal taxes and fees, according to the policy and rates determined by the PNA. The two parties will collect income taxes on economic activities conducted in their respective areas. Israel will transfer to the PNA 75% of the revenues from the income tax collected from Palestinians working in Israel. A VAT system similar to that operating in Israel will be operated also by the PNA. The VAT rates of the PNA will be between 15% and 16%.

5. Agriculture & Manufacturing: Agricultural produce from the Palestinian Territories will enter Israel freely, except for five goods on which agreed import quotas have been imposed for five years: tomatoes, cucumbers, potatoes, eggs and broilers (chickens). There will be free movement of goods manufactured in the area.

6. Tourism: A Palestinian tourism administration will be set up to manage subjects related to tourism in the areas of the PNA. Tourists will move freely between Israel and the areas of the PNA.

7. Fuel: The price of gasoline in the Palestinian areas will be determined according to the PNA's costs in purchasing it, and the taxes levied on gasoline in the areas of the PNA. The agreement stipulates that the prices of gasoline will not fall short by more than 15% of the maximum gasoline price in Israel.

8. Insurance: The protocol deals with two main topics: the full transfer of licensing and supervision authority over insurance business in the areas of the PNA, and an agreement for the compulsory insurance of motor vehicles and the compensation of the victims of road accidents.

4.2. Implementation and Obstacles: The Current Situation

The 1994 Paris Protocol on Economic Relations between Israel and the Palestinians represents a compromise between the political and economic interests of both sides. The reaction to it has been mixed. A Palestinian economic negotiator at the Paris talks, Hisham Awartani, said that " It is an agreement on nothing, ...nearly every article leaves room for alternative interpretation.... Unless the Palestinians display a lot of professionalism in dealing with this agreement, then we will be the losers. The Israelis will not spare any opportunity to exploit the Palestinians, ...the document represents a list of Palestinian concessions, but ‘coming from nothing it is something’, ...Israel has offered an important concession by opening its borders to Palestinian agricultural produce, but its attempt to push the two economies into a ‘tariff envelope’ was both ‘unfair and ridiculous’. The tariffs on goods appropriate for the Israeli economy may not be appropriate for the Palestinians. The labour issue remains an ‘unresolved problem’ which the talks have tackled by ‘sweeping it under the carpet’ (MEED, 13 May 1994, p.20).

On the other hand, the Israeli side is emphasising that not all the details of the future economic relations have been agreed upon, and negotiations will continue under committees called for in the agreement where most of the hard work is still to be done. The Palestinian side emphasised that the implementation of this agreement needs three elements to succeed: security, economic development of the OPTs, as well as, trust and confidence. However, the implementation of the provisions of the Paris Protocol was hindered by two factors: the unexpected lengthening of the negotiations on extending the PNA’s rule to the West Bank; and Israel’s response to the increasingly violent attacks by extremist factions opposed to the peace process in the OPTs.

As soon as the PNA took over in the West Bank and Gaza Strip, the economies of these territories were hit by closures of their border with Israel. Israel closure policies have flown in the face of its commitment to closer economic integration with the Palestinian economy, which was enclosed in the Paris Protocol on economic relations between the two parties. The progressively more severe closures imposed by Israel on the West Bank and Gaza Strip, particularly after the year 1993, not only restricted the flow of workers, but also impeded the movement of merchandise from these territories into or through Israel.

At present, the access of the Palestinian workers to the Israeli labour market is one of the major challenging problems facing the PNA. The Agreement is less than specific on the future of these arrangements, stating that “both sides will attempt to maintain the normality of movement of labour between them”. The policy of sealing the borders of the West Bank and Gaza Strip forms a part of the Israeli long-term vision of a permanent separation between Israel and the Palestinian territories. It has been reported that since 1992, more than 150000 foreign workers from East Asia and Eastern Europe have entered Israel as permanent replacement for Palestinian workers (MEED, 13 September 1996. p. 9).

This policy has had a devastating impact on the Palestinian economy. Before the agreement, more than 100000 workers, or almost 40% of the Palestinian labour force, worked in Israel. In contrast, the fluctuating number of Palestinians allowed to work in Israel now has become less significant for the Palestinian economy and subject to constant uncertainty because of border closures due to the Israeli security arrangements. The flow of daily Palestinian workers into Israel was reduced in 1994 and onward to a level less than half that employed there in 1990 and before. The number has dropped from an average of 115000 in 1992 to about 25000 in 1995. In 1996 unemployment soared and it was estimated that about 50% of the labour force in Gaza Strip and 40% in the West Bank were jobless.

The closures of the border with Israel have also prevented the PNA generating its own revenues and paying its running costs. It has lost tax transfers from Israel levied on Palestinians working there, while the suspension of trade has prevented the PNA collecting import duties. In this regard, a research carried out by the Palestinian Economic Policy Research Institute (MAS) pointed out that Israel is underpaying the PNA by more than $100 million a year by failing to pass on import duties on goods destined for the West Bank and Gaza Strip that are imported through Israeli agents. As MAS pointed out, this sum is equivalent to the entire annual aid to the Palestinians from the United States and the European Union, and almost twice as much as the income tax currently collected by the PNA in the West Bank and Gaza Strip. (*MEED*, 13 September 1996).

Moreover, the economic transactions between the Palestinian territories and Israel are now much more complicated than before. At the time of the occupation, the Palestinian manufacturers could list all their import needs for the year and gain approval from the Israeli trade ministry. In contrast, each individual item has now to be approved by both Palestinian and Israeli trade ministries. Companies which rely heavily on imports have been badly hit by closures. This leaves them unable to export goods and paying storage fees for imported goods which they are not allowed to get from Israeli ports.

After two and a half decades of Israeli occupation, the Palestinians wished to distance their economy as much as possible from the Israeli one. From their point of view, a Free Trade Area Agreement (FTA) with Israel would have been desirable, because it would have allowed them to conduct an independent trade policy while securing their access to the Israeli labour and goods markets. This, however, was not acceptable to Israel for both external and domestic political and economic reasons. But even if it was, given the small size of the Palestinian economy, it is unclear whether its exports will be able to fulfil the generally accepted value-added requirements satisfying the rules of origin under which goods are allowed to move duty-free within an FTA. Furthermore, an FTA would not solve the employment needs of the more than one-third of the Palestinian labour force that used to work in Israel.

On the other hand, the success of industrial parks along the Israeli-Palestinian border line which were proposed as a solution to restricted trade and unemployment, will depend mainly on the willingness of Israeli firms to set up business there. Given the present Israeli perception of the security risks involved, such a proposal cannot be taken for granted. Furthermore, the small size of most Palestinian firms makes it difficult for prospects of Israeli-Palestinian joint ventures. Meanwhile, the advances in the peace process on other neighbour Arab countries' tracks may enable Israeli firms to find alternative sources of suppliers or partners in the region. For example, the Israeli business involvement in Jordan or Egypt will come at the expense of the Palestinian economy and the loss will be felt more in the Palestinian economy in the West Bank and Gaza Strip than the corresponding gain in the two larger economies.

A potential alternative trade and economic relation for Palestinians might be with Jordan, where short distances, long-standing political and business associations, and family ties provide Palestinians with an advantage over other countries in the region. However, at present, Jordanian-Palestinian economic relations are predetermined in part by Israeli-Palestinian ones, which determines, for example, the volume of goods imported from Jordan into the Palestinian territories as well as the terms of their importation. This makes it impossible for the PNA to offer Jordan the reciprocal concessions of a customs union or an FTA. This issue raises the question of the mutual consistency of the economic relations among the three economies in the region. In this regard, Awartani, H. and Kleiman, E. (1995, p.225) stated that "in the absence of a more comprehensive integration between Israel, Jordan, and the PNA, the Palestinian Territories can at most be joined in a customs union with one of the two others, this union then forming an FTA with the third one. The most advantageous arrangement, from a Palestinian point of view, would be an asymmetrical preferential trade arrangement that would allow Palestinian goods freer access to the Jordanian markets than the PNA could grant Jordan under the restrictions imposed on it by the Israeli-Palestinian agreement."

In the area of monetary policy, despite the fact that the future Palestinian currency is one of the main issues which still requires further discussion between the Palestinians and Israel, banking has been the only sector that seems to have been developed relatively without being hit by the closures. Since the signing of the DOP between Israel and the Palestinians, new banks have opened for business in the West Bank and Gaza Strip. By the year 1996, the operation of 16 banks had been approved. Ten of them were either Jordanian or Egyptian, two Israeli and four were Palestinian. The Palestinian Monetary Authority (PMA) approval has also been given to eight new banks, including Palestine International Bank, Arab Palestine Investment Bank and Palestine Construction Bank.

However, the sector as a whole is dominated by Jordanian institutions, in particular, the Arab Bank. Of the estimated $1200 million currently deposited in the banks in the West Bank and Gaza Strip, about $800 million is with the Arab Bank which currently has 12 branches and employs almost 600 staff (The Palestinian Monetary Authority, 1996). In this connection, it should be mentioned that the plans for a PMA have come too late to control the development of banking operations in the West Bank and Gaza Strip. Furthermore, the economic accords signed separately by the PNA with Jordan and Israel have already assigned the roles for the Central Bank of Jordan and Central Bank of Israel in supervising operations in the Palestinian territories. The issue is still subject to further negotiations, but the two central banks are likely to maintain a strong presence as long as the banks in the West Bank and Gaza Strip use the Jordanian dinar and Israeli shekel. Moreover, the Israel-Jordan joint declaration signed at the end of July 1994 made no concessions to Palestinian concerns. The Palestinians were not even consulted about the Israeli-Jordanian agreement announced on the 16th August 1994 allowing Jordan to export $30 million worth of goods annually to the West Bank and Gaza Strip. All these issues lead to some worries on the Palestinian side. Yet, Palestinians recognise that Jordan is likely to be their main Arab trading partner and an essential link with the rest of the region.

It has been, then, clear that most aspects of the economic arrangements between Israel and the Palestinians are subject to further negotiations between the two parties, as well as with Jordan. However, the implementation process is going very slowly due to the lack of commitment on the part of Israel which always attempts to put impediments and obstacles in front of the Palestinian negotiators to prevent the PNA from achieving any independent economic development plans and programmes in the Palestinian territories.

On the other hand, at the time when the economic situation still deteriorated due to the continuous instability in the political and security conditions and with the lack of Israeli commitment to all the provisions of the Paris Protocol on economic relations between the two sides, hopes that the PNA's budget deficit could be closed by the end of the 1997 have evaporated. The PNA's budget shortfall for 1997 has been forecast to be about $126 million, almost twice the 1996 deficit and $74 million more than predicted at the start of the year. In this regard, observers pointed out that unless the Israeli closures policy eases significantly, the PNA will be running a deficit in its budget for the foreseeable future. In this case, donor funds will have to be used to close these deficits at the cost of urgently needed development projects (*MEED*, 17 January 1997).

Therefore, while the promise of $2400 million foreign aid, raised at an International Donors' Meeting in Washington in October 1993 for the first five years of self-rule, generated widespread hopes of an economic restoration in the West Bank and Gaza Strip, these funds have been diverted from long-term development projects to support the running costs of the PNA and emergency programmes to alleviate the chronic unemployment caused by the Israeli border closures. More important, while the PNA has relied on donors to help pay its running cost, investment in the West Bank and Gaza Strip has been left largely in the hands of the private sector. But at the same time, political uncertainties and border closures have certainly dampened the enthusiasm evident among the Palestinian investors and the uncertainty about what the future holds continues to preoccupy private business.

Taking all the above into account, and in such a region with high political and economic uncertainties, it seems that the maximum potential form of economic integration among Israel, the Palestinian, and Jordan in the foreseeable future is investment in common infrastructure projects and, more generally, in joint business ventures. However, Israel's interest in such projects seems to be a political one in which a common infrastructure facilitates the normalisation of its relations with Jordan and the Palestinians, as well as with the other Arab countries in the region. The interest of the Jordanians and the Palestinians, on the other hand, lies more in the hope of having employment-creating projects financed by regional and international aid in addition to the benefits from the Israeli high technologies.

However, in all of these countries, participation in such projects will be a political choice made at the governmental level with small chances to be available to the private sector to play its role in the integration process in the region. Moreover, while the present obstacles on the way of the peace process might delay these decisions, most of these projects may take a long time to come into being, especially if they depend on international financing and because of the small size of the participating economies. So far, and despite the obvious advantages of skills, expertise and business ties accumulated by all the three sides, there is little sign of joint private business ventures established by Jordanian and Israeli firms, and even less between Israeli and Palestinian ones. Palestinian and Jordanian business people seem very sensitive to the popular political opposing of full-fledged normalisation of relations with Israel until major political issues are tackled. These issues mainly include the future of Jerusalem, the settlement of Palestinian borders, and the resolution of the refugee question; all of which will not be settled for a number of years to come. Therefore, the prospects of closer economic integration between Israel and the other two sides seem to be unlikely in the near future.

5. PROSPECTS FOR FUTURE ECONOMIC DEVELOPMENT

In the context of the Palestinian economy in the West Bank and Gaza Strip, it is worth, at the outset, highlighting three main limitations to the task of investigating the prospects for future development and for changing the direction of the economy towards one of sustained growth.

First, in discussing the economy of the OPTs, non-economic factors work against an analytical approach which might lead to a greater understanding of the dynamics of the economic situation and the process of development in these territories. Mainly, the situation in the OPTs does not allow a clear-cut identification and analysis of economic problems, where the presence of the foreign occupation force and its intervention in most aspects of daily Palestinian life, including the economic aspects, has created conditions, over almost three decades, which subject the functioning of the economy to a variety of non-economic factors in addition to those often experienced in the usual process of economic development. Therefore, the application of traditional tools and concepts of conventional economic analysis does not always provide reliable results and may lose some of their relevance when applied to a context whose unconventionality arises not only from the occupation, but also from historical factors which have created an entity like the OPTs.

Second, with respect to the statistical data on the economies of the OPTs, it should be mentioned that there are serious data gaps and inconsistencies, and, sometimes even contradictions among different sources, especially, between the Palestinian and the Israeli sources. This makes it difficult to know the real and accurate economic trends. The picture becomes gloomier when we realise that Palestinian as well as international sources are mostly based on those of the Israeli official statistics. Before the establishment of the Palestinian Central Bureau of Statistics (PCDS) in 1993, almost all the data on the OPTs were, directly or indirectly, from official Israeli sources (ICBS). A population census has not been carried out in the OPTs for 30 years, since the first one carried out by the Israeli authorities in 1967. As a result, most of the demographic and labour force data are extrapolated and estimated on the basis of sample surveys, the reliability of which are undermined by problems of nonresponse, especially since the onset of the *Intifada* in 1987.

Third, and more importantly, a number of key issues bearing upon the future development of the OPTs (e.g., the allocation of land and water resources, the disposition of Israeli settlements in the OPTs, the future status of expatriate Palestinians, the territorial issues surrounding Jerusalem and, most importantly, the nature of the proposed "self-governing" arrangements for the OPTs) are still the subject of the ongoing bilateral negotiations between the Israelis and the Palestinians on the implementation of the Israeli-Palestinian Peace Agreement. The resolution of these issues is likely to be based primarily on political and security considerations between the two parties and in the region as a whole.

In general, investigation of prospects for future development could be carried out at two different analytical levels. First, an investigation approach through **a quantitative framework** which usually provides a rough estimate of the external and domestic resources together with the time-span required to place the economy on the road to sustainable growth based on specific various scenarios. To give an example of such an approach, a reference may be made to the UNCTAD's 1994 study of "*Prospects for Sustainable Development of the Palestinian Economy in the West Bank and Gaza Strip, 1990-2010: A Quantitative Framework*". In the Palestinian context, however, due to the three main limitations mentioned above, this analytical approach will not be used here. The second approach, which is the one used for the purpose of this paper, is **a policy investigation analytical approach** focusing on the prerequisites of macroeconomics and structural policy changes in the fiscal, financial and trade systems needed throughout the different stages of sustainable development process in the OPTs, particularly in the short run.

5.1. Toward Independent Palestinian Economic Development

The economic environment prevailing in the West Bank and Gaza Strip before 1994 has adversely affected the main issues of economic development in these territories such as access to natural resources, financial and business activities, the composition and direction of foreign trade, as well as, the physical and social infrastructures. This, in turn, was reflected in major distortions and structural imbalances in the Palestinian economy as we have seen in section three above. Moreover, the absence of national central planning regarding the economic development process over the long years of the occupation has further compounded the problems of indigenous economic development.

When it took over in the West Bank and Gaza Strip on May 1994, the PNA was confronted with a difficult social and economic situation in these territories. In addition to the severe short-term economic and social problems, the West Bank and Gaza Strip also face fundamental long-term constraints to achieving more rapid economic growth through higher private sector savings and investments. High rates of unemployment, insufficient infrastructure and the lack of economic institutions, which initially included the absence of a developed banking system, as well as trade procedures and practices, that have increased the cost of private sector activity, were among the more important challenging problems of economic development facing the PNA in the West Bank and Gaza Strip.

Understandably, then, the situation in the West Bank and Gaza Strip calls for formulation of a comprehensive programme for rehabilitation and reconstruction of the economy. Like any programme for economic revival and reconstruction, it needs to include three elements: a set of well-defined objectives, a concise evaluation of relevant constraints and opportunities, and a co-ordinated set of policies and strategies that could be adopted to achieve the objectives envisaged. However, 27 years of Israeli occupation of the West Bank and Gaza Strip means that the development process in these territories will be very different from the ones being pursued in other parts of the region. In general development looks at raising the levels of income, but in the case of Palestine, it is important to correct the dislocations and the structural imbalances as well as raising living standards. Therefore, the economic tasks facing the PNA are vast in scope and complex in nature, requiring competent, skilful, and experienced management.

Currently, the PNA is still dealing with the major three problems which have been considered as the most urgent tasks that require immediate action to be taken at the time when the PNA took formal control over the West Bank and Gaza Strip. These problems are: building Palestinian national institutions, dealing with unemployment, and rehabilitation of the deteriorated physical infrastructure. In this regard, particularly in a situation like that of the West Bank and Gaza Strip, it is important to understand that these three tasks are related to each other, and have to be tackled simultaneously. The capacity of the PNA to create effective institutions to safeguard the interest of the domestic economy through various policy instruments depends to a large extent on the credibility of these institutions, which in turn requires a fundamental improvement in the economic situation. On the other hand, improving economic conditions depends on increasing investment in the productive sectors, which in turn requires an institutional framework able to supply a regulatory environment, the basic infrastructure, and essential public services.

The interaction of these tasks, combined with the availability of foreign aid, might induce the PNA to deal with them as a single issue, and to embark, in the short run, on a programme of creating institutions that employ people directly. To achieve institution-building and alleviating unemployment, priorities should be directed towards activities that satisfy the double requirement of generating productive employment, while expanding the infrastructure that support expanding the capacity of the private productive sectors. In other words, the focus of the PNA's development programmes in the short run should be to expand the productive sectors of the economy in order to generate enough production and trade activities to absorb the labour force. This approach resulting in a structural transformation, whereby the Palestinian economy should be able, in the long run, to substitute exporting goods for exporting labour and gradually reduce its dependence on foreign aid.

Accordingly, among the most important projects should be, for example, those which increase agricultural resources. These include programmes of land reclamation aimed at increasing the area suitable for cultivation, increasing the supply of water by maintaining the old wells and drilling new ones. Similarly, stimulating industrial activities requires increasing the supply of electricity, improving transportation and communications facilities by making large investments to enhance such infrastructure projects. Meanwhile, improving and modernising the education and health systems will have direct implications for the success of social development and economic performance in the medium and long run terms.

However, in the early stages toward independent Palestinian economic development in the West Bank and Gaza Strip, the private sector alone will not be capable of generating the savings needed to finance the investments in development projects. Therefore, external financial resources, both official and private, will have to play a leading role in the early stages of the development process. Because of the central role assigned to foreign aid in the overall development process in the West Bank and Gaza Strip in the short term period, certain macroeconomic and readjustment policies need to be formulated and implemented to deal with some of the possible negative aspects of foreign aid in the development process, especially the tendency of using aid funds as a substitute for national saving and not as a supplement to it.

A considerable flow of foreign aid into an economy having limited absorption capacity, like that of the Palestinian one, threatens to bring about a rise in the general level of prices (inflation), and a change in the relative prices of tradable and non-tradable goods. In turn, these adverse effects have a harmful impact: they reduce the competitiveness of the export sector and increase the problem of import dependency. Equally important, since external financial resources will be transferred in the form of project aid, there is a potential problem of co-ordinating the different projects, especially since they are financed by different bilateral and multilateral sources. This has been evident from the experience of many developing countries that have used foreign aid in a major way to finance their development efforts. In many cases, foreign aid at the macrolevel had no significant impact on growth despite the fact that at the microlevel the majority of the financed projects have shown profitable economic results. This concern is often termed "the micro-macro paradox". In other words, foreign aid transferred through separate projects has the potential of leading to a situation where the total is less than the sum of its parts. This paradox reflects also the overlap among the projects (UNCTAD/ECDC/SEU/6, UN, New York, 1994).

To avoid such possible negative impact of foreign aid, it is important that the PNA adopt a comprehensive intersectoral development programme, and negotiate with the donor countries according to the priorities of the programme, which should reflect the sequencing of the different stages in the development process. However, while doing so, the PNA should be aware of the following two related issues: (1) public expenditure or foreign aid will have more appreciable positive impact on the economy if the private sector is free and able to function in a productive competitive manner. Thus, the ultimate success of the development efforts depends on the extent to which they facilitate economic growth in the private sector; (2) the long-run side effect of the early stages of rehabilitation and reconstruction which might threaten to make the PNA the largest employer with huge running cost and bureaucracy that creates misallocation of resources between the private and the public sectors.

Taking the above into account, the development efforts of the PNA during the short-run period should be sharply distinguished from the permanent functions of the public sector until the economy achieves sustainable growth. At that point, the PNA's institutions as a public sector should be able to carry out its function of supplying the public goods and services and offering the suitable regulatory economic environment and policies (taxes and subsidies) to enhance the role of the productive private sectors in the development process. Equally important, the PNA should have a role in smoothing the short-run fluctuations through an appropriate mix of fiscal and monetary policies, and in directing growth through its employment, commercial and industrial policies. The role of these economic policies will have a special urgency in the immediate future as we shall see in the following section.

5.2. Macroeconomic and Structural Policies for the Future

The main theme so far dominating the analysis of the current structure of the Palestinian economy has been reflected in the fact that this economy suffers from a chronic incapacity to create enough jobs to employ the labour force, generate enough saving to finance investment, and produce enough exports to pay for imports. Consequently, the development efforts need to be directed at creating an engine of growth including activities which absorb the increases in the labour force, generate income with part of it to be saved and invested in development projects in order to close the investment-saving gap, and export part of the increased output to close the trade gap.

At present and in the near future, the problem in the labour market could be eased considerably by the availability of employment in the Israeli economy. Similarly, the shortages in savings to be invested in development projects could be reduced substantially by external aid. However, employment in Israel cannot be sustained at significant levels in the long run and external aid will certainly dry up, eventually. Accordingly, in the long run, the Palestinian economy should function without the support of these two sources. Therefore, the development efforts, carried out now by the PNA, should utilise these two external sources in such a manner as to ensure the creation of replacements. In other words, these two sources should be used to increase the capacity of the productive sectors, and enhance saving, rather than finance consumption and imports.

Guided by these considerations, which may define broad national policies in the short run, achievements could be made possible by translating them into the following specific ones: accelerating private investment, promoting exports, reducing imports by substitution rather than compression, switching demand from consumption towards investment, and expanding government investment expenditures. Undoubtedly, implementing these strategies and ensuring that they achieve sound results require a radical change in fiscal, financial, and trade systems and policies, as well as other structural transformation policies related to the productive sectors, as follows:

5.2.1. The Public Finance Sector

The success of the development efforts mentioned above in this section depends to a great extent on the ability of the PNA to mobilise resources for both private and public sectors investments. Such a task requires an effective functioning of the public finance sector. However, the structure of the existing public finance sector, particularly the tax system, is not suitable for the Palestinian economy at the present stage of its revival and growth. In fact, the present system of public finances is responsible for many structural distortions and imbalances that have affected the development in the Palestinian economy in the past. It explains the poor quality of physical infrastructures over the years of the Israeli occupation and has had a discouraging effect on business activities and investments in general.

Reviewing the traditional functions of the public finance sector in any economy, particularly in developing economies, leads to recognising the urgency of each function in the Palestinian economy for the following considerations:

First, the role of the public sector as the supplier of public goods and services assumes a greater importance in the Palestinian case because of the neglect of the physical infrastructures and social services over the last 27 years of occupation. A considerable improvement in these areas is essential for creating a supportive environment within which the private sector can smoothly operate and expand.

Second, the role of fiscal policy, as a tool to support the development process, by stabilising short-run fluctuations and achieving growth-oriented adjustment, becomes critical in the Palestinian context due to the fact that the tools of monetary policy will not be effective in this period because of the absence of a national currency, and until the PMA can gain sufficient experience with the use of some tools of monetary policy.

Third, the role of the public sector in distributing income among individuals and regions is also essential in the Palestinian territories due to the notable difference in the standard of living between the West Bank and Gaza Strip, and the general problem of poverty caused by high rates of unemployment, especially in the last few years.

Guided by these considerations, reforming the **tax and public expenditure systems**, the main components of the public finance sector, necessitates the getting rid of all the negative aspects of the present system, and at the same time acquiring those positive qualities needed to make the public sector a leading force in promoting economic and social development activities.

At present, **the tax system** as a whole includes 25 taxes of 16 different types. A single firm has to collect and/or pay 13 different types of taxes. As for the direct taxes, the income tax structure is very similar to that of Israel whose per capita income is over 14 times greater than that of the Palestinian economy. Furthermore, the top marginal tax rate in the Palestinian territories is 48% as compared to 33% in the United States. As for the structure of indirect taxes, at present, the VAT rate is identical to that in Israel (17%) and according to the Paris Protocol cannot be reduced below 15% in the transition period, despite the great differences between the levels and stages of development in the two economies (George T. Abed and Abdelali Tazi, 1994). These and other features of the structure of the existing tax system suggest that the reforms should be in line with the following major criteria:

(1) In general, efforts should be made to simplify the way taxes are assessed, processed, and collected, so as to reduce both the cost of tax administration and tax evasion. Accordingly, the tax system should be redesigned to bring about the objectives of efficiency, equity, and macroeconomic stability, so as to become an effective instrument of economic growth and social development. In doing so, high importance should be given to restructuring the income tax and the VAT.

(2) Having a large number of taxes usually increases their administrative cost, and may increase distortions, so reducing economic efficiency. Accordingly it is suggested to cut the number of taxes. The experience of both developed and developing countries has shown that high marginal tax rates increase the incentive to evade, and countries with top marginal rates higher than those prevailing in advanced industrialised countries often suffer from capital flight (UNCTAD/ECDC/SEU/6, UN, New York, 1994). Equally important, is the simplification of the business taxes and a reduction in their rates. These changes would integrate the two components of the direct tax system (personal income tax and business tax), and encourage investment while preventing tax evasion.

(3) In restructuring the indirect taxes, especial attention should be given to the VAT. The 15% of the VAT is a very high rate for the Palestinian economy in its present state of economic development. The rate should be chosen so as to foster its advantages without losing other objectives of the tax system. A much lower rate may be considered more appropriate from the viewpoint of equity and growth considerations.

(4) In the immediate and short term, the proper functioning of the tax system is highly important, since taxes are likely to serve as the primary sources of the PNA revenue in addition to external foreign aid. Therefore, taxes have to play the double role of raising a reasonable amount of revenue, that increases with the growth of income, and, at the same time, encouraging private saving, which also grows with income. In this case, the need for external aid will be reduced only if the sum of private and public saving grows proportionally with income, and gradually finances a greater part of total investment.

Broadly speaking, these are the proposed requirements of change in the structure of the tax system. However, a comprehensive reform of the system requires more detailed studies dealing with issues of revenue yields, equity, and efficiency, which are constructed on more concrete assumptions regarding trade relations and tax harmonisation with the neighbour countries in the region.

As for the **public expenditure system**, the need for organising the expenditure side of public finances is not less urgent than the task of tax reform. Prior to 1993, all matters relating to public expenditures and government budget were the responsibility of the Israeli authorities. The preparation and implementation of the budget was carried out without the participation of or consultation with the Palestinian people. In the late 1980s and early 1990s, the total taxes paid by the Palestinian people in the OPTs and transferred to the Israeli authorities have been estimated at around 18-24% of GDP. At the same time, the level of public expenditures was less than 15% of GDP, which is very low compared to other countries (The World Bank, 1993). Accordingly, many public goods and services which are usually supplied by the public sector in most countries, were provided by the private sector, non-governmental organisations (NGOs), and the United Nations Relief and Work Agency (UNRWA). This is an indicator of the very small public investment expenditure and low level of government involvement in the economy.

Taking these distortions and imbalances of the previous system into account, and due to the huge institution-building and construction activities carried out and supervised by the PNA at the present, and with the relatively large amounts of external aid (see Appendix-3b), the accountability and efficiency of the expenditure side of public finances acquires a critical economic and political importance because of the uncertainty surrounding the future of the peace process. Donors, for example might find conditions too difficult to continue their support; they are looking for specific movement in both the political and economic spheres over the near future.

In order to lay the foundation of an effective public expenditure system, the PNA has indeed completed the work on organising and staffing Palestinian employees in the various public sector departments as a replacement for Israeli staff in the past Civil Administration. According to some estimates, this has involved around 2000 new employees (The World Bank, 1994); though actual developments since 1994 indicate an even greater increase in the public sector employment. This relatively large expansion in the public sector employment is justified by the fact that the new Palestinian administration will have to carry out the usual government activities in addition to reconstruction programmes and other activities in the transition period including the administration of the new Palestinian police force, which is estimated to have reached at least 15000 persons by the end of 1995.

Currently, the PNA intends to consolidate its fiscal position, after weakening since 1993 owing to the disruptions in tax administration associated with the transfer of fiscal authority. With the improvement in revenue performance as a result of the PNA's initial fiscal institution-building steps and due to strengthened domestic tax collection, the PNA intends now to restrain the growth of recurrent spending to contain its budget deficits of 1993 (see Appendix-3a and Appendix-3c) and to achieve budget balance by the end of 1998. The establishment, in 1996, of Offices of Central Budget, Treasury, and Internal Audit at the Ministry of Finance, as well as the channelling of fiscal receipts and expenditures through a centralised account, should strengthen the PNA's efforts to resist increased current spending. In this connection, the breakdown of the budget into current and development items should take into consideration the present and future needs of the public sector as an important tool to support the development process. In the next few years, the PNA has to increase public expenditures with respect to development expenditures, especially in such fields as education, health, and municipal services, in addition to public investment projects in all areas of infrastructure.

5.2.2. The Monetary Sector

Undoubtedly, assessing the potential of the public sector within the context of the PNA's efforts of restructuring the public finances depends on restoring the monetary sector which has suffered severely during the 27 years of Israeli occupation. It will be hard for the PNA to achieve any success in reforming the tax and public expenditures systems, as well as reviving the trade flows and activities, without parallel major transformation efforts in banking and other financial institutions to facilitate the smoothness of financial transactions. Generally speaking, the whole restructuring effort cannot be carried out successfully without creating sound financial institutions to perform the essential functions of supplying liquidity, encouraging savings and investments, and facilitating the role of both public and private sectors in the overall development process.

In fact, the last three years have witnessed radical developments in this sector, through renewing old financial institutions and establishing new ones. The establishment of the Palestinian Monetary Authority (PMA) and the gradual removal of the harmful Israeli restrictions of the past have facilitated the achievement of the following three distinguished steps towards the revival of the sector as a whole: (1) the return of the Arab banks to operate in the West Bank and Gaza Strip; (2) the establishment of locally owned new banks and investment companies with their own capital; examples of these two developments have been mentioned in section four above; and (3) the starting flow of both expatriate Palestinian capital, and Arab and international capital to invest in the West Bank and Gaza Strip. The establishment of the following two institutions could be mentioned as examples: the Palestinian Development and Investment Company (PADICO), founded by a group of Palestinian and Jordanian businessmen, and the Palestinian Arab Investment Bank (PAIB), which is a joint venture of international, Arab, and Palestinian capital (MEED, 13 September 1996).

The radical developments in the commercial banking activities since 1994 have resulted in a significant increase in total bank deposits, reflecting a shift in money holding from cash to bank deposits, and indicating that Palestinians have started to bring home their bank deposits in other countries. However, total bank loans have not yet responded to this increase in deposits. The ratio of loans to deposits is still very low, estimated by the PMA at the end of 1995 at 46% in the Gaza Strip banks and 25% in banks in the West Bank. The comparable ratios for Jordanian and Israeli banks were 80% and 86%, respectively. The relative high ratio for Gaza Strip banks was due to loans extended to the PNA's institutions there (The Palestinian Monetary Authority, 1996).

Despite these recent developments in banking activities and the new financial institutions, it is in fact too early and hard to assess the potential of the monetary sector and its ability to play its role of supplying the complementary services needed by all other economic activities within the context of the existing situation, and the changes expected in the near future. In this context, it is important to emphasise that while the activities noted above are essential to the process of building a sound financial sector, their ultimate success depends, in great part, on the direction, co-ordination, and supervision of the PMA and its potential power within the monetary arrangements of the transition period, as specified by the Paris Protocol.

The protocol has assigned many functions to the PMA very similar to the traditional responsibilities of a central bank, designating the PMA as the supervisor and controller of the financial system, and as banker to both the PNA and the commercial banks (see Article IV, Items 5 and 4 of the Paris Protocol, United Nations 1994). Accordingly, the ability of the PMA to perform some of these functions depends in great part on its ability to control the monetary base (high powered money, which is the sum of currency held by the public and reserves of commercial banks and usually held at a Central

Bank). In other words, the PMA needs to be able to satisfy the public demand for currency, as well as the banks' demand for reserves. At present, however, this power is severely restricted by the absence of a national Palestinian currency and the commitment that the liquidity requirement on the shekel (the Israeli national currency) accounts be linked, according to the protocol, to that used in Israel (see Article IV, Item 11 (6)).

The inability of the PMA to exercise the traditional control of a Central Bank over the monetary base implies that it has no control over the effects of changes in both demand for and supply of money. In such a situation, a major excess demand for reserves can only be met by borrowing heavily either from Jordan or from Israel, depending on which currency is demanded (both the Israeli shekel and the Jordanian dinar are legal tender during the transition period). In doing so, the PMA will place a burden on the fiscal system while its ability to manage public debt is restricted. Moreover, there is another problem associated with the use of a double currency standard reflecting in currency mismatching. This problem stems from the fact that commercial banks might find themselves with liabilities mainly in the appreciated currency while thei assets are in the depreciated currency. The risk of this will inhibit the commercial banks from accepting short-term deposits and extending loans over longer terms.

Obviously, then, the role of the PMA in using monetary instruments to counterbalance the short-run fluctuations, and to effect long-run readjustments is severely undermined. It should be apparent, therefore, that improving the monetary arrangements after the passage of the interim period envisaged in the Protocol, requires first, and foremost, ***the movement toward a single currency standard.*** The question, then, is which currency standard should be adopted?. Within the context of the existing situation, and the changes expected in the near future, the following alternative currency arrangements can be envisioned: (1) adopting an independent Palestinian currency; (2) adopting the Jordanian dinar; (3) adopting a Palestinian currency in a currency union with Jordan; (4) adopting a Palestinian currency in a currency union with Israel; or, (5) adopting a Palestinian currency in a currency union with Jordan and Israel.

Considering the historical, political and economic dimensions of the relations among the three economies in the region, our argument is that only the second and the third options constitute reasonable choices. This argument is supported by two considerations: first, the Palestinian interest is not served by a completely independent currency in the foreseeable future because of the likely initial low level of credibility of a new currency in the next stages of economic development in the Palestinian economy; second, a currency union with the Israeli shekel is not in the interest of the Palestinian economy looking for future economic independence away from the Israeli economy after 27 years of Israeli occupation. Accordingly, the Palestinian economy will be best served either by adopting a national currency that is tied to the Jordanian Dinar in a currency union with Jordan, or by retaining the Jordanian Dinar as the only legal tender, as it was in the West Bank before the occupation in 1967.

The argument stated above stems from the fact that the economic prerequisites representing compatible structures and stages of economic development necessary for a successful single currency area do not exist between Israel and the Palestinian territories. These include: factor mobility of labour and capital between the two member countries, similarity of economic structures, and an environment where shocks are common rather than country specific. It is more likely that capital and labour would be much more mobile between Palestine and Jordan than between Palestine and Israel. This is because both labour and capital markets in Jordan are relatively free and have strong ties with Arab markets in the region including the Palestinian markets, while in Israel they are to a great extent controlled by the government, and have strong ties with European and North American markets. The Israeli Government's domination of the capital market explains why, over a period of 27 years of occupation, there was no appreciable flow of Israeli private capital to the Palestinian territories. Similarly, as we mentioned above the Palestinian employment in Israel cannot be sustained at significant levels in the long run due to the fact that it is determined mainly by the economic conditions in Israel and tied with the uncertainties in political and security conditions. More important than the likely low factor mobility between Israel and the Palestinian territories is the great dissimilarity between the structure of their economies.

By contrast, the situation is very different in the case of Jordan and the Palestinian territories. The prerequisite conditions necessary for a successful single currency area combining together Jordan and the Palestinian territories in a currency union are likely to prevail in the foreseeable future. Despite the important differences between the two economies, reflecting the past 27 years of separate development and barriers to movement of people and goods, the ties between Jordan and the Palestinian territories are still strong, and can be expected to grow stronger with the removal of the prevailing restrictions. The Jordanian capital market is relatively free, and is originally tied with Palestinian capital. As we mentioned in section four above, efforts to revive the financial sector in the West Bank and Gaza Strip were dominated by initiatives taken by Jordanian financiers, and Palestinian financiers residing in

Jordan. In addition, the majority of the immediate Palestinian returnees to the West Bank will be Palestinians residing now in Jordan and have property and family ties in the West Bank.

Taking into account all these factors together, it looks more reasonable that the Palestinian territories and Jordan constitute an optimal currency area and that they could therefore form a currency union. Accordingly, the PMA could embark at the present on initiating efforts in two directions at the same time. First, establishing a Palestinian currency as the only legal tender to be used after the passage of the transition period. Second, negotiating with the Central Bank of Jordan all the aspects of monetary union. At a later stage, and within the context of possible future developments, the PMA may be able to carry out its functions as the Central Bank of Palestine, or to merge with the Central Bank of Jordan into one supranational Central Bank carrying out the functions of the central bank for both Jordan and the Palestinian territories in the West bank and Gaza Strip.

5.2.3. The Trade Sector

Of equal urgency, and parallel to reforming the public finance and monetary sectors, is the need to reorient, revive, and strengthen the trade sector, which, as we have seen in section three above, currently suffers a weak and deteriorating situation as a consequence of the long years of occupation. Sustainable economic development cannot be obtained unless the economy substitutes, gradually, goods for labour services as the main export and source of foreign exchange. Therefore, the success in adjusting the current trade patterns and imbalances, and directing the economy towards a viable external payments position should be considered as crucial tasks of the PNA's development efforts. However, substantial changes in the trade sector will take time due to the fact that adjusting trends in trade can not be separated from those in production, investment, and employment because there is always a strong link between these trends, especially in small economies. Therefore, it may be misleading to talk about an optimal trade regime such as free trade, customs union, etc., for the Palestinian economy in the near future.

In the Palestinian context, reforming external trade patterns has to follow a sequence of stages reflecting the degree to which the economy will successfully overcome the harmful effects of the Israeli policies operated in the past 27 years, increase the capacity of productive sectors, and re-establish entry into neighbouring markets and access to new ones. These tasks can not be completed during the interim period which is insufficient to carry out such a comprehensive transformation of production and trade structures. Furthermore, the Paris Protocol on economic relations between Israel and Palestine limits the possibilities for alternative changes in the trade regime in the interim period. As we have seen in section four above, the trade arrangement with Israel presents obstacles to negotiating a suitable trade arrangement between the Palestinians and other neighbour countries in the interim period specified by the Protocol. In addition, a number of non-tariff barriers that constrained exports of Palestinian products in the past still exist.

At present, however, the priority areas of action could be in certain prerequisites activities which are essential for a smoothly operating future trade sector. These include: first, rebuilding the physical infrastructure of the economy to create the supportive systems of trade activities; of high priority in this respect, is the transportation and communication systems; second, building a direct outlet to the world, so that the Palestinian economy can easily and independently trade with other countries, accordingly, the establishment of shipping services and the development of a commercial sea port in Gaza constitute a priority area of action; third, establishing specialised trade institutions to provide information, technical expertise and general guidance to producers of agricultural and industrial products.

All these tasks should be considered as prerequisite activities to be undertaken in the interim period for the next major task in the near future, which is establishing trade relations with markets of neighbouring countries. In this connection, the Protocol does have some positive elements that should be made use of in the interim period and afterwards. The Protocol allows for a limited opening to the markets of Jordan and Egypt and granting the Palestinians the right to set their own tariff on a list of "development goods" imported from these countries. This should enable the importation of capital and intermediate goods at a lower cost, which in turn reduces the cost of reconstruction and other development efforts in the interim period. This should also enable the acquisition of preferential treatment for some Palestinian exports to these countries (e.g., the economic agreement between Palestine and Jordan calls for the gradual removal of all barriers to trade between Jordan and the Palestinian territories).

This chance of opening neighbouring markets should be aggressively followed up, as the first step towards the independence of the trade sector from the Israeli economy and the reintegration of the Palestinian economy into the region. This should also be coupled in the short run, after the passage of the interim period, with efforts to exploit new markets that have accorded

Palestine a preferential treatment, like the European Union, Japan, Turkey and others. Finally, the relaxation of restrictions imposed on trade flows are expected to improve the situation. In this context, some studies have predicted a promising outlook in the interim period and afterwards. For example, M. El-Jafari (1997) applied two quantitative methods in his study to assess the potential merchandise trade flows between the Palestinian Territories and other countries in the region. The results of the study indicate that removing non-tariff barriers imposed by Israel will double merchandise exports, based on 1992 statistics, and consequently, the merchandise trade deficit will be narrowed by 30%. Moreover, under unrestricted trade conditions, the merchandise trade deficit will be at a minimum of $663 million compared to $940.2 million in 1992. More important, the study indicates that these potentials will result from trade creation with other countries and trade diversion with Israel. Thus, countries like Jordan, Iraq, Saudi Arabia, Lebanon, and Japan are expected to be the major outlets for Palestinian merchandise exports, where more than 90% of Palestinian exports could be directed to these markets. On the other hand, more than 75% of merchandise imports are expected to originate from Egypt, Syria, Lebanon, USA, Japan, Korea, Indonesia and the European Union (see El-Jafari, M., 1997).

6. SUMMARY AND CONCLUSIONS

The period immediately following the 1967 Israeli occupation of the Palestinian territories of the West Bank and Gaza Strip was characterised by high rates of economic growth in these territories. However, this growth was not sustained because of the radical structural changes brought about in the economy of these territories due to the Israeli restrictive economic measures and policies. Measures were taken by the Israeli authorities to integrate, gradually, the economy of these territories into that of Israel. An increasingly elaborate system of Israeli military orders and administrative arrangements have prevented the Palestinian people in the OPTs from determining in their territories the working of their political, economic and judicial systems, use of their natural resources, provision of public services, and, consequently, the course of their economic development. The lack of appropriate national institutions to safeguard the interest of the local economy through various policy instruments has further led to the increasing subservience of the OPTs' economy to the economy of the occupying authorities. Since then, the economy of the OPTs in general became tightly linked with that of Israel.

It has been obvious that the paradox of the Israeli occupation policies in the OPTs has been to push up per capita income while arresting any attempt to sustainable national economic development. By being tied to the Israeli economy, incomes in the West Bank and Gaza Strip were higher than those in neighbouring Arab countries although living conditions are among the poorest in the region. As a result, the level of the domestic output and its contribution to GNP have been steadily falling in the later years while labour has become increasingly dependent on employment in Israel and the rest of the world. The closure of banks and other financial institutions, since the occupation, has deprived the productive sectors of the economy from short-term and long-term sources of finance. In the area of trade, the Palestinian territories have been gradually transformed into a substantial importer of Israeli merchandise with a growing balance of trade deficit that can only be met from workers' remittances and transfers from abroad.

When the PNA began to exercise its functions in May 1994, following the Israeli-Palestinian Peace Accord of September 1993, the economic situation in the West Bank and Gaza Strip was characterised by a high degree of fragmentation and imbalances reflecting distortions in the structure of output and income, a significant gap between domestic and national output caused by high dependence upon external sources of income, sectoral imbalances coupled with a virtual paralysis of the public sector, low productive investment and uncontrollable and unfavourable flows of trade and labour. Moreover, although the start of self-rule in the West Bank and Gaza Strip has been universally welcomed, the overlap between the Israeli occupation authorities and the PNA has presented new political, economic and bureaucratic obstacles.

In the years ahead, the PNA will be trying to revive an economy riddled with distortions and structural imbalances and plagued by unemployment and under-investment. A mix of political and economic obstacles lies ahead as the PNA tries to put together a formula for future development in the West Bank and Gaza Strip. However, the task will not be easy given the uncertainty over the future political status of these territories and their present heavy dependence on Israel for trade and employment. The task of rebuilding the deteriorating infrastructure of the West Bank and Gaza Strip will not be easy. The $2400 million in international aid for the first five years gave some indication of the scale of the work ahead. Until it can raise its own revenues, the PNA will have to rely on external budgetary support. Although the PNA started recently to raise its own revenues through taxation and transfers from Israel, the economic downturn since the Israeli closures of the Palestinian territories borders has left it reliant on funds from the international community. Therefore, the donors' funds which mostly aimed at development projects in the short run will have to be diverted to fund the current expenditure of the PNA.

The PNA cannot rely on international aid alone. In this regard, it should be understood that despite the great expectations that have surrounded the donor effort, it was never going to build the Palestinian economy. Due to the uncertainty surrounding the future of the peace process, donors might find conditions too difficult to continue their support. They are looking for specific movement in both the political and economic spheres over the near future. To keep the donor funds coming in the territories there has to be political progress as well as economic development. Therefore, for independent Palestinian economic development, the key issue should not be the donors, but to create jobs and a degree of autonomy from the economies of Israel through seeking more productive local and foreign investments and expanding the regional trade. There is an urgent need to encourage and bring back Palestinian investors with their funds from outside to invest in the West Bank and Gaza Strip. However, turning their funds into a steady flow will be tough until the situation in these territories offer more attractive alternative investment prospects.

As outlined throughout the above section of this paper, the reconstruction of the Palestinian economy to facilitate the achievement of sustainable growth and development requires the successful completion of a set of bold development strategic policies and measures. These include: building of infrastructures and provision of public services; creating support systems conducive to investment, production and trade activities; removing of constraints on private business activities; the effective use of the external aid available from the international community; intensifying investment in development projects and raising exports; substantial expansion of the productive capacity of the economy and restraint on increases in consumption and imports. However, it will be hard for the PNA to achieve any development success without a major transformation effort of restructuring and reforming public finances, banking and other financial institutions, and reviving the trade flows and activities. In the Palestinian context, the whole reconstruction efforts cannot be carried out successfully without creating sound fiscal, financial, and trade systems.

Through such conscious policies and commitments, coupled with concrete measures at various levels, the economy of the Palestinian territories might be expected to move out of stagnation and set itself on a course of sustained growth and development. Indeed, the success of such strategies equally necessitates the creation and development of indigenous bodies capable of managing the economy and charting its future course.

In conclusion, the following major points may be made:

First, the economic and social underdevelopment of the OPTs is directly the result of policies and military orders issued by the Israeli occupation forces over the period of almost three decades. This has been repeatedly verified by the United Nations and its various organisations. Without a substantial reversal of many of these policies, any efforts to introduce or to stimulate economic or social development will inevitably have only marginal effects.

Second, and related to the point made above, economic and social development in the OPTs is, to a large extent, dependent upon improved political stability and the restoration of political, civil and human rights to the Palestinians living there. Without such rights and with the continuing of the restrictions and obstructions imposed by Israel on the OPTs' economic and social activities, the Palestinians in these territories can have little hope of real improvements in their quality of life, and will continue to oppose the Israeli occupation.

Third, the nature of the future economic development in Palestine will depend to a large extent on the political conditions prevailing in the area as a whole, which in turn will depend on the outcome of the peace negotiations and the final settlement between Israel and the Palestinians.

Fourth, sustainable development, and any improvements in regional peace and stability, can only take place within the context of the Palestinians being willing and given the chance of independent political and economic partnership with Israel and any other country in the region, not under the present conditions of enforced and asymmetrical integration.

Fifth, given the complex political realities, and the track record of the peace process so far, it is hard to envision a resolution of the overall conflict in the area, including the Palestinian-Israeli one. Accordingly, it is not realistic to expect a new economic order in the area in the near future. However, this political uncertainty should make it more urgent for the Palestinians to define clearly a perspective of their long-run interest, and follow its path without being influenced by the short-run conditions.

Sixth, despite the relatively gloomy picture of the future, the Palestinian economy in the West Bank and Gaza Strip has considerable potentials for economic development given the high quality of the human resources, the negligible external debt, the very small public sector (administration only), the tourism potential, and the proximity to the much larger and fast-growing economies of Jordan and Israel.

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Appendix-1a
Occupied Palestinian Territories (West Bank & Gaza Strip)
Selected Key Indicators of Economic Performance
Population & Labour Force (000s)

Years	Population	Labour Force	Employed	In OPTs	In Israel	% of Labour Force	Unemployed	Unemployment Rate(%)
1968	940	146.5	126.4	126.4	-	-	20.1	13.7
1970	978	180.8	173.3	152.8	20.5	11.3	7.5	4.1
1972	1021	192.0	189.6	126.6	63.0	32.8	2.4	1.3
1974	1084	213.0	211.0	146.1	64.9	30.4	2.0	1.0
1976	1121	207.0	205.2	138.9	66.3	32.0	1.8	0.8
1978	1171	214.0	212.3	138.2	74.1	34.6	1.7	0.8
1980	1181	218.5	215.7	140.6	75.1	34.4	2.8	1.3
1982	1227	225.2	222.9	143.8	79.1	35.1	2.3	1.0
1984	1303	248.0	241.3	151.0	90.3	36.4	6.7	2.7
1986	1383	267.3	259.4	164.7	94.7	35.4	7.9	3.0
1988	1483	289.4	281.9	172.5	109.4	37.8	7.5	2.6
1990	1599	307.8	296.5	188.9	107.6	35.0	11.3	3.6
1991	1681	312.1	287.4	189.7	97.7	31.3	24.7	7.9
1992	1768	334.0	319.9	204.9	115.0	34.4	14.1	4.2
1993	1801	338.2	315.6	235.6	80.0	23.6	22.6	6.6
1994	2238	400.1	338.9	285.9	53.0	13.2	61.2	15.3
1995	2267	416.4	319.3	294.3	25.0	6.0	97.1	23.3
1996	2357	432.6	302.9	284.9	18.0	4.1	129.7	30.0

Sources: (1) Palestinian Central Bureau of Statistics (PCBS) 1994, *Demography of the Palestinian Population in the West Bank and Gaza Strip,* Current Status Report series, No. 1, Rammallah-West Bank, December 1994. (2) Palestinian Central Bureau of Statistics (PCBS) 1995, *Labour Force Statistics in the West Bank and Gaza Strip,* Current Status Report series, No. 3, Rammallah-West Bank, May 1995. (3) The World Bank 1993, *Developing the Occupied Territories: An Investment in Peace,*Washington D.C., September 1993.

Note: Until 1993, the data of all the above sources have been based on Israeli statistics, mainly, *Statistical Abstract of Israel*, and *Judea, Samaria and Gaza Area Statistics* (Jerusalem, Central Bureau of Statistics, various years and volumes).

Appendix-1b
Occupied Palestinian Territories (West Bank & Gaza Strip)
Selected Key Indicators of Economic Performance
National Accounts Indicators (current million $)

Years	GDP	Agriclt. (%)	Indst. (%)	Const. (%)	Servs. (%)	NFI (*)	GNP	GDP/ GNP (%)	NFI/ GNP (%)	PC GDP ($)	PC GNP ($)
1968	131	35.2	5.4	6.2	53.2	3	134	97.7	2.2	139	143
1970	198	33.7	6.9	9.4	50.0	10	208	95.2	4.8	251	213
1972	267	37.6	7.1	12.1	43.2	60	327	81.6	18.3	266	320
1974	543	38.5	8.2	13.7	43.4	205	748	72.5	27.4	501	690
1976	692	31.4	7.9	17.3	43.4	207	899	76.9	23.0	617	802
1978	835	29.4	8.2	16.9	45.5	336	1171	71.3	28.6	713	1000
1980	1050	29.8	7.1	15.5	47.6	375	1425	73.6	26.3	889	1207
1982	1086	27.6	6.7	16.1	49.6	375	1461	74.3	25.6	885	1191
1984	1115	24.4	7.2	15.5	52.9	548	1663	67.0	32.9	856	1276
1986	1494	29.5	8.4	15.3	46.8	488	1982	75.3	24.6	1080	1433
1988	1653	39.9	8.3	13.0	38.8	693	2346	70.4	29.5	1115	1582
1990	2247	38.2	8.0	12.0	41.8	698	2946	76.2	23.6	1405	1842
1991	2161	31.4	8.0	13.0	47.6	648	2809	76.9	23.0	1286	1671
1992	2673	37.3	7.7	13.8	41.2	816	3489	76.6	23.0	1511	1973
1993	2593	27.3	7.8	21.6	43.3	532	3125	82.8	17.0	1440	1735
1994	2624	26.9	9.2	14.5	49.4	386	3010	87.2	12.8	1172	1345
1995	2482	21.5	10.8	13.9	53.8	248	2730	90.9	9.1	1095	1204
1996	2442	23.9	10.8	12.2	53.1	204	2646	92.2	7.7	1036	1123

Sources: (1) The World Bank 1993, *Developing the Occupied Territories: An Investment in Peace*, Washington D.C., September 1993. (2) Palestinian Central Bureau of Statistics (PCBS) 1995, *Economic Statistics in the West Bank and Gaza Strip,* Current Status Report Series, No. 2, Ramallah-West Bank, January 1995. (3) The Economist Intelligence Unit (EIU) 1997, *Country Profile 1997-98: Israel-The Occupied Territories.*

Notes: (1) Until 1993, the data of all the above sources have been based on the Israeli statistics, mainly: *Statistical Abstract of Israel*, and *Judea, Samaria and Gaza Area Statistics* (Jerusalem, Central Bureau of Statistics, various years and volumes). (2) All figures originally expressed in Israeli currency (shekel) have been converted into $US using the annual average exchange rates from IMF, *International Financial Statistics, Yearbook 1997* (Washington D.C., IMF, 1997), pp. 482-85.

(*) NFI: Net Factor Income; mainly earnings of Palestinian workers in Israel.

Appendix-1c
Occupied Palestinian Territories (West Bank & Gaza Strip)
Selected Key Indicators of Economic Performance
External Trade Indicators: Balance of Payments (million $)

Years	Exports of Goods	Imports of Goods	Trade Balance	Exports of Services*	Imports of Services	Balance	Net Transfer Payments	Current Account
1968	35.5	69.9	-34.4	-	-	-	-	-
1970	57.5	127.8	-70.3	42.6	29.8	12.8	91.5	34.0
1972	87.6	167.8	-80.2	111.1	49.4	61.7	54.3	35.9
1974	155.8	333.0	-177.2	193.8	98.4	95.4	30.2	-51.6
1976	232.4	434.3	-201.9	236.2	125.6	110.6	92.6	1.3
1978	266.6	459.0	-192.4	257.1	136.3	120.8	91.0	19.4
1980	353.5	679.4	-325.9	403.4	214.4	189.0	111.0	-25.9
1982	398.5	734.3	-335.8	491.4	233.3	258.1	106.6	28.5
1984	306.7	690.3	-383.6	518.9	230.1	288.8	89.7	-5.1
1986	387.4	891.5	-504.1	567.3	273.4	293.9	76.9	-133.3
1988	209.0	676.0	-467.0	742.0	329.0	413.0	135.3	62.0
1990	231.0	843.0	-612.0	844.0	362.0	482.0	154.2	20.0
1991	248.0	1148.0	-900	794.0	352.0	442.0	156.5	-307.0
1992	299.0	1232.0	-933.0	898.0	349.0	549.0	235.0	-149.0
1993	236.0	1138.0	-902.0	552.0	186.0	366.0	296.0	-240.0
1994	227.0	1024.0	-798.0	386.0	133.0	253.0	393.0	-152.0
1995	373.0	1660.0	-1287.0	248.0	148.0	100.0	614.0	-574.0
1996	316.0	1495.0	-1179.0	204.0	153.0	51.0	421.0	-708.0

Sources: (1) The World Bank 1993, *Developing the Occupied Territories: An Investment in Peace*, Washington, D.C., September 1993. (2) The Economist Intelligence Unit (EIU) 1997, *Country Profile 1997-98: Israel-The Occupied Territories*. (3) UNCTAD, *Main Features of Domestic and External Merchandise Trade of the West Bank and Gaza Strip*, UNCTAD/ECDC/SEU/5. UN, New York, 1994.

Note: Until 1993, the data of all the above sources have been based on the Israeli statistics, mainly: *Statistical Abstract of Israel*, and *Judea, Samaria and Gaza Area Statistics* (Jerusalem, Central Bureau of Statistics, various years and volumes).

(*) Including Net Factor Income; mainly earnings of Palestinian workers in Israel.

Appendix-1d
Occupied Palestinian Territories (West Bank & Gaza Strip)
Selected Key Indicators of Economic Performance
External Trade Indicators: Merchandise Trade by Destination (million $)

	Trade with Israel			Trade with Jordan			Trade with Other Countries		
Years	Exports	Imports	Balance	Exports	Imports	Balance	Exports	Imports	Balance
1968	15.3	53.5	-38.2	15.5	5.2	10.3	4.7	11.2	-6.5
1970	20.9	83.2	-62.3	17.2	3.7	13.5	7.1	12.6	-5.5
1972	40.8	138.3	-97.5	28.8	4.6	24.2	13.9	19.9	-6.0
1974	98.4	287.6	-189.2	35.6	4.9	30.7	12.9	29.8	-16.9
1976	143.2	391.9	-248.7	67.7	3.8	63.9	16.4	38.2	-21.8
1978	157.8	403.8	-246.0	95.3	5.0	90.3	10.0	47.0	-37.0
1980	226.4	582.4	-356.0	107.3	5.5	101.8	11.5	76.7	-65.2
1982	258.5	648.4	-389.9	125.0	8.9	116.1	7.1	71.6	-64.5
1984	185.3	619.9	-434.6	98.4	8.2	90.2	5.3	58.1	-52.8
1986	274.6	797.8	-523.2	102.1	10.9	91.2	3.1	81.3	-78.2
1988	148.0	596.0	-448.0	52.4	9.5	42.9	2.3	69.1	-66.8
1990	181.0	709.2	-193.4	32.2	9.3	22.9	8.6	118.7	-110.1
1991	189.9	976.4	-255.2	38.5	9.2	29.3	9.5	134.2	-124.7
1992	248.8	1103.6	-854.8	37.5	9.5	28.0	5.1	117.5	-112.4
					Trade with the Rest of the World				
					Exports		Imports		Balance
1993	178.0	1015.0	-837.0		56.0		158.0		-120.0
1994	205.0	920.0	-715.0		38.0		155.0		-117.0
1995	306.0	1520.0	-1214.0		20.0		170.0		-150.0
1996	235.0	1550.0	-1315.0		31.0		175.0		-144.0

Sources: (1) The World Bank 1993, *Developing the Occupied Territories: An Investment in Peace*, Washington, D.C., September 1993. (2) The Economist Intelligence Unit (EIU) 1997, *Country Profile 1997-98: Israel-The Occupied Territories*. (3) UNCTAD, *Main Features of Domestic and External Merchandise Trade of the West Bank and Gaza Strip,* UNCTAD/ECDC/SEU/5. UN, New York, 1994.

Note: Until 1993, the data of all the above sources have been based on the Israeli statistics, mainly: *Statistical Abstract of Israel*, and *Judea, Samaria and Gaza Area Statistics*, (Jerusalem, Central Bureau of Statistics, various years and volumes).

Appendix-1e
Occupied Palestinian Territories (West Bank & Gaza Strip)
Selected Key Indicators of Economic Performance
Inflation Rates (average annual change in CPI) &
Exchange Rates (NIS/US $)*

Years	West Bank	Gaza Strip	Israel	Exchange Rate (NIS/US $)
1968	-	-	-	0.00035
1970	16.1	21.9	12.0	0.00035
1972	17.6	19.5	12.9	0.00041
1974	42.6	54.7	39.7	0.00044
1976	28.1	22.3	31.3	0.00079
1978	50.4	42.8	50.6	0.0017
1980	139.4	156.0	131.0	0.0051
1982	107.4	114.6	120.3	0.02
1984	360.3	373.0	373.8	0.29
1986	50.0	49.6	48.1	1.48
1988	8.7	11.1	16.3	1.59
1990	13.0	16.9	17.2	2.01
1991	11.5	7.0	19.0	2.27
1992	13.9	14.1	12.2	2.47
	West Bank and Gaza Strip			
1993	11.0		11.1	2.83
1994	14.0		12.5	3.01
1995	11.1		9.2	3.01
1996	10.5		11.2	3.19

Sources: (1) The World Bank 1993, *Developing the Occupied Territories: An Investment in Peace*, Washington, D.C., September 1993. (2) The Economist Intelligence Unit (EIU) 1997, *Country Profile 1997-98: Israel-The Occupied Territories*. (3) IMF, *International Financial Statistics, Yearbook 1997* (Washington D.C., IMF, 1997),

Note: Until 1993, the data of all the above sources have been based on the Israeli statistics, mainly: *Statistical Abstract of Israel*, and *Judea, Samaria and Gaza Area Statistics*, (Jerusalem, Central Bureau of Statistics, various years and volumes).

(*) Average of the period; NIS: Newly Israeli shekel.

Appendix-2

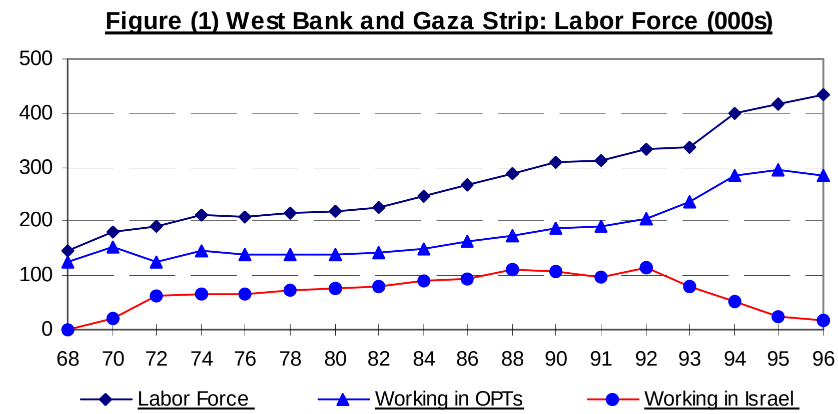


Figure (1) West Bank and Gaza Strip: Labor Force (000s)
500
400
300
200
100
0
68 70 72 74 76 78 80 82 84 86 88 90 91 92 93 94 95 96
Labor Force
Working in OPTs
Working in Israel

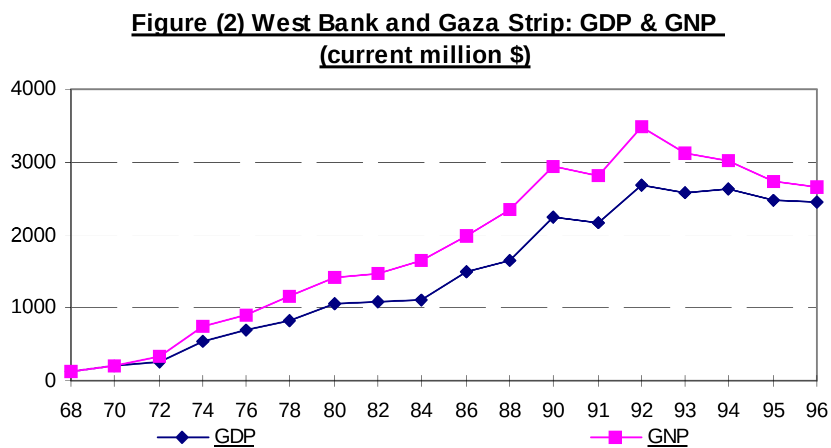


Figure (2) West Bank and Gaza Strip: GDP & GNP (current million $)
4000
3000
2000
1000
0
68 70 72 74 76 78 80 82 84 86 88 90 91 92 93 94 95 96
GDP
GNP

Figure (3) West Bank and Gaza Strip: PC GDP & PC GNP ($)

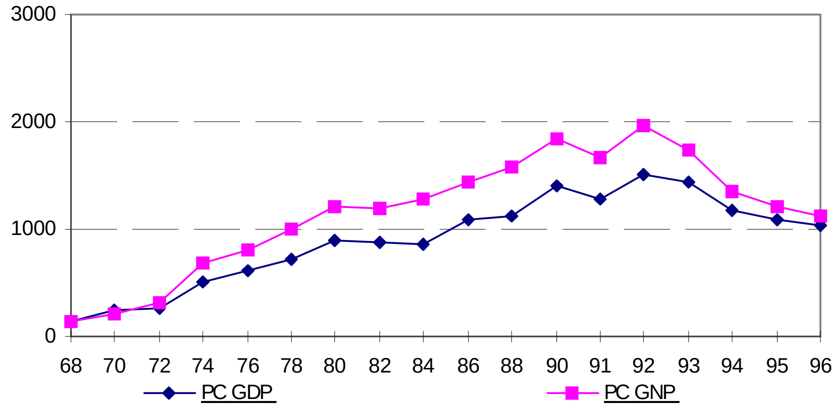


Figure (4) West Bank and Gaza Strip: Export of Merchandise by Destination (million $)

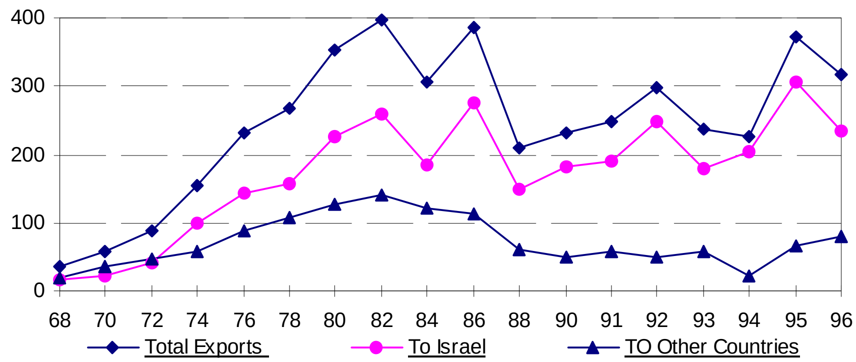


Figure (5) West Bank and Gaza Strip: Imports of Merchandise by Origin (million $)

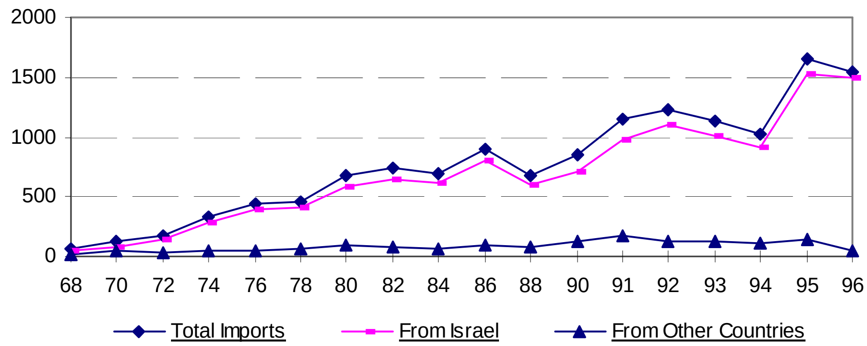
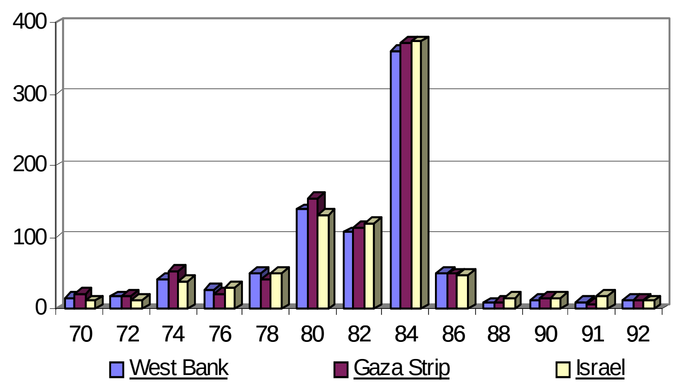


Figure (6) West Bank, Gaza Strip and Israel: Inflation Rates (Average Annual Change in CPI)



Appendix-3a
West Bank and Gaza Strip: Central Government Finances
(million US $)

	1993	1994	1995	1996	1997
Revenue	279	269	511	684	816
Current Expenditure	258	334	578	780	866
Current Balance	21	-65	-67	-96	-50
Capital Expenditure	26	45	189	160	n/a
Overall Balance	-104	-110	-256	-305	n/a
(Incl external funding)					
% of GDP	-4.0	-3.6	-8.0	-7.8	n/a

Sources: The Economist Intelligence Unit (EIU) 1997, *Country Profile 1997-98: Israel-The Occupied Territories;* Palestinian and Israeli authorities; IMF staff estimates and projections; World Bank estimates.

Appendix-3b
West Bank and Gaza Strip: Donor Assistance
(million US $)

Donor	1995		1996		1997	
	Commit-ments	Disbur-sements	Commit-ments	Disbur-sements	Commit-ments	Disbur-sements
Arab Fund (AFSED)	10.0	0.00	70.16	2.47	39.09	0.00
Canada	4.68	4.68	11.91	10.44	10.39	3.84
Denmark	15.71	15.71	10.42	10.42	9.90	12.65
Egypt	0.03	0.00	1.85	0.18	10.00	10.00
EU	95.35	73.21	106.84	99.41	61.36	21.06
France	18.65	9.36	20.75	8.90	19.93	2.87
Germany	29.43	16.42	36.32	34.71	47.37	27.63
IFC	0.00	0.00	7.50	0.00	46.50	3.80
Israel	4.00	4.00	0.00	0.00	14.50	0.00
Italy	18.10	9.50	32.83	7.48	14.57	20.63
Japan	82.92	74.92	76.92	71.42	24.24	4.23
Netherlands	53.33	16.73	68.99	55.80	18.37	0.53
Norway	35.07	35.08	49.28	46.89	38.95	33.93
Saudi Arabia	65.00	7.50	20.00	20.00	20.00	51.70
Spain	21.46	20.56	15.68	6.50	20.71	2.81
Sweden	9.94	2.45	28.37	29.03	23.39	2.48
Switzerland	17.98	14.71	13.64	18.19	18.52	15.41
UK	4.74	5.60	14.63	12.89	15.71	3.74
US	89.64	59.70	94.65	71.82	29.97	68.56
World Bank	20.00	22.17	85.00	26.90	68.50	33.47
Total (Incl others)	636.21	428.09	894.35	537.49	593.17	334.52

Sources: The Economist Intelligence Unit (EIU) 1997, *Country Profile 1997-98: Israel-The Occupied Territories;* Palestinian Authorities; Ministry of Planning and International Cooperation, November 1997.

Appendix-3c
West Bank and Gaza Strip: Central Government Finances
(million US $)

	1996 Budget	1996 Actual	1997 Budget
Total Revenue	**555**	**684**	**816**
Domestic revenue	137	179	210
Income Tax	n/a	52	65
VAT	n/a	66	77
Customs duties	n/a	23	20
Property	n/a	1	-
Excises	n/a	37	47
Revenue clearance	347	420	484
Customs duties	n/a	86	139
VAT	n/a	217	211
Petroleum excise	n/a	100	116
Income tax	n/a	4	4
Health fees	n/a	6	8
Other	n/a	6	6
Non-tax revenues	71	86	122
Transportation fees	n/a	23	30
Health insurance fees	n/a	13	13
Health fees	n/a	9	10
Other	n/a	41	69
Total Expenditure	**902**	**989**	**1732**
Current Expenditure	629	780	866
Civilian salaries	250	247	296
Police salaries	147	157	199
Other	232	377	371
Foreign-Financed Employment Prog.	n/a	49	9.0
Capital Expenditure	273	160	866
Balance	**-347**	**-305**	**866**
Total Financing	273	293	n/a

Sources: The Economist Intelligence Unit (EIU) 1997, *Country Profile 1997-98: Israel-The Occupied Territories;* Palestinian Authorities; IMF staff estimates.

Notes: (1) These statistics are unreliable and include discrepancies. (2) The 1996 budget was revised during the year to take into account the effect of the closure.